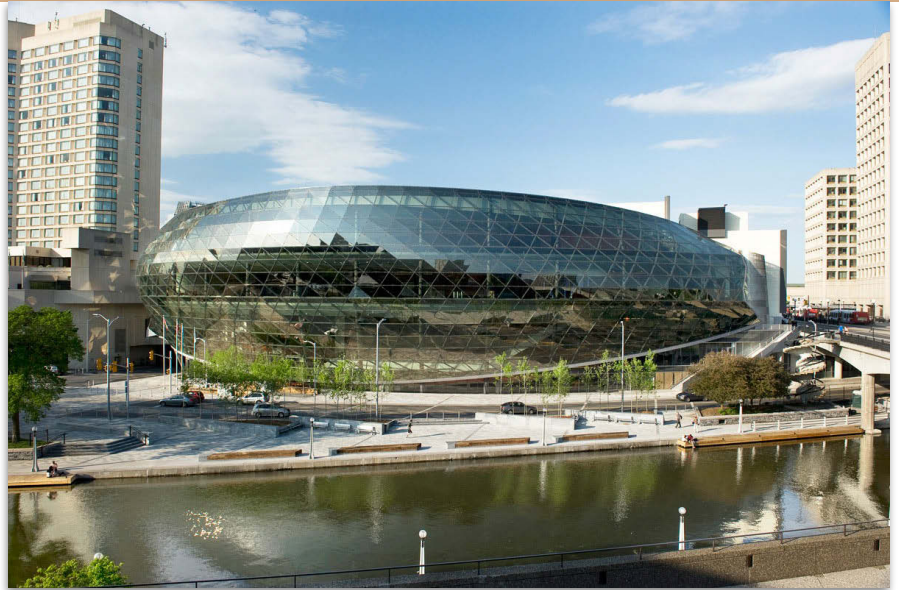


**Annual Conference  
Ottawa Convention  
Centre, Canada  
Sept 12-14, 2014**



**Plenary  
Lecture  
Anil  
Shivdasani**

Wachovia  
Distinguished  
Professor of Finance,  
Kenan-Flagler  
Business School,  
University of North  
Carolina



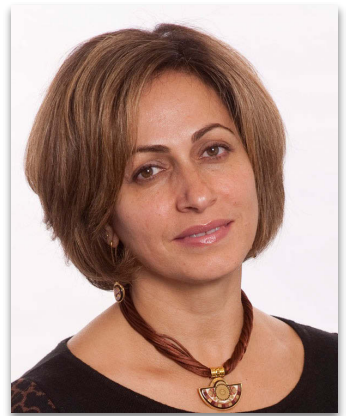
**Program  
Chair  
Gordon  
Sick**

Professor of Finance,  
Haskayne  
School of Business,  
University of Calgary



**PhD  
Program  
Wayne  
Ferson**

Ivadelle & Theodore  
Johnson Chair in  
Banking & Finance,  
Marshall  
School of Business,  
University of  
Southern California



**PhD  
Program  
Nadia  
Massoud**

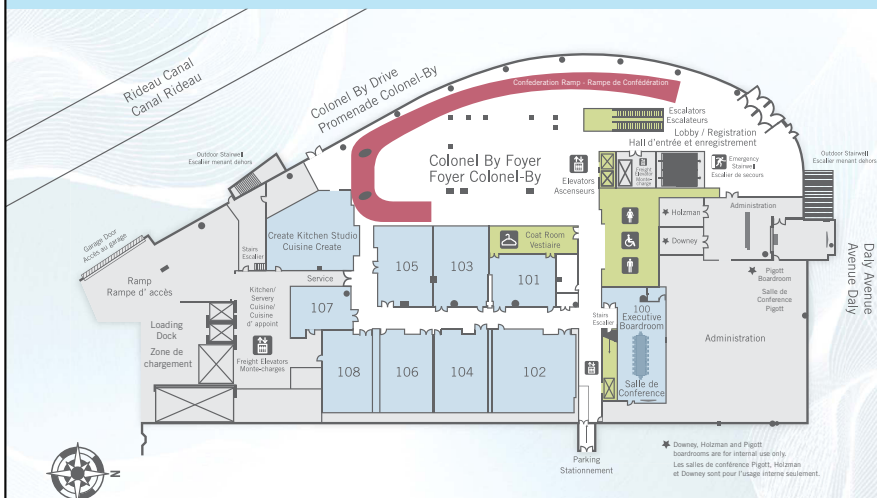
Ian Potter Chair  
Professor of Finance  
Melbourne Business  
School,  
Australia

## Colonel By Foyer

- Registration  
Except at special times, as noted below
- Breakfast  
Saturday, Sunday 7-8 am
- Breaks  
Friday 3-3:30 pm  
Saturday, Sunday 9:30 - 10 am  
Saturday 3:30 - 4 pm
- Exhibits

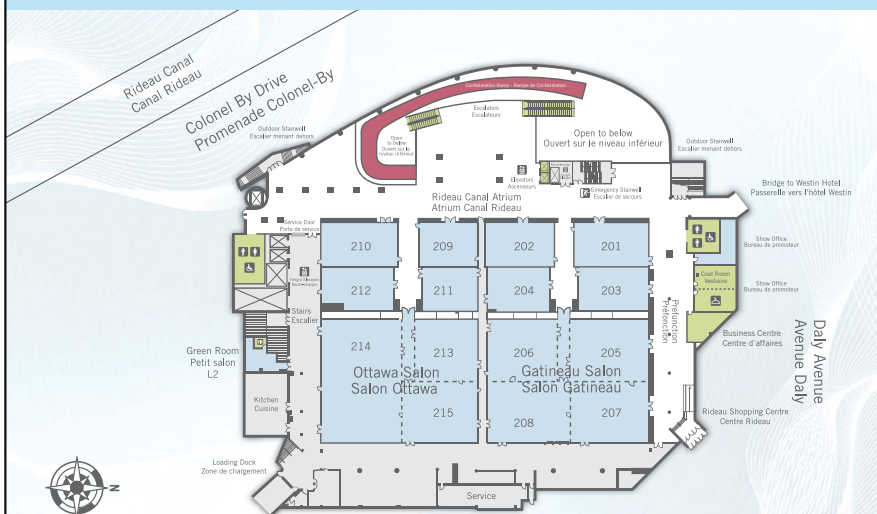
## Rooms 101-108

- Parallel Sessions  
Friday 1 - 3 pm, 3:30 - 5:30 pm  
Saturday, Sunday 8 - 9:30 am,  
10 - 11:30pm  
Saturday 1:30 - 3:30 pm



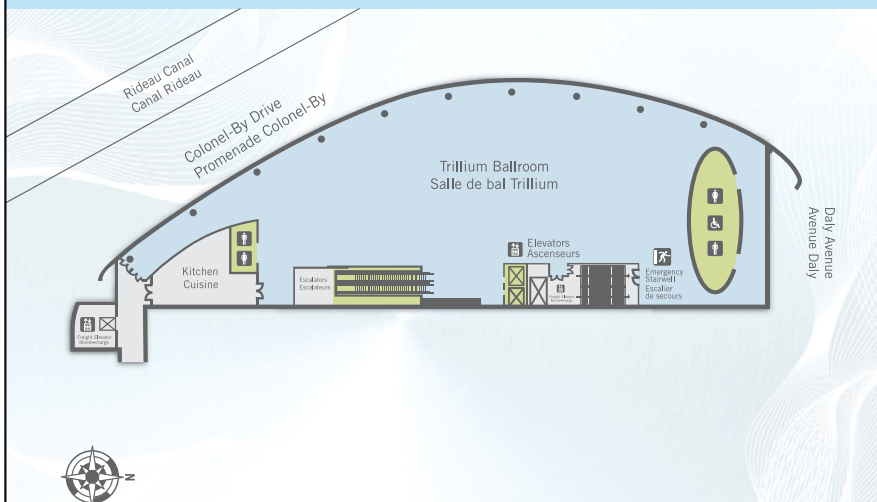
## Room 214

- Lunch & AGM  
Saturday 11:45 am - 1:15 pm
- Plenary Lecture  
Saturday 4 - 5:30 pm
- Registration  
During the Lunch and Plenary Lecture



## Trillium Ballroom

- Reception  
Friday 5:30 - 8 pm
- Dinner  
Saturday 6 - 9:30 pm
- Registration  
During the Reception and Dinner



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## Welcome and Notes from the Program Chair

Welcome to Ottawa and the Northern Finance Association Annual Conference for 2014.

This is the 26<sup>th</sup> Annual NFA Conference, but the first to be run under our recently incorporated Association, rather than under the wing of a sponsoring university. For the first time since the first NFA Conference in 1989, the NFA returns to Ottawa.

We have a broad international presence: the papers come in equal amounts from 3 geographies: Canada, the US, and the Rest of the World. We received a record 503 paper submissions and accepted only 119 for the Main Program and a further 20 for the PhD program.

We have had the lowest acceptance rate ever: under 24% for the main program, and still under 28%, including the PhD program.

Only one paper was withdrawn from each program, which is a new low that signals the desire of authors to come to the NFA conference, because of the high quality of the conference and our new low registration fees. We are also on track to set a new attendance record, which will likely be in the range of 250 to 300 attendees.

We have been able to roll back registration fees, mainly because of three features:

- When we incorporated, we raised capital by donations from 15 business schools and sold over 50 Inaugural Memberships (see page 44 of this program). We are using this capital to absorb risk, which allows us to remove the risk premium from the conference fee.
- We have increased the number of sponsors and exhibitors for the 2014 conference, which generates substantial income to subsidize fees. See pages 40-43 for more details on these organizations. The inside back cover of the program lists our paper awards. Although awards don't provide income to the NFA, they enhance the attraction of the NFA and they often come from our sponsors and exhibitors.
- We have substituted a significant amount of volunteer work to replace salaries paid by prior conferences.

Thus, thanks go to our Inaugural NFA Board that incorporated the NFA and developed our capital campaign. This Board continued to be the current NFA Board (although our Vice President Issouf Soumaré stepped down to leave way for Stéphane Chrétien, and Ranjini Jha joined as Treasurer for the current year). Our current Board and next year's Board are listed on page 39 of this program.

Thanks go to Mark Kamstra for steering our drive for conference sponsors, exhibitors and organizations that give paper awards.

Several other Board Members took on tasks that could have been done by paid staff. Brian Smith helped me to visit and select the Ottawa Convention Centre as our conference site. He also shared a lot of the Treasurer functions with

Ranjini Jha, so that I could be confident that bills were being paid on time, and fees were going into the bank.

This year, I, as Program Chair, implemented a system of selecting Discussants and Program Chairs who were not presenting papers, in order to maximize conference participation. This meant that the Program Chair had to coordinate the process, rather than delegating it to Session Chairs. I used a large database of people who have participated in the NFA in recent years for this. When I asked the Board if they had any suggestions, Lisa Kramer jumped into this project and wore out the bearings on her Rolodex. She brought in people who weren't in my database, which has helped to broaden our list of NFA contacts. Lisa also has handled record-keeping and filing duties as Secretary of the NFA, which is a big help.

Many other people helped to put this Conference together. Page 39 lists the 143 Paper Reviewers, who generated over 1325 reviews to help me select papers for the program.

I am also grateful to the authors who submitted papers for consideration, as well as the Session Chairs and Discussants who are making this a very active conference.

I am grateful to Anil Shivdasani for agreeing to be our first NFA Plenary Speaker. He will provide a more useful and comprehensive talk than is typical for a brief keynote speech.

Wayne Ferson and Nadia Massoud kindly agreed to help us build a PhD program that is more useful for PhD students than in the past.

We also are receiving a lot of help from:

- Sharon Provost (U of Alberta ) for running the Wild Apricot conference registration system.
- Barbara Merlihan (U of Calgary) for helping with administrative tasks. Barbara is our only employee.
- Karen Lovett (Ottawa Convention Centre) has provided a great deal of help with meal planning and venue optimization.
- Carmel Sick for help with registration.
- Tor-Erik Bakke for volunteering to do photography and videography of the Plenary Address.

Thanks to all of the above people and organizations for their assistance.

Gordon Sick  
NFA 2014 Program Chair  
Professor of Finance, University of Calgary



Friday, 12 September 2014

13:00-15:00

PhD Program: Attendance is open to anyone who has registered for the Conference	
Room 103	Room 105
<b>Volatility and Microstructure</b> <i>Chair:</i> Wayne Ferson <i>Slow Price Adjustment to Public News in After-Hours Trading</i> Jiasun Li <i>Discussant:</i> Julien Cuijean <i>Empirical Test of the Liquidity-Based Theory of Closed-End Funds</i> Jerry Parwada; Kenny Siaw <i>Discussant:</i> Stéphane Chrétien <i>Inventory Risk, Market-Maker Wealth, and the Variance Risk Premium</i> Mathieu Fournier <i>Discussant:</i> Masahiro Watanabe <i>Correlated Demand and Excess Comovement of Exchange-Traded Fund Returns</i> Markus Broman <i>Discussant:</i> Akiko Watanabe	<b>Institutions</b> <i>Chair:</i> Nadia Massoud <i>Banking and Shadow Banking</i> Ji Huang <i>Discussant:</i> Eric Stephens <i>Does A Firm's Bond IPO Have Implications For The Degree Of Monitoring By Private Lenders?</i> Tashfeen Hussain <i>Discussant:</i> Michael King <i>Institutional Trading around Material Information Announcements</i> Vivek Sharma; Lei Gao; Pankaj Jain <i>Discussant:</i> Mehdi Beyhaghi <i>The Effects of Government Intervention in Financial Market on the Real Economy</i> Jinfai Sheng <i>Discussant:</i> George Georgopoulos <i>Why Are Bad Loans Securitized? The Impact of Shareholder Rights in the Banking Industry</i> Jing Zhang <i>Discussant:</i> Anthony Saunders

15:00-15:30

**Refreshment Break** (Colonel By Foyer)

15:30-17:30

PhD Program: Attendance is open to anyone who has registered for the Conference	
Room 103	Room 105
<b>Asset Pricing and Agency</b> <i>Chair:</i> Wayne Ferson <i>Continuous-Time Principal-Agent Problem with Drift and Stochastic Volatility Control: With Applications to Delegated Portfolio Management</i> Raymond C. W. Leung <i>Discussant:</i> David Feldman <i>Mutual Fund Intermediation, Equity Issues, and the Real Economy</i> Bill Yiqing Zu <i>Discussant:</i> Sergey Isaenko <i>Oil Prices and Core Inflation</i> Haibo Jiang <i>Discussant:</i> Antonio Diez de los Rios <i>Stock Return Comovement and the Business Cycle</i> Lu Zhang <i>Discussant:</i> Nikolay Gospodinov <i>Pricing in Auction Markets for Alternative Assets: Theory and Experimental Evidence</i> Matthew Boland; Daniel Thornton <i>Discussant:</i> Pauline Shum	<b>Corporate Finance</b> <i>Chair:</i> Nadia Massoud <i>Corporate Defined Benefit Pension Plans And Chapter 11 Bankruptcy</i> Milka Dimitrova <i>Discussant:</i> Alan Huang <i>Firm-Manager Match and Executive Compensation</i> Jing Pan; Lei Ma <i>Discussant:</i> Keke Song <i>Loss-induced Trades of Insurance Companies</i> Michael Liu <i>Discussant:</i> Lynnette Purda <i>Optimal Disclosure as a Trade-off between Capital and Product Market Considerations: Theory and Evidence</i> Jianqu Bai; Yun Ling <i>Discussant:</i> Archishman Chakraborty <i>Superstar CEOs and Innovation</i> Keun Jae Park <i>Discussant:</i> Jonathan Witmer
<b>Reception</b> (Trillium Ballroom)	

17:30-20:00

# Saturday, 13 September 2014

7:00-8:00

8:00-9:30

## Breakfast (Sponsored by Eventus) (Colonel By Foyer)

### Main Program

Room 101	Room 103	Room 104	Room 105	Room 106	Room 107	Room 108
<b>Systemic Risk and Crises</b> <i>Chair:</i> Giovanni Barone Adesi <i>Disclosed Derivatives Use, Securitization, And The Systemic Equity Risk Of Banks</i> Gregor Weiss; Rouven Trapp <i>Discussant:</i> Alfred Lehar <i>Investment Waves under Cross Learning</i> Shiyang Huang; Yao Zeng <i>Discussant:</i> Matthieu Bouvard <i>Risk Taking and Low Longer-Term Interest Rates: Evidence from the U.S. Syndicated Loan Market</i> Seung Jung Lee; Sirio Aramonte; Viktors Stebunovs <i>Discussant:</i> Thomas Gilbert, University of Washington & University of British Columbia	<b>Governance and Disclosure</b> <i>Chair:</i> David Stangeland <i>Voluntary Disclosure and Market Competition: Theory and Evidence from The U.S. Service Sector</i> Nathan Dong; Eda Orhun <i>Discussant:</i> Jiro Kondo <i>CEO Job Security and Risk-Taking</i> Peter Cziraki; Moqi Xu <i>Discussant:</i> David Koslowsky <i>Managerial Compensation, Regulation And Risk In Banks: Theory And Evidence From The Financial Crisis</i> Tommaso Oliviero; Vittoria Cerasi <i>Discussant:</i> Shastri Sandy	<b>Institutions</b> <i>Chair:</i> Bryan Campbell <i>A Better Measure of Institutional Informed Trading</i> Hui Guo; Buhui Qiu <i>Discussant:</i> Kenneth Vetzal <i>Banking Competition and Stability: The Role of Leverage</i> Xavier Freixas; Kebin Ma <i>Discussant:</i> Katarzyna Sum <i>Credit Risk Determinants of Insurance Companies</i> Liliana Gonzalez; Lorenzo Naranjo <i>Discussant:</i> Madhu Kalimpalli	<b>Behavioural Finance</b> <i>Chair:</i> Kai Li <i>CEO Appearance</i> Douglas Cook; Shawn Mobbs <i>Discussant:</i> Amos Nadler <i>Information Asymmetry, Information Content, And Underreaction To Earnings Announcements</i> Kee H. Chung; Oliver Kim; Steve C. Lim; Sean Yang <i>Discussant:</i> David Ng <i>Contagious Negative Sentiment and Corporate Policies: Evidence from Local Bankruptcy Filings</i> Jawad Addoum; Alok Kumar; Nhan Le <i>Discussant:</i> Kai Li	<b>International and Arbitrage</b> <i>Chair:</i> George Georgopoulos <i>A wake-up call theory of contagion</i> Toni Ahnert; Christoph Bertsch <i>Discussant:</i> Denis Gorea <i>Out-of-Sample Evidence on the Returns to Currency Trading</i> David Chambers; Olivier Accominotti <i>Discussant:</i> Marie-Claude Beaulieu <i>The Impact Of Arbitrage On Market Liquidity</i> Dominik Rosch <i>Discussant:</i> Piet Sercu	<b>Mergers and Acquisitions</b> <i>Chair:</i> Ash Hossain <i>Fear, Feedback and Disclosure: Governance Role of Negative Media Coverage in M&amp;A Decisions</i> Shantanu Dutta; Kose John; Samir Saadi; Pengcheng Zhu <i>Discussant:</i> Olivier Dessaint <i>Strategic Acquisitions by Corporate Venture Capital Investors</i> Lora Dimitrova <i>Discussant:</i> Chen Liu <i>Why Do Some Target Firms Choose to Seek a Second Fairness Opinion in Mergers and Acquisitions?</i> Tingting Liu <i>Discussant:</i> Sandra Betton	<b>Microstructure</b> <i>Chair:</i> Jason Smith <i>What Makes the S&amp;P 500 Jump?</i> Marcel Prokopczuk; Chardin Wese Simen <i>Discussant:</i> Dominik Rosch <i>Liquidity Supply Across Multiple Trading Venues</i> Laurence Lescourret; Sophie Moinas <i>Discussant:</i> Elena Pikulina <i>Debt Maturity and the Liquidity of Secondary Debt Markets</i> Max Bruche; Anatoli Segura <i>Discussant:</i> Nathalie Moyen

9:30-10:00

## Refreshment Break (Colonel By Foyer)

10:00-11:30

Main Program						
Room 101	Room 103	Room 104	Room 105	Room 106	Room 107	
<b>Equity Valuation</b> <i>Chair:</i> Adlai Fisher <i>The Idiosyncratic Volatility-Expected Return Relation: Reconciling the Conflicting Evidence</i> Doron Avramov; Scott Cederburg <i>Discussant:</i> Grant Wang <i>Spurious Inference in Unidentified Asset-Pricing Models</i> Nikolay Gospodinov; Raymond Kan; Cesare Robotti <i>Discussant:</i> Alan Huang <i>Small Growth and Distress Anomalies: Two Sides of the Same Coin?</i> Kyung Shim; Harjoat Bhamra <i>Discussant:</i> Adlai Fisher	<b>Governance</b> <i>Chair:</i> Vikas Mehrotra <i>Are Entrepreneurs Special? Evidence from Board Appointments</i> Olubunmi Faleye; Wilson Kung; Jerry Parwada; Gloria Y Tian <i>Discussant:</i> Tu Nguyen <i>Do Rating Agencies Act as Third-Party Monitors? Evidence from Moody's Credit Watches</i> Hamdi Driss; Gordon Roberts; Nadia Massoud <i>Discussant:</i> Amir Barnea <i>Creditor Control through Loan-to-Loan and Loan-to-Own</i> Kai Li; Wei Wang <i>Discussant:</i> Vikas Mehrotra	<b>Institutions</b> <i>Chair:</i> John Murray <i>A Market-Based Funding Liquidity Measure</i> Zhuo Chen; Andrea Lu <i>Discussant:</i> Scott Hendry <i>Subjective or Objective? Nonparametric Estimation Of Misreporting and Misassessment in Corporate Credit Rating</i> Ruichang Lu; Yao Luo; Ruli Xiao <i>Discussant:</i> Martin Boyer <i>Tipsters and Tippees: Brokers' Pre-release of Price-Sensitive Information to their VIP Clients</i> Tamara Nefedova <i>Discussant:</i> Ranjini Jha	<b>Capital Structure</b> <i>Chair:</i> Ashraf Zaman <i>Protection of Trade Secrets and Capital Structure Decisions</i> Sandy Klasa; Hernan Ortiz-Molina; Matthew A. Serfling; Shweta Srinivasan <i>Discussant:</i> Nilanjan Basu <i>Loan Covenant Violation and Corporate Liquidity Management</i> Yijia Zhao <i>Discussant:</i> Ing-Haw Cheng <i>Credit Default Swaps and Corporate Cash Holdings</i> Marti Subrahmanyam; Dragon Tang; Sarah Wang <i>Discussant:</i> Ashraf Zaman	<b>Derivatives</b> <i>Chair:</i> Ivan Sergienko <i>Non-Transferable Non-Hedgeable Executive Stock Options Pricing</i> David Colwell; David Feldman; Wei Hu <i>Discussant:</i> Gordon Sick <i>Volatility-of-Volatility Risk</i> Darien Huang; Ivan Shaliastovich <i>Discussant:</i> Bo Young Chang <i>Slow Diffusion of Information and Price Momentum in Stocks: Evidence from Options Markets</i> Zhuo Chen; Andrea Lu <i>Discussant:</i> Chayawat Ornthanalai	<b>Flexibility and Investment</b> <i>Chair:</i> Ron Giammarino <i>Idiosyncratic Risk and the Manager</i> Brent Glover; Oliver Levine <i>Discussant:</i> Wei Wei <i>Real Options And The Option To Withdraw: Evidence From Open Market Share Repurchases</i> Mark Mietzner <i>Discussant:</i> Brian Smith <i>The Value in Waiting to Issue Debt</i> Babak Lotfaliei <i>Discussant:</i> Yuanshun Li	<b>Microstructure</b> <i>Chair:</i> Gbenga Ibikunle <i>High Frequency Trading with Speed Hierarchies</i> Wei Li <i>Discussant:</i> Archisman Chakraborty <i>Asymmetric Information and Inventory Concerns in Over-the-Counter Markets</i> Julien Cuijean; Remy Praz <i>Discussant:</i> Maria Pacurar <i>Information Percolation, Momentum, and Reversal</i> Daniel Andrei; Julien Cuijean <i>Discussant:</i> Aditya Kaul

11:45-13:15

## Luncheon, NFA Annual General Meeting and Awards

### Luncheon (Sponsored by Bank of Canada) and NFA Annual General Meeting (Room 214)

*Chair:* Stéphane Chrétien, NFA President and Université Laval  
The NFA Annual General Meeting will take place at the Luncheon.

Agenda:

- Election of Directors
- Appointment of Accountants
- Best Paper Awards
- Announcement of NFA 2015 Conference

Saturday, 13 September 2014

13:30-15:30

Main Program						
Room 101	Room 103	Room 104	Room 105	Room 106	Room 107	
<b>Macro Asset Pricing</b> <i>Chair:</i> Michael Brennan <i>Slow Capital Movement and Risk Premium Puzzle</i> Sergey Isenko <i>Discussant:</i> Amir Akbari <i>Heterogeneous Agents and Long Horizon Features of Asset Prices</i> Blake LeBaron <i>Discussant:</i> Chris Hrdlicka <i>Price Dynamics and Market Selection in Small and Large Economies</i> Filippo Massari <i>Discussant:</i> Emilio Osambela <i>Stock Market Ambiguity and the Equity Premium</i> Panayiotis Andreou; Anastasios Kagkadiis; Paulo Maio; Dennis Philip <i>Discussant:</i> Masahiro Watanabe <i>Model Disagreement and Economic Outlook</i> Daniel Andrei; Bruce Carlin; Michael Hasler <i>Discussant:</i> Ali Lazrak	<b>Governance</b> <i>Chair:</i> Martin Boyer <i>Influence of Public Opinion on Investor Voting and Proxy Advisors</i> Reena Aggarwal; Isil Erel; Laura Starks <i>Discussant:</i> Florian Muenkel <i>Investment Horizons and Information</i> Ker Shen Huang; Alex Petkevich <i>Discussant:</i> Kee-Hong Bae <i>Lawyers in the Executive Suite: Gatekeepers as Internal Governance</i> Adair Morse; Wei Wang; Serena Shuo Wu <i>Discussant:</i> Fred Bereskin <i>Powerful Independent Directors</i> Kathy Fogel; Liping Ma; Randall Morek <i>Discussant:</i> Martin Boyer	<b>Institutions</b> <i>Chair:</i> Allen Goss <i>A Mechanism for LIBOR</i> Brian Coulter; Joel Shapiro <i>Discussant:</i> Daniel Bergstresser <i>Being Local or Going Global? Competition and Entry Barriers in the Canadian Banking Industry</i> Hector Perez Saiz; Hongyu Xiao <i>Discussant:</i> Mehdi Beyhagi <i>Capital Market Consequences of Index Membership</i> Charles Cao; Matthew Gustafson; Raisa Velthuis <i>Discussant:</i> Tor-Erik Bakke <i>The Impact of Non-Traditional Activities on Risk, Performance and Capital of Canadian Banks Under Regulatory Changes</i> Jean-Pierre Gueyrie; Alaa Guidara; Van Son Lai; Issouf Soumaré <i>Discussant:</i> Yuriy Zabolotnyuk <i>The Interbank Network Across The Great Financial Crisis: Evidence From Italy</i> Alberto Franco Pozzolo; Massimiliano Affinito <i>Discussant:</i> Ben Craig	<b>Payout Policy</b> <i>Chair:</i> Martin Boileau, University of Colorado <i>Does Change in Hoarding Prices Influence Corporate Payout Policy?</i> Sara Ding; Kose John; Yang Ni; Samir Saadi <i>Discussant:</i> Chris Mitchell <i>Leverage Boundaries, Financial Flexibility and Dividends</i> Alan Douglas <i>Discussant:</i> Sean Cleary, Queen's <i>Positive Asymmetry and Systematic Propensity to Save</i> Alexander Vadiyev <i>Discussant:</i> Abdul Rahman Khokhar, St Mary's University <i>The Real Effects of Share Repurchases</i> Heitor Almeida; Vyacheslav Fos; Mathias Kronlund <i>Discussant:</i> Pablo Moran <i>Predictable Corporate Distributions and Stock Returns</i> Feng Zhang; Hank Bessembinder <i>Discussant:</i> Susan Christoffersen	<b>International Credit Risk</b> <i>Chair:</i> Usha Mittoo <i>Do Foreign Listings in the U.S. Affect U.S. Firms?</i> Yan Wang; Sergei Sarkissian <i>Discussant:</i> Arnold Cowan <i>Financial Liberalization and Innovation</i> Fariborz Moshirian; Xuan Tian; Zhengyuan Wang; Bohui Zhang <i>Discussant:</i> Pat Akey <i>Lemons and Proud of it: Information Asymmetry and Risk Transfer Markets</i> Eric Stephens; James Thompson <i>Discussant:</i> Jun Yang <i>Sovereign Credit Risk and Government Effectiveness</i> Alexandre Jeanneret; Jean-Claude Cosset <i>Discussant:</i> Rémy Lambinet	<b>IPOs, SEOs and Investment Banking</b> <i>Chair:</i> Imants Paeglis <i>Do IPO Underwriters Collude?</i> Fangjian Fu; Evgeny Lyandres <i>Discussant:</i> Zheng Liu <i>Underwriter Competition in Canadian Accelerated Seasoned Equity Offerings</i> Erdal Gunay; Nancy Ursel <i>Discussant:</i> Evan Dudley <i>Investment Bank Deal Pipeline and the Pricing of IPOs</i> Kevin Boehl; Craig Dunbar <i>Discussant:</i> Parianen Veeren <i>Crowd Sourcing in Capital Formation: An Empirical Investigation</i> Emma Li; J. Spencer Martin <i>Discussant:</i> Aazam Virani <i>Does Overpricing to Avert IPO Withdrawal Pay? An Empirical Analysis</i> Walid Busaba; Zheng Liu <i>Discussant:</i> Imants Paeglis	<b>Investment Funds</b> <i>Chair:</i> David Downie, RBC Capital Markets <i>An ETF Premium Puzzle and a Market Segmentation Explanation</i> Louis Piccotti <i>Discussant:</i> Pauline Shum <i>Dynamic Performance of Canadian Fixed Income Mutual Funds</i> Mohamed Ayadi; Skander Lazrak; Yusui Liao; Robert Welch <i>Discussant:</i> Saurin Patel <i>Endogenous Credit Constraints and Household Portfolio Choices</i> Kyoung Jin Choi; Hyeng Keun Koo; Byung Hwa Lim; Jane Yoo <i>Discussant:</i> Michael Brennan <i>Management of Flow Risk in Mutual Funds</i> Martin Rohleder; Dominik Schulte; Marco Wilkens <i>Discussant:</i> Timothy Simin <i>Mutual Fund Competition, Managerial Skill, and Alpha Persistence</i> Gerard Hoberg; Nitin Kumar; Nagpurnanand Prabhala <i>Discussant:</i> Fabio Moneta

15:30-16:00 Refreshment Break (Colonel By Foyer)

16:00-17:30

## First Annual NFA Plenary Lecture

### Plenary Lecture (Room 214)

*Chair:* Gordon Sick  
Anil Shivdasani, Wachovia Distinguished Professor of Finance at the Kenan-Flagler Business School, University of North Carolina  
Anil will present the NFA 2014 Plenary Lecture on Corporate Governance.

18:00-21:30

## NFA Banquet

**Dinner (Sponsored by Scotiabank) (Trillium Ballroom)**



# Sunday, 14 September 2014

7:00-8:00

8:00-9:30

## Breakfast (Colonel By Foyer)

Main Program						
Room 101	Room 103	Room 104	Room 105	Room 106	Room 107	Room 108
<b>Equity Valuation</b> <i>Chair: William Rentz</i> <i>Aggregation of Information About the Cross Section of Stock Returns: A Latent Variable Approach</i> Nathaniel Light; Denys Maslov; Oleg Rytchkov <i>Discussant: Bruno Feunou</i> <i>Investment and the Term Structure of Stock Returns</i> Sandra Mortal; Michael Schill <i>Discussant: Fatma Saryal</i> <i>Conditioning Information and Asset Pricing</i> <i>Anomalies in Multivariate Tests of Financial Integration</i> Marie-Claude Beaulieu; Marie-Hélène Gagnon; Lynda Khalaf <i>Discussant: William Rentz</i>	<b>Governance</b> <i>Chair: Wendy Rotenberg</i> <i>A Theory of Family Firms</i> Jin Yu; Palve Radicevic <i>Discussant: Melissa Toffanin</i> <i>The Differences between Public and Private Firms: Agency, Financing and Technology</i> Nan Xiong <i>Discussant: Iraj Fooladi</i> <i>Who Captures the Power of the Pen?</i> Jiaxing You; Bohui Zhang; Le Zhang <i>Discussant: Paul Calluzzo</i> <i>Spillover Effects from US Class Action Lawsuits: Evidence from Foreign Firms</i> <i>Cross-listed in the US</i> Yi Ding; Louis Gagnon; Xiaoqiao Wang <i>Discussant: Wendy Rotenberg</i>	<b>Empirical Issues</b> <i>Chair: Ilias Tsiakas</i> <i>Do Options Volatility Skew and Spread Really Predict Stock Returns?</i> Jason Wei <i>Discussant: Maksim Isakin</i> <i>Maximum Likelihood Estimation of the Equity Premium</i> Efsthathios Avdis; Jessica Wachter <i>Discussant: Alex Maynard</i> <i>Does Realized Skewness Predict the Cross-Section of Equity Returns?</i> Diego Amaya; Peter Christoffersen; Kris Jacobs; Aurelio Vasquez <i>Discussant: Ilias Tsiakas</i>	<b>Behavioural Finance</b> <i>Chair: Alli Nathan</i> <i>Mutual Fund Window Dressing: Prevalence, Flow Reaction, and Limited Attention</i> Xiaolu Wang <i>Discussant: Lisa Kramer</i> <i>Peer Pressure: Does Social Interaction Explain the Disposition Effect?</i> Rawley Heimer <i>Discussant: Andreanne Tremblay Simard</i> <i>The Blame Game</i> Dexin Zhou <i>Discussant: Stéphane Chrétien</i>	<b>Energy Derivatives</b> <i>Chair: Kenneth Vetzal</i> <i>Macroeconomic Drivers of Crude Oil Futures Risk Premia</i> Ron Alquist; Gregory H. Bauer; Antonio Diez de los Rios <i>Discussant: Gabriel Power</i> <i>Short-Term Hedging For An Electricity Retailer</i> Debbie Dupuis; Genevieve Gauthier; Frederic Godin <i>Discussant: Perry Sadorsky</i> <i>The Price of Oil Risk</i> Steven Baker; Bryan Routledge <i>Discussant: Alexander David</i>	<b>Capital Structure and Debt</b> <i>Chair: Laurence Booth</i> <i>Common Factors in Corporate Capital Structure</i> Murray Frank; Tao Shen <i>Discussant: Redouane Elkamhi</i> <i>Financing as a Supply Chain: The Capital Structure of Banks and Borrowers</i> Will Gornall; Ilya Strebulaev <i>Discussant: Egor Marveyev</i> <i>Reputation and Loan Contract Terms: the Role of Principal Customers</i> Ling Cen; Sudipto Dasgupta; Redouane Elkamhi; Raunaq Pungaliya <i>Discussant: Einar Kjenstad</i>	<b>Microstructure</b> <i>Chair: Akiko Watanabe</i> <i>Dynamic Dispersed Information and the Credit Spread Puzzle</i> Elias Albagli; Christian Hellwig; Aleh Tsyvinski <i>Discussant: Murray Carlson</i> <i>High Frequency Trading, Price Efficiency, and the Cost of Immediacy: Evidence from the 2008 Short Sale Ban</i> Jonathan Brogaard; Terrence Hendershott; Ryan Riordan <i>Discussant: Andriy Shkilko</i> <i>Comparing Trade Flow Classification Algorithms in the Electronic Era: the Good, the Bad, and the Uninformative</i> Marios Panayides; Thomas Shohfi; Jared Smith <i>Discussant: Akiko Watanabe</i>

9:30-10:00

## Refreshment Break (Colonel By Foyer)

Sunday, 14 September 2014

10:00-11:30

Main Program

Room 101	Room 103	Room 104	Room 105	Room 106	Room 107	Room 108
<b>Equity Valuation</b> <i>Chair:</i> Carlton Osakwe <i>Asset Pricing and the 1%</i> Alexis Akira Toda; Kieran Walsh <i>Discussant:</i> Gregory H. Bauer <i>Perceived Crash Risk and Cross-Sectional Stock Returns</i> George P Gao; Zhaogang Song; Liyan Yang <i>Discussant:</i> Mark Potter <i>Is Idiosyncratic Volatility Risk Priced? Evidence from the Physical and Risk-Neutral Distributions</i> Ali Boloorforoosh <i>Discussant:</i> Carlton Osakwe	<b>Governance</b> <i>Chair:</i> Lynnette Purda <i>Institutional Investment Horizon, the Information Environment and Firm Credit Risk</i> Lorne Switzer; Jun Wang <i>Discussant:</i> Mohammad Rahaman <i>The effect of monitoring on CEO pay practices in a matching equilibrium</i> Pierre Chaigneau; Nicolas Sahuguet <i>Discussant:</i> Alexander Dyck <i>Director Network and IPO Performance</i> Yi Feng; Keke Song; Yisong Tian <i>Discussant:</i> Lynnette Purda	<b>Institutions</b> <i>Chair:</i> Kent Womack <i>Do Analysts' Preferences Affect Corporate Policies?</i> Francois Degeorge; Francois Derrien; Ambrus Kecskes; Sebastian Michenaud <i>Discussant:</i> Mohamed Al Guindy <i>Investor Attrition and Mergers in Mutual Funds</i> Susan Christoffersen; Haoyu Xu <i>Discussant:</i> Laleh Samarbakhsh <i>Roller Risk and the Maturity Transformation Function of Banks</i> Teodora Paligorova; Joao Santos <i>Discussant:</i> Michael King	<b>Behavioural Finance</b> <i>Chair:</i> Lisa Kramer <i>Informational Herding by Institutional Investors: Evidence from Analyst Recommendations</i> Jonathan Clarke; Chayawat Ornthanalai; Ya Tang <i>Discussant:</i> Anna Scherbina <i>Stock Market Overreaction to Management Earnings Forecasts</i> Jean-Sebastien Michel <i>Discussant:</i> Mark Kamstra <i>The Social Dynamics of Performance</i> Julien Cujean <i>Discussant:</i> Chi Liao	<b>Derivatives</b> <i>Chair:</i> Don Cyr <i>Measuring Uncertainty in Monetary Policy Using Implied Volatility and Realized Volatility</i> Bo Young Chang; Bruno Feunou <i>Discussant:</i> Alexander David <i>The Term Structure of CDS Spreads and Sovereign Credit Risk</i> Patrick Augustin <i>Discussant:</i> Mathieu Fournier <i>What We Can Learn From Pricing 139,879 Individual Stock Options</i> Lars Stentoft <i>Discussant:</i> Phelim Boyle	<b>Fixed Income</b> <i>Chair:</i> Alexandra MacKay <i>Search-For-Yield In Canadian Fixed-Income Mutual Funds</i> Sermin Gungor; Jesus Sierra <i>Discussant:</i> Narat Charupat <i>Impact of Sponsor Ownership on Fixed-income Fund Performance</i> Mohamed Ayadi; Lawrence Kryzanowski; Mahmood Mohebshahedin <i>Discussant:</i> Stephen Szaura <i>Bond Risk Premia and Structure Models</i> Bruno Feunou; Jean-Sebastien Fontaine <i>Discussant:</i> Jia Shen	<b>Microstructure</b> <i>Chair:</i> Tom McCurdy <i>Catching Fire: An Anatomy of Information Diffusion using Retweets</i> Mao Ye; Zhi Da; Nitesh Chawla; Jian Xu <i>Discussant:</i> Xiaozhou Zhou <i>Liquidity-Adjusted Intraday Value At Risk Modeling And Risk Management: An Application To Data From Deutsche Börse</i> Georges Dionne; Maria Pacurar; Xiao Zhou <i>Discussant:</i> Bidisha Chakrabarty <i>The Dynamics of Trading in Commodity Futures</i> Aditya Kaul; Lorenzo Naranjo; Carmen Stefanescu <i>Discussant:</i> Xuhui (Nick) Pan

12:00-14:00

Meeting of Incoming and Outgoing NFA Boards (Jim Durrell Boardroom)

*Chair:* Gordon Sick, NFA

This is a closed meeting for the New and Old NFA Board Members.

# NFA 2014 Program Abstracts

## Friday, September 12, 2014

### 1:00 PM – 3:00 PM

#### Volatility and Microstructure (Room 103)

**Session Chair: Wayne Ferson, University of Southern California**

*Slow Price Adjustment to Public News in After-Hours Trading*  
Jiasun Li, University of California Los Angeles, United States

*Discussant:* Julien Cujean, University of Maryland

Recent years see a growing trend among firms to publish corporate events away from regular trading hours. In specific, as almost all firms now announce quarterly earnings in after-hours, after-hours trading has become indispensable for studying how stock prices incorporate new market information (a central theme of finance research). This paper closely examines the after-hours price discovery process in response to firm earnings releases. While quoted bid/ask prices adjust almost immediately, actual traded prices adjustments take hours. From 2002 to 2012, such slow price adjustment creates 5,881 rule-based intra-day trading opportunities, with an average return of 1.53% within 4 hours. After cost (assessed by a real trading experiment), a marginal investor who properly exploits the slow price adjustment beat the market by 11.5% per year. Under Regulation National Market System (Reg NMS), I find intensive use of intermarket sweep orders (ISO), while non-ISO orders slow down price adjustment. My results provide direct implications for academia, practitioners, and regulators.

*Empirical Test of the Liquidity-Based Theory of Closed-End Funds*

Jerry Parwada, The University of New South Wales, Australia  
Kenny Siaw, The University of New South Wales, Australia

*Discussant:* Stéphane Chrétien, Université Laval

Theory argues that the rationale for the existence of closed-end funds (CEFs) is that they provide investors indirect exposure to their underlying illiquid assets without the high cost associated with trading them directly. Consistent with this reasoning, we show that risk-averse investors invest in CEFs to diversify their portfolios into the illiquid markets in which CEFs specialize. Moreover, investor demand for CEFs is a positive function of the CEF portfolio's illiquidity level. A direct comparison of CEF holdings with those of CEF investors reveals that the latter underweight stocks invested by CEFs, which are typically small and illiquid. Such impacts of liquidity on investment behavior also vary across investor identities, depending on the level of fiduciary responsibility, investment horizon, and investment style. Beyond the CEF industry, our findings shed new insights on the benefits of the closed-end structure observed in other market segments.

*Inventory Risk, Market-Maker Wealth, and the Variance Risk Premium*

Mathieu Fournier, Rotman School of Management, Canada

*Discussant:* Masahiro Watanabe, University of Alberta

I examine how inventory risk and market-maker wealth jointly determine the value of index options through their effects on the variance risk premium. My analysis demonstrates that part of the variance risk premium compensates option market-makers for their exposure to market variance. I find that the amount of inventory exposure to market variance, and recent profits and losses of delta-hedged inventory predict the variance risk premium. Based on these findings, I develop a theoretical model in which market variance is stochastic and the representative market-maker accumulates inventory over time by absorbing end-users' net demand for index options. Starting from the market-maker's optimal trading strategy, I derive an explicit formula linking the variance risk premium to inventory risk and market-maker wealth. Finally, I estimate a parsimonious version of the theoretical model in which option market-makers' inventory risk is explicitly modeled and influences the price of S&P 500 index options.

*Correlated Demand and Excess Comovement of Exchange-Traded Fund Returns*

Markus Broman, York University, Schulich School of Business, Canada

*Discussant:* Akiko Watanabe, University of Alberta School of Business

Exchange-Traded Funds (ETFs) offer a unique setting to examine whether return comovements are excessive because the fundamentals of the ETF and its underlying portfolio (NAV) are the same. Controlling for systematic risk, I find strong evidence of excessive return comovements among ETFs grouped by style (size, value/growth) and liquidity characteristics over daily, weekly and monthly horizons. Similar comovement patterns are found in the abnormal trading activity of ETFs. Moreover, the amount of comovement in returns is positively associated with both the degree of commonality in abnormal trading activity and the level of ETF liquidity relative to its underlying portfolio. These results agree with a clientele based story where investors with shorter holding periods and correlated demand self-select into ETFs due to their high perceived liquidity.

#### Institutions (Room 105)

**Session Chair: Nadia Massoud, Melbourne Business School**

*Banking and Shadow Banking*

Ji Huang, Princeton University, United States

*Discussant:* Eric Stephens, Carleton University

Does stringent financial regulation always lower financial instability? No, it does not when shadow banking plays a role. To provide a general answer to the question, this paper incorporates shadow banking modeled as off-balance sheet financing into a standard continuous-time macro-finance model. Our modeling of off-balance sheet financing captures both its regulatory arbitrage motive and also the enforceability problem with its use of implicit guarantees for the arbitrage purpose. We show that the enforceability problem gives rise to an en-

ogenous leverage constraint for shadow banking. In addition, we show that shadow banking is pro-cyclical and that shadow banking adds to financial instability due to the interplay of its pro-cyclicality, its regulatory arbitrage motive, and its asset fire sale to regular banks in downturns. Based on these preliminary results, we show that financial instability as a function of financial regulation is U-shaped instead of monotonically decreasing as the conventional view predicts.

*Does A Firm's Bond IPO Have Implications For The Degree Of Monitoring By Private Lenders?*

Tashfeen Hussain, Queens University, Canada

*Discussant:* Michael King, Ivey Business School at Western University

In this paper, I investigate whether a firm's undertaking a bond IPO influences the monitoring of the private loans granted to the firm by private lenders. Specifically, I test the hypothesis that the private lenders' degree of monitoring of private loans changes after a firm undertakes a bond IPO. The agency relationships and the leverage of a firm are transformed significantly as a result of a firm accessing the public debt market for the first time. Hence, there exists the potential for a change in the extent of monitoring of private loans by the private lenders after a firm undertakes a bond IPO. Using a sample of nearly 23,000 private loans granted to about 5,500 non-financial U.S firms over the 1991-2010 period, I find that private lenders increase the degree of monitoring of loans that they extend to a firm after it issues a bond IPO. In addition, by employing a robust two stage Model, I find that private lenders stiffens the monitoring of private loans that they grant to a firm if they anticipate that the firm will access the public debt market. These findings are robust to loan and firm characteristics, and bond market conditions. The evidence suggests that private lenders get concerned about the potential increase of agency problems and leverage as a result of a firm accessing the public debt market, and consequently, find it valuable to increase the degree of monitoring of loans that they extend to the firm.

*Institutional Trading around Material Information Announcements*

Vivek Sharma, University of Memphis, United States

Lei Gao, University of Memphis, United States

*Discussant:* Mehdi Beyhaghi, University of Texas at San Antonio

Trading by institutional investors has always been under scrutiny, both by regulators as well as academics. Several academic studies show that institutional investors are taking advantage of their connections and use private information hence acquired to trade profitably. However, Griffin et al. (2012) show that even if such information is available to them they do not trade on it. All prior studies, including Griffin et al.(2012), look at direct connections, we give the smart savvy institutional investors their due and find that they do take advantage of the private information they have but in a crafty manner. They trade on information leakages around events which are not heavily monitored. Our results have policy making implications, address the importance of regulation implementations, and could help reconcile the contradictory findings in the literature.

*The Effects of Government Intervention in Financial Market on the Real Economy*

Jinfei Sheng, University of British Columbia, Canada

*Discussant:* George Georgopoulos, York University

This paper investigates the effects of government intervention---Troubled Asset Relief Programs (TARP)---on the real economy. Difference-in-Difference analysis indicates that banks that received TARP funds lent more to firms than Non-TARP banks did after TARP launched. Using firms borrowed from Non-TARP banks as control group, I find that firms borrowed from TARP banks didn't have more investment, employment, or R&D after TARP. Instead, these firms held more liquidity (cash and working capital) than control group firms did.

*Why Are Bad Loans Securitized? The Impact of Shareholder Rights in the Banking Industry*

Jing Zhang, McGill University, Canada

*Discussant:* Anthony Saunders, New York University

This paper investigates the influence of shareholder rights on the quality of loans originated and securitized by financial firms. Using a sample of bank holding companies, I find that banks with large shareholder rights experience poor securitized loan performance, especially for banks which suffer large information asymmetry or have extreme risk-seeking shareholders. In addition, the negative impact of shareholder rights on quality of securitized loans is mitigated if banks provide less securitization recourse. Lastly, banks with the highest shareholder rights pre-crisis are found to suffer the largest losses in securitized loans during the financial crisis. Overall, the evidence supports the view that securitized loan risk is mostly kept by banks and impelled by shareholders. Hence, there could be a potential negative consequence of having powerful shareholders in banks. These findings should provide insights into the ongoing regulatory reform with regard to rebuilding governance mechanisms for financial institutions.

## 3.00 PM - 3.30 PM

Refreshment Break (Colonel By Foyer)

## 3.30 PM - 5.30 PM

Asset Pricing and Agency (Room 103)

Session Chair: Wayne Ferson, University of Southern California

*Continuous-Time Principal-Agent Problem with Drift and Stochastic Volatility Control: With Applications to Delegated Portfolio Management*

Raymond C. W. Leung, University of California, Berkeley, United States

*Discussant:* David Feldman, University of New South Wales

We study a continuous-time principal-agent problem where the agent can privately influence the choice of volatility but yet the principal cannot continuously observe this choice without providing incentives to the agent. This represents a significant departure from the drift-only control moral hazard models in the literature. The drift of the cash flows links both



the private effort choice and volatility choice of the agent that captures a effort-risk-reward trade-off. The overall diffusion of the cash flows is determined by one component that is endogenously managed by the agent, and another component that is exogenously not managed by the agent. The dollar incentives the principal gives to the agent to induce the agent to act optimally, critically depends on the agent's own choice of volatility, and also by an exogenous factor level. This effect is captured through the "risk adjusted sensitivity" (RAS). The model can naturally be applied to a delegated portfolio management problem, especially in the context of hedge funds. Our model suggests outside investors should actively seek investment firms with the following characteristics: (i) has an "internal fund" available only to management, and an "external fund" only available to external investors; (ii) the investment strategies of the internal fund and of the external fund are closely correlated to each other; (iii) the firm has dynamic watermark compensation schemes; and (iv) has an independent and impartial auditor that reports the value of the internal fund, and selects and reports the appropriate benchmark to judge the performance of the internal fund.

*Mutual Fund Intermediation, Equity Issues, and the Real Economy*

Bill Yiqing Zu, University of Melbourne, Australia

*Discussant:* Sergey Isaenko, Concordia University

This paper provides evidence on the real economic roles of mutual funds. With their superior ability to screen and monitor firm investments, mutual funds can enhance economic growth by allocating capital more efficiently through equity markets. Empirically, at both the aggregate and industry level, I find that new equity issues leads to higher subsequent economic growth, only when mutual fund participation in these issues are high. In addition, the participation-growth relation is stronger when fund inflows are low. At the firm-level, equity issues also lead to higher subsequent productivity growth when fund participations are high. These evidence is largely consistent with a simple model of mutual fund intermediation where funds perform a positive role in the economy by screening and monitoring real investments, and suggests that mutual fund perform important roles in the real economy.

*Oil Prices and Core Inflation*

Haibo Jiang, Sauder School of Business, University of British Columbia, Canada

*Discussant:* Antonio Diez de los Rios, Bank of Canada

The pass-through of crude oil prices into inflation attracts excessive attention from policymakers and economists. Oil price hikes not only directly raise household expenditure on gasoline but also indirectly drive up prices of other goods as oil is used as inputs in production. While the direct impact is straightforward, the pass-through of oil price shocks into core CPI (all items less food and energy) inflation is subtle. I document a stylized fact of the correlation between core inflation and changes in oil prices that exhibits a U-shaped curve from 1973 to 2013: being large and positive before 1980s, declining and then being negative for a substantial period from late 1990s to 2008, and finally bouncing up after 2008. This paper shows that the negative correlation, which is unexplained by existing literature, arises when the oil price is endogenously determined and there is feedback effect from the aggregate demand shocks to oil prices. I build a two-sector DSGE model

to rationalize these facts. The pass-through of oil prices into core inflation depends on the origin of oil price shocks. Oil supply shocks cause oil prices and core inflation to co-move, whereas aggregate demand shocks in the final good sector lead to an opposite movement of oil prices and core inflation.

*Stock Return Comovement and the Business Cycle*

Lu Zhang, University of Alberta, Canada

*Discussant:* Nikolay Gospodinov, Federal Reserve Bank of Atlanta

Stock return comovement, measured by the level of the firm-specific component relative to the systematic component of stock market volatility, contains useful information about future economic conditions. Using firm-level U.S. stock returns from 1921 to 2011 reveals that the ratio of firm-specific volatility to systematic volatility can help to predict future real GDP growth, industrial production, real fixed assets investment, and unemployment rates. The predictions are generally significant one-quarter-ahead, particularly after World War II. These effects persist after controlling for other potential economic indicators, both in-sample and out-of-sample. Stock return comovement can also improve the forecasting performance of models predicting NBER business cycles out of sample, up to six months ahead.

*Pricing in Auction Markets for Alternative Assets: Theory and Experimental Evidence*

Matthew Boland, Queen's University, Canada

Daniel Thornton, Queen's University, Canada

*Discussant:* Pauline Shum, York University

This study investigates the utility participants derive from investing in alternative assets called "collectibles," which comprise wine, artwork, antiques, and other similar assets. A model of an auction market is developed that captures some key characteristics of professional and non-professional investors who attend auctions of collectibles and generates predictions that are consistent with prior evidence. Some additional implications of the model are then developed using data derived from an experiment using human subjects. The experimental results indicate: 1. Art enthusiasts derive utility from both financial returns and the pleasure associated with holding collectibles; hence they are willing to pay a premium--called a "pleasure premium"--to own collectibles. This direct confirmation of the existence of the pleasure premium is consistent with postulates contained in prior research. 2. Heterogeneous expectations on the part of non-professionals attending auctions make it likely that at least some non-professionals overbid for collectibles. 3. Pleasure premia included in the bids of non-professionals further reduce the probability of professionals purchasing collectibles at auctions and reduce the returns that are likely to be realized by successful bidders. 4. Overbidding by non-professionals forces professionals out of the market, ensuring that investments in collectibles return less than zero net present value, and the probability of this occurring escalates rapidly as the number of non-professionals attending the auction increases, reaching virtual certainty at about ten. The results are consistent with prior studies indicating that investors who hold collectibles as investments derive little in the way of return benefits.

**Corporate Finance (Room 105)****Session Chair: Nadia Massoud, Melbourne Business School***Corporate Defined Benefit Pension Plans And Chapter 11 Bankruptcy*

Milka Dimitrova, University of British Columbia, Canada

*Discussant:* Alan Huang, University of Waterloo

In this paper, I study the impact of corporate defined benefit pension beneficiaries on the likelihood of Chapter 11 bankruptcy. Defined benefit claimants may play a role in distress because they differ from traditional lenders in the human capital they invest in the firm. Consistent with this view, I find that the higher the defined benefit liabilities' share of the firms' overall liabilities, the lower the likelihood of Chapter 11 bankruptcy. Once in Chapter 11, firms with defined benefit claimants are more likely to emerge from bankruptcy as an independent entity than are firms with traditional lenders. Overall, defined benefit claimholders impact firms' likelihood of Chapter 11 differently from traditional bondholders.

*Firm-Manager Match and Executive Compensation*

Jing Pan, University of Utah, United States

Lei Ma, University of Utah, United States

*Discussant:* Keke Song, Dalhousie University

We investigate the importance of firm-manager match effects in explaining top executive compensation. Our analysis is based on an empirical specification of the determinants of executive compensation that includes time-invariant manager and firm random effects, and an interaction (random) effect between the firm and manager. The interaction effect measures the match effect between a firm and manager, and captures the compensation consequences of match-specific productivity. We find that 11% of the variation in executive pay is explained by time-invariant match effects, while time-invariant manager effects explain 9% of the variation in executive pay. The results imply that a sizeable proportion of what has previously been identified as manager effects is in fact match effects. Further, we show that CEO turnover is more likely when estimated match effects are small. We also find that estimated match effects in compensation are positively related to two firm-manager complementarities: (1) between firm size and managerial talent and (2) between diversification and general management ability. Finally, we show that match effects in compensation are significantly correlated to match effects in firm performance and corporate policies.

*Loss-induced Trades of Insurance Companies*

Michael Liu, The University of Melbourne, Australia

*Discussant:* Lynnette Purda, Queen's University

This paper examines insurance company trading behaviour caused by insurance company operating profits or losses from 2001 through 2009 in the United States. Insurance companies determine the operation and investment strategies endogenously. To identify the causal effect of operating results on trading behaviour, I apply an instrumental variable methodology where the identification comes from the exogenous insured losses of major natural catastrophes. I find that insurance companies experiencing large operating losses tend to decrease existing bond positions. Similarly, insurance companies experiencing large operating profits increase their positions in bond holdings. I expect that the loss-induced transac-

tions of insurance companies create significant price pressures in overlapping bond holdings. Bonds subject to loss-induced sales exhibit price declines and subsequent reversals.

*Optimal Disclosure as a Trade-off between Capital and Product Market Considerations: Theory and Evidence*

Jianqiu Bai, University of Southern California, United States

Yun Ling, University of Southern California, United States

*Discussant:* Archishman Chakraborty, Yeshiva University

We study how firms disclosure decisions are related to their existing financing and production policies. We develop a rational expectations model in which a firm trades off the benefits of more precise disclosure in reducing its cost of capital against the costs of more precise disclosure in potentially revealing confidential information to competitors. Using abnormal return variance and trading volume (Beaver (1968)) as proxies for disclosure precision, we find correlations consistent with our model. We further exploit three quasi-experiments that exogenously affect three underlying parameters in the model and find evidence consistent with our model's predictions. Our model suggests several important determinants of firms optimal disclosure policies and we offer directions for future research.

*Superstar CEOs and Innovation*

Keun Jae Park, University of Oregon, United States

*Discussant:* Jonathan Witmer, Bank of Canada

In this paper, I examine whether a shift in CEO status, as a result of winning a high-profile CEO award affects innovation decisions. On the one hand, agency theory predicts that such an award will increase managerial entrenchment and reduce their efforts to create valuable innovations because they will either pursue value-decreasing pet projects, or simply enjoy the quiet life. On the other hand, these awards may increase managerial job security allowing the CEO to focus on long-term innovative projects rather than trying to boost the stock price through current earnings. I find that CEOs who win an award, on average, innovate more during the four years following the award than similar CEOs who do not win such an award in terms of both the number of patents and the number of citations per patent. I also find that the positive award-winning effect on innovation is stronger for states which have passed anti-takeover laws and for firms with low institutional ownership. Overall, the evidence suggests that winning prestigious awards can have positive long-term consequences for the firm.

**5.30 PM - 8.00 PM****Reception (Trillium Ballroom)**

# Saturday, September 13, 2014

## 7.00 AM - 8.00 AM

Breakfast (Sponsored by Eventus) (Colonel By Foyer)

## 8.00 AM - 9.30 AM

Systemic Risk and Crises (Room 101)

Session Chair: Giovanni Barone Adesi, Swiss Finance Institute, Lugano

*Disclosed Derivatives Use, Securitization, And The Systemic Equity Risk Of Banks*

Gregor Weiss, TU Dortmund University, Germany  
Rouven Trapp, TU Dortmund University, Germany

*Discussant:* Alfred Lehar, University of Calgary

In this paper, we investigate whether the information on derivative use and securitization activities of U.S. banks as disclosed in their pre-crisis 10-K filings predicts their systemic equity risk during the financial crisis. We find strong evidence that disclosed information on the use of financial derivatives increased a banks' systemic equity risk during the financial crisis. Moreover, we find that banks which disclosed significant securitization activities and were thus potentially exposed to under-capitalized risks from conduits possess a higher vulnerability of their equity to market downturns. These effects are economically large and cannot be attributed to larger (and thus systemically more important) banks disclosing more information on their risk management.

*Investment Waves under Cross Learning*

Shiyang Huang, London School of Economics and Political Science, United Kingdom  
Yao Zeng, Harvard University, United States

*Discussant:* Matthieu Bouvard, McGill University

We investigate the driver of multi-firm investment waves, highlighting firms' cross learning. Firms' fundamentals are governed by their idiosyncratic shocks as well as an industry-wide common shock, and their prices aggregate speculators' private information about the two types of shocks. For making better investment decisions, a firm learns from its own as well as other firms' prices, the latter being additional information sources on the common shock. Thus, a spiral between firms' investment sensitivity to the common shock and speculators' weighting on the common shock emerges. This leads to higher investment and price comovements as well as their comovements with the common shock in many relevant circumstances. However, a firm's cross learning creates a novel pecuniary externality on other firms, because it renders other firms' prices less informative on their idiosyncratic shocks through speculators' endogenous over-weighting on the common shock. This externality increases in the number of firms, suggesting that more competitive industries may exhibit more inefficient investment waves.

*Risk Taking and Low Longer-Term Interest Rates: Evidence from the U.S. Syndicated Loan Market*

Seung Jung Lee, Federal Reserve Board, United States  
Sirio Aramonte, Federal Reserve Board, United States  
Viktors Stebunovs, Federal Reserve Board, United States

*Discussant:* Thomas Gilbert, University of Washington & University of British Columbia

We use quarterly supervisory data to investigate risk-taking trends in the U.S. syndicated loan market during the recent period of low long-term interest rates. We study credits acquired by different types of syndicated lenders in both the primary and secondary markets, and we contrast the credit risk taken by banks with that taken by nonbank lenders to better distinguish alternative risk-taking hypotheses. We find that while U.S. and foreign banks' risk taking is generally insensitive to changes in (instrumented) U.S. Treasury note yields, nonbank lenders--in particular, asset managers, including those located in offshore financial centers--add riskier credits to their portfolios in response to a decline in yields. Our results are consistent with "search for yield" by nonbank lenders, and they highlight a risk-taking channel of monetary policy.

Governance and Disclosure (Room 103)

Session Chair: David Stangeland, University of Manitoba

*Voluntary Disclosure and Market Competition: Theory and Evidence from The U.S. Service Sector*

Nathan Dong, Columbia University, United States  
Eda Orhun, Zayed University, United Arab Emirates

*Discussant:* Jiro Ko, McGill University

This paper analyzes a firm's incentives to disclose private information about market demand and its cost when there is a potential entrant. The model illustrates that if signalling to the credit market is not in question, there is a unique fully revealing disclosure equilibrium in which every type of the incumbent, except the high demand-high cost type is transparent. This result is due to the strong incentive of the high demand-high cost type to be nontransparent in any equilibrium candidate in order to discourage entry. However, if one considers the effect of signalling to the credit market which would be especially critical for high-debt firms, a partial disclosure equilibrium where high demand-high cost type pools with the incumbent type with the least prospects (the low demand-high cost type) may also occur. This is due to a second force affecting the disclosure policy, which is the incumbent's own profitability. We use the panel data of service firms in the U.S. to test our theoretical predictions. Consistent with the model's implications, the empirical results indicate that among low-debt service firms, those of high demand-high cost type are likely to avoid information disclosure, whereas among high-debt firms, those of high demand-high cost and low demand-high cost types are less likely to disclose private information.

*CEO Job Security and Risk-Taking*

Peter Cziraki, University of Toronto, Canada  
Moqi Xu, London School of Economics, United Kingdom

*Discussant:* David Koslowsky, University of British Columbia

We use the length of employment contracts to estimate CEO turnover probability and its effects on risk-taking. Protection against dismissal should encourage CEOs to pursue

riskier projects. Indeed, we show that firms with lower CEO turnover probability exhibit higher return volatility, especially idiosyncratic risk. An increase in turnover probability of one standard deviation is associated with a volatility decline of 17 basis points. This reduction in risk is driven largely by a decrease in investment and is not associated with changes in compensation incentives or leverage.

*Managerial Compensation, Regulation And Risk In Banks: Theory And Evidence From The Financial Crisis*

Tommaso Oliviero, CSEF, Italy

Vittoria Cerasi, Bicocca University, Milan, Italy

*Discussant:* Shastri Sandy, University of Missouri

This paper analyzes the relation between CEOs monetary incentives, financial regulation and risk in banks. We present a model where banks lend to opaque entrepreneurial projects to be monitored by managers; managers are remunerated according to a pay-for-performance scheme and their effort is unobservable to depositors and shareholders. Within a prudential regulatory framework that defines a capital ratio and a deposit insurance premium, we study the effect of increasing the variable part of managerial compensation on risk taking. We then test empirically on a sample of large banks around the World how monetary incentives provided to CEOs in 2006 affected banks' stock prices and their volatility during the 2007-2008 financial crisis. The cross-country dimension of our sample allows us to study the interaction between CEO incentives and financial regulation. Our empirical analysis suggests that the sensitivity of CEOs equity portfolios to stock prices is indeed related to the lower performance and higher volatility of stock returns during the financial crisis. This evidence is coherent with the main prediction of the model, that is, the variable part of the managerial compensation, combined with weak insiders' monitoring, exacerbates the risk-shifting attitude by managers. Consistently, both theory and empirical evidence show that the negative relation between banks' performance and CEOs' variable compensation is stronger in countries with explicit deposit insurance and weaker monitoring by outsiders.

**Institutions (Room 104)**

**Session Chair: Bryan Campbell, Concordia University & CIRANO**

*A Better Measure of Institutional Informed Trading*

Hui Guo, University of Cincinnati, United States

Buhui Qiu, Erasmus University Rotterdam, Netherlands

*Discussant:* Kenneth Vetzal, University of Waterloo

Although many studies show that the presence of institutional investors facilitates the incorporation of accounting information into financial markets, the evidence of informed trading by institutions is rather limited in the extant literature. We address these inconsistent findings by proposing PC\_NII, percentage changes in the number of a stock's institutional investors, as a novel informed trading measure. PC\_NII is better able to detect informed trading than are changes in institutional ownership ( $\Delta IO$ )—the measure commonly used in previous studies—because (1) entries and exits are usually triggered by substantive private information and (2) only a small fraction of institutions have superior information. As conjectured, PC\_NII subsumes the information content of  $\Delta IO$  and other institutional trading and herding measures in the forecast of stock returns, and its strong predictive power for stock

returns reflects mainly its close correlation with future earnings surprises. PC\_NII also sheds new light on important empirical issues that require a reliable measure of institutional informed trading.

*Banking Competition and Stability: The Role of Leverage*

Xavier Freixas, University of Pompeu Fabra, Spain

Kebin Ma, University of Warwick, United Kingdom

*Discussant:* Katarzyna Sum, Warsaw School of Economics

This paper re-examines the classical issue of the possible trade-offs between banking competition and financial stability by highlighting the different types of risk and the role of leverage. By means of a simple model we explore whether competition increases portfolio risk, insolvency risk, liquidity risk and systemic risk. We show that the effect of competition on financial stability depends crucially on banks' liability structure, on whether banks are financed by insured retail deposits or by uninsured wholesale investors, whether indebtedness is exogenous or endogenous and on the degree of competition in the banking industry. In particular we show that, while in a classical originate-to-hold banking industry competition might increase financial stability, the opposite might be true for an originate-to-distribute banking structure characterized by a larger fraction of market short term funding. This leads us to revisit the existing empirical literature using a more precise classification of risk. Our theoretical model, thus clarifies a number of apparently contradictory empirical results and proposes new ways to analyze the impact of banking competition on financial stability.

*Credit Risk Determinants of Insurance Companies*

Liliana Gonzalez, ESSEC Business School, France

Lorenzo Naranjo, ESSEC Business School, France

*Discussant:* Madhu Kalimipalli, Wilfrid Laurier University

This paper investigates the determinants of credit risk in insurance companies in the U.S. and Europe. Consistent with recent results for non-financial firms in the U.S., we find that equity volatility is a major determinant and predictor of CDS spreads for both U.S. and European insurers, even after controlling for the composition of their investment portfolios and other firm-specific characteristics such as leverage and macro controls. Furthermore, we find macroeconomic factors to affect the credit risk of European but not U.S. insurers, whereas cash holdings seem to be relevant in explaining the credit spreads of U.S. insurance companies. We find that cash holdings and credit spreads of U.S. insurers are positively correlated. However, the availability of cash reduces the credit risk of firms experiencing positive solvency shocks. Overall, our results are economically significant and suggest that equity and credit markets incorporate quickly relevant information on the creditworthiness of large insurers.

**Behavioural Finance (Room 105)**

**Session Chair: Kai Li, University of British Columbia**

*CEO Appearance*

Douglas Cook, University of Alabama, United States

Shawn Mobbs, University of Alabama, United States

*Discussant:* Amos Nadler, Western University

Using an objective measure of executive facial attractiveness we find that shareholders value beauty. Specifically, at-



tractive executives are associated with a higher abnormal return around the announcement of their appointment as CEO. These results are strongest for insider appointments and relatedly, more attractive facial features increase the likelihood of an executive winning a tournament and being selected as CEO. We also find that facial beauty is more important when there is a larger pool of qualified candidates with similar tangible skills and it is less important in firms where unique or technical skills are more valuable. Lastly, we discover some evidence that females are held to a higher standard of beauty than males. These results indicate that beauty is an important executive trait that has significant labor market and corporate finance implications.

*Information Asymmetry, Information Content, And Underreaction To Earnings Announcements*

Kee H. Chung, State University of New York (SUNY) at Buffalo, United States

Oliver Kim, University of Maryland, United States

Steve C. Lim, Texas Christian University, United States

Sean Yang, State University of New York (SUNY) at Buffalo, United States

*Discussant:* David Ng, Cornell University

This paper shows, both analytically and empirically, that the market reaction to earnings announcements and post-earnings announcement drift depend on both the information content of earnings and the information asymmetry between traders that arises from the differential utilization of earnings information. Specifically, we show that  $ERC = k(1 - p^2)$  and  $PEAD = kp^2$ , where ERC is the earnings response coefficient, PEAD is the post-earnings announcement drift,  $k$  is the information content of earnings, and  $p$  is the correlation coefficient between order imbalance and earnings surprise. In our model,  $p^2$  is an empirical metric of the information asymmetry-driven underreaction that can be used to predict the size of the post-earnings announcement drift in a timely manner. We provide strong empirical evidence that is consistent with our analytical predictions. Overall, our results suggest that PEAD could be a noisy equilibrium outcome in the presence of asymmetric information.

*Contagious Negative Sentiment and Corporate Policies: Evidence from Local Bankruptcy Filings*

Jawad Addoum, University of Miami, United States

Alok Kumar, University of Miami, United States

Nhan Le, University of Mannheim, Germany

*Discussant:* Kai Li, University of British Columbia

This study shows that corporate bankruptcy events affect the corporate behavior of geographically proximate firms. Following the bankruptcy of a local peer, non-filing local firms significantly reduce investment expenditures, reduce capital structure leverage, and hold more cash. The effects of local bankruptcy are more pronounced when the filing firm is larger and more mature, and stronger among firms managed by CEOs with relatively short tenure. Importantly, the spillover effects associated with geographic proximity cannot be explained by intra-industry or supply chain effects documented in the extant literature. We also find that the effects cannot be explained by shocks to the local economy. Collectively, these results suggest that corporate managers follow the availability heuristic and become overly conservative in their investment and financial policies in response to local distress events.

**International and Arbitrage (Room 106)**

**Session Chair: George Georgopoulos, York University**

*A Wake-Up Call Theory Of Contagion*

Toni Ahnert, Bank of Canada; London School of Economics, Canada

Christoph Bertsch, Sveriges Riksbank, Sweden

*Discussant:* Denis Gorea, Goethe University Frankfurt and Bank of Canada

Financial contagion can occur in the absence of interconnectedness, a common investor base, or ex-post correlated fundamentals. A financial crisis in one region is a wake-up call for investors in other regions. If the correlation of regional fundamentals is potentially positive but uncertain ex-ante, investors acquire information about this correlation to determine their exposure. Despite zero exposure ex-post, contagion can occur due to elevated strategic uncertainty among informed investors. Our novel theory of contagion after a wake-up call -- applicable to currency crises, bank runs, and debt crises -- generates new empirical predictions and testable implications for laboratory experiments.

*Out-of-Sample Evidence on the Returns to Currency Trading*

David Chambers, Cambridge University, United Kingdom

Olivier Accominotti, London School of Economics, United Kingdom

*Discussant:* Marie-Claude Beaulieu, Université Laval

We document the existence of excess returns to naïve currency trading strategies during the emergence of the modern foreign exchange market in the 1920s and 1930s. This era of active currency speculation constitutes a natural out-of-sample test of the performance of carry, momentum and value strategies well documented in the modern era. We find that the positive carry and momentum returns in currencies over the last thirty years are also present in this earlier period. In contrast, the returns to a simple value strategy are negative. In addition, we benchmark the rules-based carry and momentum strategies against the discretionary strategy of an informed currency trader: John Maynard Keynes. The fact that the strategies outperformed a superior trader such as Keynes underscores the outsized nature of their returns. Our findings are robust to controlling for transaction costs and, similar to today, are in part explained by the limits to arbitrage experienced by contemporary currency traders.

*The Impact Of Arbitrage On Market Liquidity*

Dominik Rosch, Erasmus University, Netherlands

*Discussant:* Piet Sercu, KU Leuven

How arbitrage affects liquidity depends on the reason why the arbitrage opportunity arises. Using tick-by-tick data (in the Depositary Receipts market, as an example where arbitrage is almost risk-free) from the US and five different countries from 1996 to 2013, I find that 70% of all arbitrage opportunities arise because of demand shocks. Impulse response functions indicate that a one standard deviation increase in arbitrage activity predicts a decrease in order imbalance and a 0.25 standard deviation increase in liquidity. These findings suggest that arbitrageurs trade against market order imbalance, and thereby improve market integration and liquidity. I then use days on which the home-market stock or the ADR is ex-dividend, but the other is cum-dividend, as an instrument to

show that arbitrage activity contemporaneously causes an improvement in liquidity.

## Mergers and Acquisitions (Room 107)

**Session Chair: Ash Hossain, Memorial University of Newfoundland**

### *Fear, Feedback and Disclosure: Governance Role of Negative Media Coverage in M&A Decisions*

Shantanu Dutta, University of Ontario Institute of Technology, Canada

Kose John, New York University, United States

Samir Saadi, University of Ottawa, Canada

Pengcheng Zhu, University of San Diego, United States

*Discussant:* Olivier Dessaint, University of Toronto

We examine the governance role of media coverage on the M&A decision-making process using a large sample of M&A events, and relate those events to news items appeared in leading newspapers and on newswires. Our results show that negative media coverage reduces the probability of a firm making an acquisition. It does so by playing a number of governance roles. We find that negative media (i) disciplines managers, by influencing turnover decisions and escalating costs of acquisitions, and (ii) shapes ingratiation behavior of managers, by giving useful feedback and providing an efficient platform for self-disclosure. Our results further show that distinct media sources (newspaper and newswire) play governance roles differently.

### *Strategic Acquisitions by Corporate Venture Capital Investors*

Lora Dimitrova, University of Exeter, United Kingdom

*Discussant:* Chen Liu, Queen's University

Unlike traditional venture capitalists, corporate venture capital (CVC) investors are likely to eventually acquire portfolio ventures. I find that the likelihood of such an acquisition decreases with the uncertainty associated with the venture's innovation and increases with the number of CVCs co-invested. Moreover, CVCs with lower level of internal innovation are more likely to acquire portfolio ventures. However, the acquisition signals poor prospects for future innovation, which explains the negative market reaction to the announcements of such deals. I also show that CVCs appear to be learning through active management of their portfolios and acquire ventures backed by other CVCs when their own portfolio performs poorly.

### *Why Do Some Target Firms Choose to Seek a Second Fairness Opinion in Mergers and Acquisitions?*

Tingting Liu, University of Georgia, United States

*Discussant:* Sandra Betton, John Molson School of Business

A key question in Mergers and Acquisitions is whether the transactions are fair. A common practice is to ask a financial advisor to evaluate the fair value of a transaction and provide a fairness opinion. However, fairness opinions have been viewed as a "rubber stamp" since almost every target firm obtains one. Using a manually compiled data set over the period 1996-2011, I examine why some target firms choose to obtain a SECOND fairness opinion and the wealth effects of this choice. More specifically, I test two competing hypotheses: the agency theory hypothesis which predicts the use of multiple opinions destroys shareholder value, and the shareholder interests hypothesis which argues that target firms obtain a second

fairness opinion for strategic reasons. The results show that after controlling for endogeneity, the use of multiple opinions has a significantly positive impact on announcement returns. Target firms are more likely to obtain a second fairness opinion in management buyout deals, in hostile deals, and in large deals. A second fairness opinion is also more likely to be sought if the target has multiple business segments. Overall, my findings provide new evidence that is consistent with the shareholder interests hypothesis and is inconsistent with the agency theory hypothesis.

## Microstructure (Room 108)

**Session Chair: Jason Smith, Utah State University**

### *What Makes the S&P 500 Jump?*

Marcel Prokopczuk, Zeppelin University, Germany

Chardin Wese Simen, University of Liverpool, United Kingdom

*Discussant:* Dominik Rosch, Erasmus University

Using intraday transaction prices and a non-parametric test, we study jumps in the S&P 500 market. We show that jumps are low probability, high impact events. Using a comprehensive set of newswires, we explore the events that trigger jumps. We are able to relate around 80% of jumps to scheduled and, more importantly, unscheduled news. Interestingly, unscheduled events frequently trigger the largest jumps in the stock market, indicating that unexpected events truly "shock" the market. Analyzing scheduled announcements, we find limited evidence in support of a positive relationship between announcement surprises and uncertainty on the one hand, and the likelihood of jumps on the other. Collectively, our results challenge common beliefs about the triggers of jumps, suggesting that the relationship between news and jumps may be more complex than originally thought.

### *Liquidity Supply Across Multiple Trading Venues*

Laurence Lescourret, ESSEC Business School, France

Sophie Moinas, U. Toulouse, France

*Discussant:* Elena Pikulina, UBC Sauder

Fragmentation and technological innovations have given rise to new trading strategies. One of them is to supply liquidity simultaneously in multiples venues. This "global" market-making implies to actively manage inventory risk across venues. In this paper, we build a global inventory model and show that in some cases dealers consolidate the order flow, which fragments across venues, leading to lower transaction costs. We also show that global market-making strategies result in interrelated spreads. We use Euronext proprietary data on liquidity suppliers for multi-traded firms to empirically investigate the predictions of our model. We find evidence of mean reversion and order placement strategies supporting implications of global inventory management across venues. We also show that spreads in one venue vary with the total order flow across venues and with liquidity suppliers global inventories, consistently with our main prediction.

### *Debt Maturity and the Liquidity of Secondary Debt Markets*

Max Bruche, City University London, United Kingdom

Anatoli Segura, CEMFI, Spain

*Discussant:* Nathalie Moyen, University of Colorado at Boulder

We develop an equilibrium model of debt maturity choice of firms, in the presence of fixed issuance costs in primary debt

markets, and an over-the-counter secondary debt market with search frictions. Liquidity in this market is related to the ratio of buyers to sellers, which is determined in equilibrium via the free entry of buyers. Short maturities improve the bargaining position of debtholders who sell in the secondary market and hence reduce the interest rate that firms need to offer on debt. Long maturities reduce re-issuance costs. The optimally chosen maturity trades off both considerations. Firms individually do not internalize that choosing a longer maturity increases the expected gains from trade in the secondary market, which attracts more buyers, and hence also facilitates the sale of debt issued by other firms. As a result, the laissez-faire equilibrium exhibits inefficiently short maturity choices. Empirical implications of the model include that issuance yields and bid-ask spreads should be increasing in maturity.

## 9.30 AM - 10.00 AM

Refreshment Break (Colonel By Foyer)

## 10.00 AM - 11.30 AM

Equity Valuation (Room 101)

Session Chair: Adlai Fisher, University of British Columbia

*The Idiosyncratic Volatility--Expected Return Relation: Reconciling the Conflicting Evidence*

Doron Avramov, Hebrew University, Israel

Scott Cederburg, University of Arizona, United States

Discussant: Grant Wang, Highstreet Asset Management

This paper develops a simple model to resolve the conflicting evidence of a large negative (Ang, Hodrick, Xing, and Zhang (AHXZ, 2006)) versus large positive (Fu (2009)) relation between idiosyncratic volatility (IVOL) and average returns. In the proposed model, IVOL strongly predicts the cross section of average returns, even when it is unpriced. The predictive ability of IVOL arises in the model because of its relations with dividend size and expected dividend growth, both of which are related to risk premiums. In particular, firms with small dividends have high IVOL and high expected returns, while low dividend growth firms have high IVOL and low expected returns. Empirical evidence strongly supports the model's novel prediction of a negative relation between IVOL and firm growth. Consistent with predictions, we find that IVOL is positively related to returns in the dividend size dimension and negatively along the dividend growth dimension. Finally, the AHXZ and Fu measures are more closely aligned with dividend growth and dividend size, respectively, consistent with their opposing relations with IVOL.

*Spurious Inference in Unidentified Asset-Pricing Models*

Raymond Kan, University of Toronto, Canada

Nikolay Gospodinov, Federal Reserve Bank of Atlanta, United States

Cesare Robotti, Imperial College of London, United Kingdom

Discussant: Alan Huang, University of Waterloo

This paper studies some seemingly anomalous results that arise in possibly misspecified and unidentified linear asset-pricing models estimated by maximum likelihood and one-

step generalized method of moments. Strikingly, when useless factors (that is, factors that are uncorrelated with the returns on the test assets) are present, the models exhibit perfect fit, as measured by the squared correlation between the model's fitted expected returns and the average realized returns, and the tests for correct model specification have asymptotic power that is equal to the nominal size. In other words, applied researchers will erroneously conclude with high probability that the model is correctly specified even when the degree of misspecification is arbitrarily large. We also derive the highly non-standard limiting behavior of these invariant estimators and their  $t$ -tests in the presence of identification failure. These results reveal the spurious nature of inference as factors that are useless are selected with probability approaching one asymptotically, while factors that are useful are driven out from the model. The practical relevance of our findings is demonstrated using simulations and an empirical application.

*Small Growth and Distress Anomalies: Two Sides of the Same Coin?*

Kyung Shim, University of New South Wales, Australia

Harjoat Bhamra, Imperial College, United Kingdom

Discussant: Adlai Fisher, University of British Columbia

We develop a firm valuation model with growth options and downward jump risk as a proxy for distress to capture the cross-sectional variation of stock returns associated with high distress, size and book-to-market. A greater jump risk reduces the ratio of fixed assets to firm value due to a greater option value (Merton (1976)) and simultaneously decreases the sensitivity of firm value to systematic risk. We propose a novel mechanism that simultaneously generates the low equity returns of small firms with low book-to-market ratio (small growth anomaly), and the low equity returns of high distress firms (distress anomaly) shown to exist separately in the literature. The model further predicts that the stocks of high distress firms capture the risk of small growth firms; and that this relation strengthens in the firms' reliance on growth options. Empirical results support these predictions.

Governance (Room 103)

Session Chair: Vikas Mehrotra, University of Alberta

*Are Entrepreneurs Special? Evidence from Board Appointments*

Olubunmi Faleye, Northeastern University, United States

Wilson Kung, University of New South Wales, Australia

Jerry Parwada, University of New South Wales, Australia

Gloria Tian, University of Lethbridge, Canada

Discussant: Tu Nguyen, University of Waterloo

We study the appointment of entrepreneurs as outside directors to examine their effect on corporate outcomes in firms not created by them. We provide additional evidence on how the professional backgrounds of directors impact board effectiveness. Entrepreneur directors are more likely to join smaller firms and those whose founders currently serve as directors. Appointments of entrepreneur directors attract higher stock price reactions than appointments of other outside directors and firm value increases with their number. The value effect is greater when the firm is smaller or operates in more competitive industries. Entrepreneur directors are also associated with higher risk-taking, increased R&D investments, and improved revenue growth, each of which effect is associated with higher firm values.

*Do Rating Agencies Act as Third-Party Monitors? Evidence from Moody's Credit Watches*

Hamdi Driss, York University, Canada

Gordon Roberts, York University, Canada

Nadia Massoud, The University of Melbourne, Australia

*Discussant:* Amir Barnea, HEC, Montreal

Based on Moody's issuer-level credit watch actions on U.S. nonfinancial public borrowers between 1992 and 2011, we study the relations between credit watch resolution outcomes and the dynamics of corporate fundamentals. Using firms with watch-preceded rating downgrades (control firms) as a benchmark, we document that firms with watch-preceded rating confirmations (treatment firms) experience an increase in long-term financing, investment, and profitability immediately following the credit watch period. These patterns are stronger for treatment firms of lower credit quality, for which external monitoring is more valuable. We further show that financially constrained treatment firms substantially increase their long-term financing immediately following the watch period, indicating that agency's monitoring can help alleviate capital constraints resulting from information asymmetry. Additional tests show that treatment firms are more profitable regardless of corporate governance, implying that agency's monitoring is independent of corporate governance. These findings suggest that credit agencies have real effects on corporate behavior, and that a credit watch with direction downgrade acts as an effective monitoring mechanism.

*Creditor Control through Loan-to-Loan and Loan-to-Own*

Kai Li, University of British Columbia, Canada

Wei Wang, Queen's University, Canada

*Discussant:* Vikas Mehrotra, University of Alberta

This paper provides new evidence on the different roles and strategies adopted by creditors of distressed firms. Loan-to-loan occurs when secured bank lenders continue to provide debtor-in-possession financing after a borrower files for Chapter 11, while loan-to-own occurs when unsecured creditors become equity holders at emergence and/or activist investors provide debtor-in-possession financing. We find that loan-to-loan creditors gain power against junior claimants but do not affect CEO or board turnover, while loan-to-own creditors actively improve corporate governance and operating performance of emerged firms. We show the importance of differentiating creditors by their types, roles, and strategies when studying creditor control.

**Institutions (Room 104)****Session Chair: John Murray, Bank of Canada***A Market-Based Funding Liquidity Measure*

Zhuo Chen, Northwestern University, United States

Andrea Lu, Northwestern University, United States

*Discussant:* Scott Hendry, Bank of Canada

In this paper, we construct a measure for funding liquidity that exploits information in both the time series and cross-section of stock returns. We show that in an economy where investors face asset-specific funding constraints (margins), the risk premium of a market-neutral portfolio that longs leveraged low-beta stocks and shorts de-leveraged high-beta stocks, as in Frazzini and Pedersen (2013), depends on both the market-wide funding conditions and stocks' margin requirements.

We isolate funding liquidity shocks as the return difference between two zero-beta portfolios constructed using stocks with high and low margins. Our market-based funding liquidity measure is highly correlated with other proxies proposed in the literature, and cannot be explained by existing pricing factors, such as the Fama-French three factors. Moreover, our measure helps explain the cross-section of hedge fund returns: hedge funds with the lowest funding liquidity sensitivities earn 10.7% per year higher returns than their peers whose returns strongly comove with funding liquidity shocks. We provide a possible explanation for this finding: some funds have the ability to manage the funding liquidity risk and thus can earn higher returns.

*Subjective or Objective? Nonparametric Estimation Of Misreporting and Mis-assessment in Corporate Credit Rating*

Ruichang Lu, National University of Singapore, Singapore

Yao Luo, University of Toronto, Canada

Ruli Xiao, Johns Hopkins University, United States

*Discussant:* Martin Boyer, HEC Montreal

This paper investigates the misreporting and mis-assessment of corporate credit ratings by credit rating agencies (CRAs). We distinguish between "mis-assessment", which is the noise from the unobservable true rating to the rating perceived by CRAs (the internal rating), and "misreporting", which is the difference between perceived and reported rating by CRAs. Using a sample of corporate credit ratings during 1986-2011, we find that the mis-assessment in credit rating is very small and statistically insignificant. Also, there is a U-shaped relationship between true credit rating and misreporting probability. Specifically, CRAs misreport the credit ratings for high-grade firms with a probability of 3%, for middle-grade firms with a probability of 0, and for low-grade firms with a probability of 6%. Second, the misreporting behavior of CRAs differ significantly across the industries. The financial industry has the highest misreporting probability (35% in the lowest-grade firms) and the largest misreporting magnitude (rating grade jump between true and reported grade). The energy industry has the lowest misreporting probability. Last, when economic conditions are bad, the credit rating agent is more likely to deflate the rating.

*Tipsters and Tippees: Brokers' Pre-release of Price-Sensitive Information to their VIP Clients*

Tamara Nefedova, NYU Stern School of Business, United States

*Discussant:* Ranjini Jha, University of Waterloo

Using proprietary high-frequency trading data, I analyze information leakage of financial analyst recommendations to their elite clients, as well as characteristics of the institutional investors receiving such advance knowledge. I find that investment managers, who have an established relationship with their brokers, on average buy more than other investors do in the 5-day period before positive analyst coverage initiations. My results suggest that clients, who enjoy a privileged relationship with their brokers, receive and use the pre-released information in their trades.



**Capital Structure (Room 105)****Session Chair: Ashraf Zaman, Saint Mary's University***Protection of Trade Secrets and Capital Structure Decisions*

Sandy Klasa, University of Arizona, United States

Hernan Ortiz-Molina, University of British Columbia, Canada

Matthew A. Serfling, University of Arizona, United States

Shweta Srinivasan, University of Arizona, United States

*Discussant:* Nilanjan Basu, Concordia University

We study whether a firm's capital structure decisions are affected by the risk that its rivals in product markets could gain access to its non-patented "trade secrets." Our tests exploit the staggered recognition of the Inevitable Disclosure Doctrine (IDD) by U.S. state courts as an exogenous event that increases the protection of a firm's trade secrets by reducing the mobility of workers with knowledge of the trade secrets to similar jobs at rival firms. We find that firms increase their leverage following the recognition of the IDD, especially those in more competitive industries, those whose workers are more likely to know trade secrets, and those that face greater ex-ante risk of losing key employees to rivals. Also, firms' borrowing costs decrease after the recognition of the IDD controlling for leverage, implying that better protection of trade secrets reduces firms' risk. Overall, our findings suggest that the risk of losing intellectual property to rivals increases the value of financial slack and thus leads firms to choose conservative capital structures.

*Loan Covenant Violation and Corporate Liquidity Management*

Yijia Zhao, University of South Carolina, United States

*Discussant:* Ing-Haw Cheng, Dartmouth College

I provide evidence on a significant impact of loan covenant violations on corporate liquidity management. Specifically, I find that firms begin to exhibit a significant tendency to save cash out of their cash flows (as represented by a positive cash flow sensitivity of cash) after covenant violations, suggesting that firms resort to internally-generated cash for liquidity after breaching external credit contracts. Moreover, the increase in the cash saving rate after covenant violations is more pronounced among firms that are likely to be financially constrained, firms that have greater hedging needs, firms that depend more on external finance. I further show that shareholders attach a higher value to an additional dollar of internal cash after covenant violations. Collectively, the empirical findings are consistent with creditor intervention following covenant violations increasing the cost of external finance, which causes firms to rely more on self-produced cash for liquidity. The stock market perceives the proactive cash retention policy in response to covenant violations to be value-enhancing.

*Credit Default Swaps and Corporate Cash Holdings*

Marti Subrahmanyam, New York University, United States

Dragon Tang, University of Hong Kong, Hong Kong

Sarah Wang, Warwick Business School, United Kingdom

*Discussant:* Ashraf Zaman, Saint Mary's University

Firms obtain improved access to credit supply after their debt is referenced by credit default swaps (CDS). However, CDS-referenced firms also face tougher creditors and greater refinancing risk. In this context, we examine how firms manage their liquidity in response to the introduction of CDS trading on their debt. We find that firms hold significantly more cash after the inception of CDS trading. This finding is

robust to the endogeneity of CDS trading, using instrumental variables and propensity score matching. The increase in cash holding by CDS firms is more pronounced for firms with lines of credit, suggesting that banks with CDS protection impose greater discipline on firms, causing them to take a more conservative risk management approach.

**Derivatives (Room 106)****Session Chair: Ivan Sergienko, Scotiabank***Non-Transferable Non-Hedgeable Executive Stock Options Pricing*

David Colwell, University of New South Wales, Australia

David Feldman, University of New South Wales, Australia

Wei Hu, Curtin University, Australia

*Discussant:* Gordon Sick, University of Calgary

We introduce a method of valuating non-transferable non-hedgeable (NTNH) contingent claims and use it to price executive stock options (ESOs). We use NTNH constraints to break local co-linearity, caused by derivative assets, that renders common portfolio optimization methods ineffective. We are, thus, able to translate portfolios that include NTNH derivatives into portfolios of primary assets (only). We achieve this by replicating derivatives using primary assets, then, integrating NTNH constraints into a single rectangular constraint. Solving the constrained portfolio optimization facilitates identification of stochastic discount factors that price any contingent claim in such portfolios. Implementing our method, we find subjective prices of NTNH European and American ESOs, both for block exercise and a continuum of exercise ratios. We identify executives' optimal exercise policies. We use these to find the objective ESOs price/cost to firms.

*Volatility-of-Volatility Risk*

Darien Huang, The Wharton School, University of Pennsylvania, United States

Ivan Shaliastovich, The Wharton School, University of Pennsylvania, United States

*Discussant:* Bo Young Chang, Bank of Canada

We show that time-varying volatility-of-volatility is a separate and significant risk factor that affects prices and risk premia in options markets. Shocks to volatility-of-volatility command a negative price of risk, which is an additional source of risk distinct from volatility risk. We use the VVIX index, which is a model-free, forward-looking measure of the volatility-of-volatility constructed from VIX options, as an ex-ante measure of expected volatility-of-volatility risk. Using high-frequency data, we shed light on the fine structure of variance risks and document that while the VVIX is a strong predictor of future realized volatility-of-volatility, the VIX itself is not. Options that pay off when volatility-of-volatility is high have significantly negative returns. In the cross-section, options more sensitive to volatility-of-volatility risks earn more negative expected returns. In the time-series, high expectations of future volatility-of-volatility predicts more negative expected returns to delta-hedged option portfolios. The VVIX explains fluctuations in the risk premia in both the S&P500 and VIX options markets. Our results are robust to accounting for jump risk proxies. Overall, the evidence we find supports a significant negative risk premium for time-varying volatility-of-volatility risk.

*Slow Diffusion of Information and Price Momentum in Stocks:  
Evidence from Options Markets*

Zhuo Chen, Northwestern University, United States  
Andrea Lu, Northwestern University, United States

*Discussant:* Chayawat Ornthanalai, University of Toronto

This paper investigates the source of price momentum in the equity market using information from options markets. The empirical results provide direct evidence of the gradual information diffusion model in Hong and Stein (1999). Consistent with their theory, we show that a successful identification of stocks' information diffusion stage helps explain momentum profits. We are able to enhance momentum profits by longing winner stocks with higher growth (and shorting loser stocks with larger drop) in call options implied volatility. Our empirical strategy generates a risk-adjusted alpha of 1.8% per month for a hedged winner-minus-loser portfolio over the 1996-2011 period, during which the simple momentum strategy fails to perform. The results are stronger and clearer if we use call options compared to put options, which are consistent with managers' tendency to reveal good news and hide bad news. Our results are robust to transaction costs, choice of options' moneyness, elimination of implied volatility persistence, and choice of options' time-to-maturity. Finally, our results are not driven by existing stock-level characteristics, such as size, trading volume, and analyst coverage.

**Flexibility and Investment (Room 107)**

**Session Chair:** Ron Giammarino, University of British Columbia

*Idiosyncratic Risk and the Manager*

Brent Glover, Carnegie Mellon University, United States  
Oliver Levine, University of Wisconsin, United States

*Discussant:* Wei Wei, University of Calgary

Compensating a manager with equity-based pay induces effort but also exposes the manager to firm-specific risk. In comparison to a diversified shareholder, this distorts the manager's discount rate and, in turn, investment and financing decisions. We embed this agency conflict in a structural model of the firm and estimate its effect on firm policies. We estimate the agency friction for a large panel of U.S. public firms and find significant cross-sectional and time-series variation in a manager's incentive to over- or under-invest. Our panel of incentive estimates helps to explain a broad set of empirical patterns, including investment, leverage, cash holdings, valuation ratios, and acquisition activity.

*Real Options And The Option To Withdraw: Evidence From  
Open Market Share Repurchases*

Mark Mietzner, Zeppelin University, Germany

*Discussant:* Brian Smith, Wilfrid Laurier University

A fairly large number of share repurchase programs are announced but not completed. In this paper, we explore the distinguishing characteristics of firms that completed or withdrew their repurchase programs. Our findings help further understanding of the economic reasons why firms would withdraw previously announced buyback programs. Based on our sample of 818 completed and 101 withdrawn share repurchases, we show a significant drop in systematic risk for repurchasers. This suggests that completed share buybacks are a response to deteriorating investment opportunities. In con-

trast, the systematic risk of non-repurchasing firms decreases prior to the announcement, followed by an increase that peaks during the event period. This finding suggests that firms withdraw their stock repurchase intentions when growth options move into the money.

*The Value in Waiting to Issue Debt*

Babak Lotfaliei, McGill University, Canada

*Discussant:* Yuanshun Li, Ryerson University

This paper addresses the zero-leverage puzzle, the observation that many firms do not issue debt and thus seem to forego sizable debt benefits. By considering the real option of issuing debt, small and risky firms have incentives to postpone debt issuance, even when standard trade-off theory predicts that these firms should have leverage. Thus, the value of debt-free firms should include an option component whose value is derived from future debt issuance benefits. The paper proposes a model of optimal timing for issuing debt and finds empirical support for the model's predictions.

**Microstructure (Room 108)**

**Session Chair:** Gbenga Ibikunle, University of Edinburgh

*High Frequency Trading with Speed Hierarchies*

Wei Li, University of Maryland, Johns Hopkins University, United States

*Discussant:* Archisman Chakraborty, Yeshiva University

Traders differ in speed and their speed differences matter. I model strategic interactions induced when high frequency traders (HFTs) have different speeds in an extended Kyle (1985) framework. HFTs are assumed to anticipate incoming orders and trade rapidly to exploit normal-speed traders' latencies. Upon observing a common noisy signal about the incoming order flow, faster HFTs react more quickly than slower HFTs. I find that these front-running HFTs effectively levy a tax on normal-speed traders, making markets less liquid and prices ultimately less informative. Such negative effects on market quality tend to be more severe when HFTs have more heterogeneous speeds. Even when infinitely many HFTs compete, their negative effects in general do not vanish. I analyze policy proposals concerning HFTs and find that (1) lowering the frequency of trading mitigates the negative impact of HFTs on market quality and (2) randomizing the sequence of order execution can degrade market quality when the randomizing interval is short. Consistent with empirical findings, a small number of HFTs can generate a large fraction of the trading volume and HFTs' profits depend on their speeds relative to other HFTs.

*Asymmetric Information and Inventory Concerns in Over-the-Counter Markets*

Julien Cujean, University of Maryland, United States  
Remy Praz, EPFL, Switzerland

*Discussant:* Maria Pacurar, Dalhousie University

We study how transparency, modeled as information about one's counterparty liquidity needs, affects the functioning of an over-the-counter market. In our model, investors hedge endowment risk by trading bilaterally in a search-and-matching environment. We construct a bargaining procedure that accommodates information asymmetry regarding investors' inventories. Both the trade size and the trade price are

endogenously determined. Increased transparency improves the allocative efficiency of the market. However, it simultaneously increases inventory costs, and leads to a higher cross-sectional dispersion of transaction prices. For investors with large risk exposure, the increase of the inventory costs dominates the benefits of the market efficiency. We link the model's predictions to recent empirical findings regarding the effect of the TRACE reporting system on bond market liquidity.

*Information Percolation, Momentum, and Reversal*

Daniel Andrei, UCLA Anderson, United States

Julien Cujean, University of Maryland, United States

*Discussant:* Aditya Kaul, University of Alberta

The tendency of asset prices to trend over short horizons and revert over long horizons---momentum and reversal---can find an explanation within a simple, rational model. The key ingredient is word-of-mouth communication, which we introduce in the standard noisy rational expectations framework. Word-of-mouth communication accelerates the information revelation and generates momentum in asset returns. Due to social interactions, investors with heterogeneous trading strategies coexist in the marketplace---some agents are contrarians, others are momentum traders, yet momentum is not completely eliminated. Finally, word-of-mouth communication can propagate a rumor and a price run-up, followed by reversals once the rumor subsides.

## 11.45 AM - 1.15 PM

### Luncheon (Sponsored by Bank of Canada) and NFA Annual General Meeting (Room 214)

**Chair:** Stéphane Chrétien, NFA President and Université Laval

The NFA Annual General Meeting will take place at the Luncheon.

*Agenda:*

- Election of Directors
- Report of Program Chair
- Best Paper Awards
- Announcement of NFA 2015 Conference

## 1.30 PM - 3.30 PM

### Macro Asset Pricing (Room 101)

**Session Chair:** Michael Brennan, UCLA

*Slow Capital Movement and Risk Premium Puzzle*

Sergey Isaenko, Concordia University, Canada

*Discussant:* Amir Akbari, McGill University

We consider an economy where investors trade stock market to which they can allocate only with delays. We find a linear equilibrium in this economy and calibrate the slow capital movement by using a typical portfolio turnover observed empirically. Then we show that the risk premium and the volatility of the stock market returns are many times bigger than in an economy with no delays in capital allocations. It follows that the presence of delays in capital allocation can help to solve the risk premium puzzle. Furthermore, our model

predicts price overreaction to both bad and good news at short horizons and the absence of the "cliente effect" introduced by Amihud and Mendelson (1986).

*Heterogeneous Agents and Long Horizon Features of Asset Prices*

Blake LeBaron, Brandeis University, United States

*Discussant:* Chris Hrdlicka, University of Washington

Heterogeneous agent models for financial markets have provided explanations for many empirical regularities of relatively high frequency (hourly/daily) financial time series. They have been much quieter when it comes to longer range features. This paper examines a simplified computational heterogeneous agent model in the context of various longer range time series properties for equity returns. The model is compared to a specially created long range data set, and is found to perform well in terms of replicating features, and even revealing some aspects of the data that have not been well quantified to date. By matching empirical properties at both short and long horizons this sets a higher standard in terms of validation which this model is able to match.

*Price Dynamics and Market Selection in Small and Large Economies*

Filippo Massari, UNSW, Australia

*Discussant:* Emilio Osambela, Carnegie Mellon University

This paper investigates the hypothesis that markets favor traders with more accurate beliefs. Unlike existing results, notably Sandroni (2000) and Blume-Easley (2006), I propose an approach that (i) is directly informative about equilibrium prices, (ii) provides a condition that is necessary as well as sufficient for the wealth-share of a trader to converge to zero, and (iii) can be applied to both small and large economies. My analysis reveals that these two settings are qualitatively different. In small economies, irrespective of traders' risk attitudes, markets select for traders with more accurate beliefs. In large economies, risk attitudes can play a determinant role on the survival of a trader: there are cases in which the wealth-share of a group of traders with rational expectations converges to zero even if no other trader in the economy has correct beliefs.

*Stock Market Ambiguity and the Equity Premium*

Panayiotis Andreou, Cyprus University of Technology, Cyprus  
Anastasios Kagkadis, Durham University Business School, United Kingdom

Paulo Maio, Hanken School of Economics, Finland

Dennis Philip, Durham University Business School, United Kingdom

*Discussant:* Masahiro Watanabe, University of Alberta

We create a novel measure of stock market ambiguity that is derived from the dispersion of S&P 500 index options trading volume across strike prices. We show that, for the 1996:01--2012:12 period, ambiguity consistently forecasts negative market excess returns for horizons up to two years ahead, exhibiting a predictive ability comparable to that of the variance risk premium (VRP) and outperforming all other traditional predictors considered both in-sample and out-of-sample. Moreover, trading strategies that are based on the out-of-sample forecasting power of stock market ambiguity at both the aggregate and the portfolio level provide a mean-variance investor with significant utility gains compared to a buy-hold strategy. We find that the information embedded in stock market ambiguity is not subsumed by other option-implied

measures that proxy for variance and jump risk, or reflect investors' hedging demand. Our results are in line with equilibrium models that incorporate Bayesian learning and an elasticity of intertemporal substitution lower than one.

#### *Model Disagreement and Economic Outlook*

Daniel Andrei, UCLA, United States

Bruce Carlin, UCLA, United States

Michael Hasler, University of Toronto, Canada

*Discussant:* Ali Lazrak, UBC Sauder

We study the impact of model disagreement on the dynamics of asset prices, return volatility, and trade in the market. In our continuous-time framework, two investors have homogeneous preferences and equal access to information, but disagree about the length of the business cycle. We show that model disagreement amplifies return volatility and trading volume by inducing agents to have different economic outlooks, which generates a term structure of disagreement. Different economic outlooks imply that investors will trade even if they do not disagree about the current value of fundamentals. Also, we find that while the absolute level of return volatility is driven by long-run risk, the variation and persistence of volatility (i.e., volatility clustering) is driven by disagreement. Compared to previous studies that consider model uncertainty with a representative agent or those that study heterogeneous beliefs with no model disagreement, our paper offers a theoretical foundation for the GARCH-like behavior of stock returns.

#### **Governance (Room 103)**

##### **Session Chair: Martin Boyer, HEC Montréal**

#### *Influence of Public Opinion on Investor Voting and Proxy Advisors*

Reena Aggarwal, Georgetown University, United States

Isil Erel, Ohio State University, United States

Laura Starks, University of Texas at Austin, United States

*Discussant:* Florian Muenkel, University Of Washington

We examine the evolution in voting patterns across firms over time. We find that investors have become more independent in their voting decisions, voting less with the recommendations of management or proxy advisors. Moreover, we also find that proxy advisory recommendations have become more supportive of shareholder proposals. Our main contribution is to examine the role of public opinion in the voting changes. We find that public opinion on corporate governance issues, as reflected in media coverage and surveys, is strongly associated with investor voting, particularly mutual fund voting. In addition, even proxy advisor's recommendations are associated with public opinion. Our analysis suggests that public opinion influences corporate governance through the voting process.

#### *Investment Horizons and Information*

Kershen Huang, Bentley University, United States

Alex Petkevich, University of Toledo, United States

*Discussant:* Kee-Hong Bae, York University

We examine the relation between institutions' investment horizons on firms' financing and investment decisions. Firms with larger short-term institutional ownership use less debt financing and invest more in corporate liquidity. In contrast, firms with larger long-term institutional ownership use more internal funds, less external equity financing, and preserve

investments in long-term assets. These results are driven significantly by information, in addition to the long-term demand shock of institutional ownership. We argue that short-term (long-term) institutions collect and use value-neutral (value-enhancing) information.

#### *Lawyers in the Executive Suite: Gatekeepers as Internal Governance*

Adair Morse, UC Berkeley, United States

Wei Wang, Queen's University, Canada

Serena Shuo Wu, Queen's University, Canada

*Discussant:* Fred Bereskin, University of Delaware

Lawyers are increasingly part of executive decision-making reflecting the growing role of internal gatekeeping. We document that governance failures (frauds) occur less frequently after hiring general counsels into the executive suite. Perceived and caught frauds are 10% and 2.7% less likely to occur. We then hand-collect the career paths of executive general counsels to test how equity incentives given to gatekeepers causally impact governance and investment. Our identification comes from differences in reputational capital comparing lawyers hired from law firms and lawyers hired from positions in other corporations. In a matched difference-in-differences, we find that a one standard deviation increase in pay-for-performance sensitivity increases investment and acquisition intensity by 2.4% and 9.1% respectively. However, the same increase in equity incentives increases the likelihood of class action frauds by 13%, unwinding 66% of the gatekeeper role of improving governance. The evidence is consistent with the story that, when gatekeepers become executives, governance improvements may come at a shareholder cost in terms of risk appetite. Thus, boards use equity incentives to unwind the conservatism, but in the process, these equity incentives unwind the governance improvements of executive gatekeepers.

#### *Powerful Independent Directors*

Kathy Fogel, Suffolk University, United States

Liping Ma, University of Texas at Dallas, United States

Randall Morck, University of Alberta, Canada

*Discussant:* Martin Boyer, HEC Montréal

Shareholder valuations are economically and statistically positively correlated with more powerful independent directors, their power gauged by social network power centrality measures. Sudden deaths of powerful independent directors significantly reduce shareholder value, consistent with independent director power "causing" higher shareholder value. Further empirical tests associate more powerful independent directors with fewer value-destroying M&A bids, more high-powered CEO compensation and accountability for poor performance, and less earnings management. We posit that more powerful independent directors can better detect and counter managerial missteps because of their better access to information, their greater credibility in challenging errant top managers, or both.

**Institutions (Room 104)****Session Chair: Allen Goss, Ryerson University***A Mechanism for LIBOR*

Brian Coulter, University of Oxford, United Kingdom

Joel Shapiro, University of Oxford, United Kingdom

*Discussant:* Daniel Bergstresser, Brandeis University

The ongoing investigations into LIBOR have highlighted that the current benchmark is subject to manipulation. In this paper, we propose a mechanism that gets banks to reveal their borrowing costs truthfully at no cost to the administrator. The mechanism works even when borrowing does not occur. It has three parts. First, banks report the rates at which they can borrow. Second, a whistleblower bank may contest another bank's report by either revealing an executed transaction or stating a different rate at which the reporting bank could borrow. Third, the whistleblower's claim and the initial reported rate are confirmed or denied by the willingness of other banks to lend at those rates.

*Being Local or Going Global? Competition and Entry Barriers in the Canadian Banking Industry*

Hector Perez Saiz, Bank of Canada, Canada

Hongyu Xiao, Bank of Canada, Canada

*Discussant:* Mehdi Beyhaghi, UT San Antonio

For decades, the Canadian retail banking industry has had an oligopolistic structure, along with large variations in geographical presence among the different depository institutions. These facts could potentially be explained by the regulatory and cultural entry barriers between provinces, as well as the large heterogeneity between the "global" Big Six banks and the local players such as credit unions. In this paper, we quantify the importance of these effects in rural markets by estimating a static entry game, as in Bajari, Hong and Ryan (2010). We find that credit unions are the strongest competitors among all banks, and that entry barriers vary greatly across Canadian provinces. We also find that large, global banks do not have an advantage when competing against smaller, local players. We use these estimates to model the effect of a new regulation that would allow Desjardins, a large regional credit union, to expand across provinces. We find that this new regulation would not significantly change the competitive landscape in Canada.

*Capital Market Consequences of Index Membership*

Charles Cao, Pennsylvania State University, United States

Matthew Gustafson, Pennsylvania State University, United States

Raisa Velthuis, Pennsylvania State University, United States

*Discussant:* Tor-Erik Bakke, University of Oklahoma

We document the large capital market consequences that index membership has on small firms. Using regression discontinuity analysis, we show that joining the Russell 2000 increases institutional ownership by 4.5 percentage points (or 15%), increases the number of unique institutional owners by 35%, reduces bid-ask spreads by 30%, and doubles a firm's equity beta from 0.6 to 1.2. Indexed firms respond to these capital market changes by transitioning away from bank financing in favor of public seasoned equity offerings. We find no evidence that index inclusion affects the probability of private equity placements, public debt offerings, or convertible bond offerings.

*The Impact of Non-Traditional Activities on Risk, Performance and Capital of Canadian Banks Under Regulatory Changes*

Jean-Pierre Gueyie, ESG UQAM, Canada

Alaa Guidara, Laval University, Canada

Van Son Lai, Laval University, Canada

Issouf Soumaré, Laval University, Canada

*Discussant:* Yuriy Zabolotnyuk, Carleton University

Using the big six Canadian chartered banks quarterly financial statements and daily stock market data from 1982 to 2010, we examine the impact of non-interest income on Canadian banks' risk, performance and capital under the different major regulatory changes made to the Bank Act of Canada. We document a significant increasing trend in non-interest income with a substitution effect between non-interest income and net interest margin following the 1987 amendment to the Bank Act allowing commercial banks to acquire (or merge with) investment dealers and brokerage firms. Our results show that Canadian banks' expansion into non-traditional activities had resulted into decreased risk and increased performance benefitting from income diversification. Moreover, while adhering to capital adequacy regulation, reshuffling banks' portfolio towards non-traditional activities did not reduce Canadian banks' capital ratio, buttressing the effectiveness of capital adequacy regulation in Canada in linking banks capital allocation with their risk taking in spite of the regulation towards universal banking.

*The Interbank Network Across The Great Financial Crisis: Evidence From Italy*

Alberto Franco Pozzolo, Università degli Studi del Molise, Italy

Massimiliano Affinito, Banca d'Italia, Italy

*Discussant:* Ben Craig, Deutsche Bundesbank

We study the effects of the great financial crisis on interbank markets using the tools of network analysis. More specifically, using data on all bilateral interbank positions of Italian banks between 1998 and 2013, we analyze the impact on bank's centrality within the network of: the liquidity crisis of August 2007, Lehman's default in September 2008, the Eurosystem's Long Term Refinancing Operations that took place between 2009 and 2012, the Sovereign debt crisis of July 2011, and the announcement of the Outright Money Transactions in 2012. The results show that the 2007 liquidity crisis and especially the default of Lehman Brothers caused a strong reduction of the interconnectedness within the Italian banking sector, but that in the following years the system progressively recovered the initial level of integration, thanks also to the Eurosystem's monetary policy interventions. However, the average effect hides different impacts across banks, depending on their characteristics and initial positions within the system.

**Payout Policy (Room 105)****Session Chair: Martin Boileau, University of Colorado***Does Change in Housing Prices Influence Corporate Payout Policy?*

Sara Ding, University of San Francisco, United States

Kose John, New York University, United States

Yang Ni, Shanghai Jiao Tong University, United States

Samir Saadi, University of Ottawa, Canada

*Discussant:* Chris Mitchell, Bank of Canada

We examine whether corporate payout policy responds to changing investor tastes for non-dividend over dividend-paying stocks following an increase in housing prices. Exploiting the cross-regional dispersion in housing prices growth within the U.S., we find a significant negative effect of growth in housing prices on local firms' propensity to pay and initiate dividends, as well as on their dividend yield, payout ratio, and net payout. Such housing effect is particularly strong for small firms, young firms, volatile firms, and low profitability firms. Providing further support to our hypothesis, we report weaker market reactions to dividend changes when local housing prices increase. Our results are robust to controlling for several firm-specific variables, macro-economic variables, market sentiment, dividend premium, and after addressing potential endogeneity issue. This study is the first to establish a relationship between growth in housing prices and corporate policy decision. It also supports the view that investor's preference and firm's geographic location matter to payout policy.

*Leverage Boundaries, Financial Flexibility and Dividends*

Alan Douglas, University of Waterloo, Canada

*Discussant:* Sean Cleary, Queen's School of Business

We derive boundaries for an efficient leverage range, and illustrate how the range helps facilitate financial flexibility and dividend smoothing. The boundaries originate from discrete jumps in the cost of incentive conflicts, and evolve with cash flows and investment opportunities in a manner that enables the actual leverage employed to help motivate efficient investment and compensation choices. Firms with a limited range can become financially constrained, and face stricter credit terms to mitigate expropriation incentives following poor performance. Our analysis helps explain observed leverage ratios, dividend patterns, and debt composition, and suggests directions for empirical studies.

*Positive Asymmetry and Systematic Propensity to Save*

Alexander Vadilyev, University of New South Wales, Australia

*Discussant:* Abdul Rahman Khokhar, St Mary's University

The existing literature offers contrasting evidence regarding the corporate propensity to save cash from cash flows (referred to as the cash flow sensitivity of cash). Using an alternative empirical model, this study reveals that the cash flow sensitivity is positive and asymmetric to cash flow environments. In addition, corporate saving is systematically related to internal cash flow among both financially constrained and unconstrained firms. The results indicate that a multitude of forces, along with external financing constraints, drive corporate saving propensities. The findings support the hypotheses that firms (i) operating in different cash flow environments and (ii) having different exposures to financing frictions systematically save cash from their cash flows.

*The Real Effects of Share Repurchases*

Heitor Almeida, University of Illinois, United States

Vyacheslav Fos, University of Illinois, United States

Mathias Kronlund, University of Illinois, United States

*Discussant:* Pablo Moran, University of Calgary

We employ a regression discontinuity design to identify the real effects of share repurchases on other firm outcomes. The probability of share repurchases that increase earnings per share (EPS) is sharply higher for firms that would have just missed the EPS forecast in the absence of the repurchase, when compared with firms that "just beat" the EPS forecast. This discontinuity allows us to measure the causal effect of repurchases on other corporate policies in a fuzzy regression discontinuity (RD) framework. EPS-motivated repurchases are associated with reductions in employment and investment and a decrease in financial slack in the four quarters following the repurchase. Our evidence suggests that managers are willing to trade off investments and employment for stock repurchases that allow them to meet analyst EPS forecasts. Nevertheless, this behavior does not appear to hurt shareholders or firm performance. Stock returns and future profitability of firms that change the sign of their earnings surprises from negative to positive using repurchases are similar to those of firms that surprise positively without conducting repurchases.

*Predictable Corporate Distributions and Stock Returns*

Feng Zhang, University of Utah, United States

Hank Bessembinder, University of Utah, United States

*Discussant:* Susan Christoffersen, University of Toronto

Corporate distribution events, including stock splits, stock dividends, special dividends, and increases in regular dividends, are predictable, in part because they tend to recur at regular calendar intervals. The market fails to fully appreciate the implications of current distribution events for future distribution events and returns, as a simple trading strategy that involves purchasing firms with high predicted probabilities of recurring distribution events earns significant abnormal monthly returns. These results are distinct from previously documented return anomalies related to regular earnings and dividend announcements and return seasonality.

**International Credit Risk (Room 106)****Session Chair: Usha Mittoo, University of Manitoba***Do Foreign Listings in the U.S. Affect U.S. Firms?*

Yan Wang, McGill University, Canada

Sergei Sarkissian, McGill University, Canada

*Discussant:* Arnold Cowan, Iowa State University

The extant literature has focused on the potential impact of foreign-listed firms in the U.S. on their own performance and that of their respective local markets and firms. This paper takes a diametrically opposite stand and examines whether foreign firms by listing on or delisting from regular U.S. stock exchanges affect U.S. companies. We find that they do - negatively for listings and positively for delistings, - and the impact is especially profound for listing events. The competing U.S. firms experience severe underperformance in the short- and long-run: the average 60-day cumulative abnormal return of U.S. firms around the foreign listing date is negative 2%, while the 36-month post-listing return is negative 4.3%. Following the listings of competing foreign firms on U.S. ex-

changes, incumbent U.S. firms show declines across a variety of other metrics such as capital expenditures, growth in sales, profits, and total assets. They also experience changes in their financing policies and a reduction in analyst coverage. Subsequent tests reveal that certain market, industry, and both U.S. and foreign firm characteristics increase the adverse impact of foreign firm placements in the U.S. Our findings therefore highlight an important role of international markets in influencing financial, growth, and visibility prospects of U.S. firms and therefore the U.S. market as a whole.

*Financial Liberalization and Innovation*

Fariborz Moshirian, University of New South Wales, Australia

Xuan Tian, Indiana University, United States

Zhengyuan Wang, University of New South Wales, Australia

Bohui Zhang, University of New South Wales, Australia

*Discussant:* Pat Akey, University of Toronto

We investigate the impact of financial liberalization on technological innovation. Using a fixed effects identification strategy and a sample of 37 developed and emerging economies over the period between 1980 and 2009, we identify economic mechanisms through which financial liberalization affects innovation. Industries that are more dependent on external finance, have greater growth opportunities, are younger, have higher operational risk, and are more high-tech intensive have a disproportionately higher level of innovation output following financial market liberalization. The positive effects of financial liberalization on innovation are substantiated in countries with low implicit barriers to international investments. We provide new insights into the real effects of financial liberalization on the economy and growth.

*Lemons and Proud of it: Information Asymmetry and Risk*

*Transfer Markets*

Eric Stephens, Carleton University, Canada

James Thompson, University of Waterloo, Canada

*Discussant:* Jun Yang, Bank of Canada

In this paper we analyze asymmetric information in risk transfer markets. We extend the financial markets literature to allow for counterparty risk in an intermediated market and analyze the consequences of this risk being private information. We show that information revelation can exist in competitive equilibrium driven purely by market forces; however, the allocation is shown to be inefficient. The inefficiency is highlighted by considering the imposition of a transaction tax, which can improve welfare by encouraging more information revelation and increasing risk transfer. We conclude with a discussion on how a central counterparty may also promote transparency of counterparty risk.

*Sovereign Credit Risk and Government Effectiveness*

Alexandre Jeanneret, HEC Montréal, Canada

Jean-Claude Cosset, HEC Montréal, Canada

*Discussant:* Rémy Lambinet, Global Risk Institute

This paper investigates how the level of government effectiveness in a country affects its creditworthiness. We develop a structural model for sovereign credit risk in which the government adjusts its default and debt policies to the ability to collect and use fiscal revenues efficiently. We predict that better-governed countries exhibit lower incentives to default and thus benefit from a narrower sovereign credit spread. Moreover, the impact of government effectiveness on sovereign credit

risk is non-linear. Specifically, the effect strengthens with the level of default risk, ineffectiveness, and with a deterioration in economic conditions. Using a sample of 75 developed and emerging countries over the period 1996-2011, we provide empirical support for the model's predictions.

**IPOs, SEOs and Investment Banking (Room 107)**

**Session Chair: Imants Paeglis, Concordia University**

*Do IPO Underwriters Collude?*

Fangjian Fu, Singapore Management University, Singapore

Evgeny Lyandres, Boston University, United States

*Discussant:* Zheng Liu, Highstreet Asset Management

We propose and implement, for the first time, a direct test of the hypothesis of implicit collusion in the U.S. underwriting market against the alternative of oligopolistic competition. We construct two models of an underwriting market -- a market characterized by oligopolistic competition among IPO underwriters and a market in which banks collude in setting underwriter fees. The two models leads to different equilibrium relations between market shares and compensation of underwriters of different quality on one hand and the state of the IPO market on the other hand. We use 39 years of data on U.S. IPOs to test the predictions of the two models. Our empirical results are generally consistent with the implicit collusion hypothesis, and are inconsistent with the oligopolistic competition hypothesis.

*Underwriter Competition in Canadian Accelerated Seasoned Equity Offerings*

Erdal Gunay, University of Windsor, Canada

Nancy Ursel, University of Windsor, Canada

*Discussant:* Evan Dudley, Queen's University

Accelerated seasoned equity offerings (SEOs) are now the most common form of SEO in the United States, Canada and Europe. Canadian accelerated SEOs do not feature competitive bidding for the underwriting mandate. Using secondary and field study data, we investigate underwriter competition in the Canadian accelerated SEO market. We find competition, but not on the basis of underwriting fee. Instead underwriters choose a non-price competitive strategy of building, maintaining and defending relationships with issuers. These relationships benefit both parties: underwriters stabilize their deal flow, permitting them to efficiently use their established capacity, and issuers secure reliable access to underwriting services

*Deal Flow and the Pricing of IPOs*

Kevin Boeh, Pacific Lutheran University, United States

Craig Dunbar, Western University, Canada

*Discussant:* Parianen Veeren, University of Alberta

This study examines how the decisions that issuers and their investment banks make about IPO pricing are affected by the value of deals in registration, measured at the aggregate, industry and bank levels both as of the filing date and the offering date (in order to identify changes in the IPO pipeline over the issuance process). Examining 1888 IPOs from 1998-2011 we find evidence that measures of the IPO pipeline significantly affect pricing decisions. The evidence is mostly consistent with agency-based arguments that investment banks with large and growing pipelines of deals partially adjust prices given market information but also leave more money on the table. While harming issuers, this both helps clear their pipe-



line of deals, and attracts institutional clientele ensuring the banks can sell their backlog of deals

*Crowd Sourcing in Capital Formation: An Empirical Investigation*

Emma Li, University of Melbourne, Australia

J.Spencer Martin, University of Melbourne, Australia

*Discussant:* Azam Virani, University of Arizona

Financial institutions arise in the presence of market imperfections such as information asymmetry. Recently a new type of institution has emerged, crowd funders. These entities: 1) channel the funds to create intellectual property; 2) gather information on the quality of the project and the entrepreneur; and 3) gauge demand information directly from individuals to improve the efficiency of capital allocation. Data from crowd funder Kickstarter is a new resource for investigation of capital formation and contracting theories. A crucial advantage is that this database reports all cases where entrepreneurs try and fail to acquire funds, a feature impossible to observe in almost all other data sources. This paper empirically examines the determinants of contractual outcomes in reward-based crowd funding, with an emphasis on the role played by entrepreneur reputation and reputation formation.

*Does Overpricing to Avert IPO Withdrawal Pay? An Empirical Analysis*

Walid Busaba, Ivey Business School - Western University, Canada

Zheng Liu, Highstreet Asset Management, Canada

*Discussant:* Imants Paeglis, Concordia University

An offering that generates a weaker investor reception than anticipated by the issuer might be withdrawn unless aggressively priced—overpriced—to meet the issuer's reservation price. This paper empirically demonstrates that overpricing offerings to avert withdrawal not only increases the payoff to the underwriter from the respective deals but also enhances the underwriter's share of future IPO business. In particular, it finds that banks which engage issuers with a higher ex ante propensity to withdraw, and then aggressively price the offerings to actually avert withdrawal, experience a pronounced increase in their future IPO market share. Such reward is not experienced by underwriters which at the outset avoid engaging issuers with high likelihood of withdrawal. The paper also finds that withdrawals have more of an adverse effect on future market share than does mere overpricing. Furthermore, when overpricing is accompanied by price support during first-day of public trading, the effect on the bank's future market share is significantly less adverse than that associated with otherwise letting the offer be withdrawn.

**Investment Funds (Room 108)**

**Session Chair: David Downie, RBC Capital Markets**

*An ETF Premium Puzzle and a Market Segmentation Explanation*

Louis Piccotti, University at Albany, The State University of New York, United States

*Discussant:* Pauline Shum, Schulich School of Business, York University

This paper shows that exchange traded funds (ETFs) persistently trade at a premium to net asset value (NAV) and that

market segmentation can explain this puzzling regularity. Tracking error standard deviation is used as the measure of market segmentation. ETFs with larger tracking error standard deviations trade at higher premiums, consistent with the notion that investors are willing to pay a premium to receive liquidity and diversification benefits from holding ETFs rather than the underlying securities directly. These results are robust to investor sentiment effects. Further tests validate that tracking error standard deviation has the desirable properties of a market segmentation measure.

*Dynamic Performance of Canadian Fixed Income Mutual Funds*

Mohamed Ayadi, Brock University, Canada

Skander Lazrak, Brock University, Canada

Yusui Liao, Brock University, Canada

Robert Welch, Brock University, Canada

*Discussant:* Saurin Patel, Western University

This article uses Markov regime switching models to examine the performance of six different categories of Canadian fixed income mutual funds spanning the period from 1980 to 2011. We find strong evidence that more than one state variable is necessary to explain the dynamics of the returns on Canadian fixed income funds. In this dynamic setting, Canadian bond fund alphas are generally negative, which suggests weak selection abilities. There is also evidence that Canadian fixed income fund portfolio managers are successful market timers who shift portfolio weights between risky and riskless financial assets according to expected market conditions. Conversely, Canadian inflation protected funds, Canadian long-term fixed income funds and Canadian money market funds do not possess market timing ability. These funds' managers generally do not achieve positive performance by actively managing their portfolios. We also report that Canadian fixed income fund portfolios perform asymmetrically under different economic regimes. In particular, these portfolio managers demonstrate poorer selection skills during recessions. Finally, we demonstrate that a multivariate regime-switching model is superior to univariate models given the dynamic market conditions and the correlation between fund portfolios.

*Endogenous Credit Constraints and Household Portfolio Choices*

Kyoung Jin Choi, Haskayne School of Business, University of Calgary, Canada

Hyung Keun Koo, Ajou University, Republic Of Korea

Byung Hwa Lim, Suwon University, Republic Of Korea

Jane Yoo, Ajou University, Korea, Republic Of

*Discussant:* Michael Brennan, Anderson School UCLA

This paper presents a continuous-time consumption-investment model for a household without debt enforcement. Using a duality approach, we derive closed-form solutions for optimal consumption and portfolio policies and for endogenous credit (debt) limits over time. Our model suggests that current income levels, particularly wages, play an important role in determining credit limits. However, current wealth or net worth including financial assets do not affect credit limits. An increase in the income growth rate or a decrease in income volatility leads to an increase in the household's credit limit. We also show that investments in risky assets are endogenously related to the procyclical credit limit, in contrast to the countercyclical Sharpe ratio. Finally, all these results generate the heterogeneous investment behavior among households: The risky asset holdings given the fixed level of wealth is higher for

Saturday, September 13, 2014

8.00 AM - 9.30 AM

the rich during the downturn with a higher Sharpe ratio than during the boom with a lower Sharpe ratio, while they are lower for the poor during the downturn than during the boom. Finally, we empirically test our theoretical prediction using the Survey of Consumer Finances data.

*Management of Flow Risk in Mutual Funds*

Martin Rohleder, University of Augsburg, Germany

Dominik Schulte, University of Augsburg, Germany

Marco Wilkens, University of Augsburg, Germany

*Discussant:* Timothy Simin, The Pennsylvania State University

This paper is the first to relate the investment practices of equity mutual funds to their management of flow risk induced by investors' in- and outflows. Using a matched sample of 3,075 actively managed US domestic equity funds from the CRSP mutual fund database and the SEC's N-SAR filings we detect cross-sectional differences in the funds' response to flow risk from 1996 to 2012. Specifically, we find that in contrast to non-users, users of complex instruments are not significantly impacted by flow risk. By using derivatives and leverage they are able to offset the negative effects of adverse investor flows on fund performance helping them to gain abnormal returns of 0.23 percentage points per year higher than non-users. Hence, superior flow management ability is a valuable skill in managing funds.

*Mutual Fund Competition, Managerial Skill, and Alpha Persistence*

Gerard Hoberg, University of Maryland, College Park, United States

Nitin Kumar, Indian School of Business, India

Nagpurnanand Prabhala, University of Maryland, College Park, United States

*Discussant:* Fabio Moneta, Queens University

Whether fund managers can generate positive alpha and do so persistently are key questions in the mutual fund literature. We propose a new economic force that limits persistence in alpha: competition from other funds that cater to similar segments of investor demand. We make three contributions. First, we use new spatial methods to identify the dynamic competition faced by funds. Second, we develop a new measure of fund manager skill, viz., the ability of a fund to beat its spatially close rivals. The skill measure predicts alphas for at least four quarters ahead. Finally, we show that alpha is persistent only when a fund has few rivals. This new persistence is not driven by diseconomies of scale, is economically large, and lasts up to four quarters. Thus, besides the scale diseconomies emphasized by Berk and Green (2004), competition between funds is a potent force that limits the persistence of alpha.

## 3.30 PM - 4.00 PM

Refreshment Break (Colonel By Foyer)

# Saturday, September 13, 2014

## 4.00 PM - 5.30 PM

Plenary Lecture (Room 214)

**Session Chair: Gordon Sick, NFA 2014 Program Chair and University of Calgary**

Anil Shivdasani

Wachovia Distinguished Professor of Finance

Kenan-Flagler Business School

University of North Carolina

*NFA 2014 Plenary Lecture on Corporate Governance*

Professor Shivdasani will review important developments in the growing field of corporate governance, with a focus on research on boards of directors and executive compensation. He will discuss how corporate governance impacts firms' financial policies, performance, and valuation. He will review recent findings in the field including implications of corporate governance for financial institutions and financial reform and highlight potentially fruitful areas for future research.

## 6.00 PM - 9.30 PM

Dinner (Sponsored by Scotiabank) (Trillium Ballroom)

# Sunday, September 14, 2014

## 7.00 AM - 8.00 AM

Breakfast (Colonel By Foyer)

## 8.00 AM - 9.30 AM

Equity Valuation (Room 101)

**Session Chair: William Rentz, University of Ottawa**

*Aggregation of Information About the Cross Section of Stock Returns: A Latent Variable Approach*

Nathaniel Light, Temple University, United States

Denys Maslov, University of Texas at Austin, United States

Oleg Rytchkov, Temple University, United States

*Discussant:* Bruno Feunou, Bank of Canada

We propose a new approach for estimating expected returns on individual stocks from a large number of firm characteristics. We treat expected returns as latent variables and develop a procedure that filters them out using the characteristics as signals and imposing restrictions implied by any asset pricing model with one or several risk factors. The estimates of expected returns obtained by applying our method to twenty six asset pricing anomalies generate a surprisingly wide cross-sectional dispersion of realized returns. Our results provide evidence of strong commonality in the anomalies. The use of portfolios based on the filtered expectations as test assets increases the power of asset pricing tests.

*Investment and the Term Structure of Stock Returns*

Sandra Mortal, University of Memphis, United States

Michael Schill, University of Virginia, United States

*Discussant:* Fatma Saryal, Queen's University

In this paper we explore the momentum and reversal regularity in the term structure of stock returns. We show that these patterns in stock returns depend highly on leads and lags in firm investment such that there is no residual momentum or reversal effect in stock returns independent of that associated with firm investment. Our results also provide an explanation for the delay in momentum effects observed by Novy-Marx (2012). We propose new explanations consistent with our findings for the large literature on the momentum and reversals regularities.

*Conditioning Information and Asset Pricing Anomalies in Multivariate Tests of Financial Integration*

Marie-Claude Beaulieu, Laval University, Canada

Marie-Hélène Gagnon, Laval University, Canada

Lynda Khalaf, Carleton University, Canada

*Discussant:* William Rentz, University of Ottawa

This paper develops and tests asset pricing model based implications for financial market integration in North America, when there is conditioning information in the form of a set of lagged instruments. Single and multi-factor time series setups are tested that track factor sensitivities rather than only risk premiums. We assess robustness to systematic risk, using domestic and international Fama and French risk factors, augmented with momentum. Tested hypotheses characterize partial, mild and strong degrees of integration. We show that conclusive results that support mild integration can be reached regardless of the considered risk measures. We also provide evidence, from an international perspective, that conditioning does not explain anomalies out, and more specifically that both conditional and unconditional international market models lack empirical support.

**Governance (Room 103)**

**Session Chair: Wendy Rotenberg, University of Toronto**

*A Theory of Family Firms*

Jin Yu, The University of New South Wales, Australia

Palve Radicevic, The University of New South Wales, Australia

*Discussant:* Melissa Toffanin, Ryerson University

We develop a financial contracting model to analyze the effect of family control on corporate risk-taking. The ex post optimal (second best) risk-taking policy maximizes the controlling party's interest and usually fails to internalize those of other claimholders. This may give rise to inefficiency as financiers capitalize the risk-taking policy into financial contracts and, therefore, the ex ante optimal (first best) risk-taking has to maximize the total firm value. We show that family control emerges as an optimal mechanism because a family owner's propensity to take on risk features both an equity component (equity ownership stake) and a debt-like component (defaultable private benefits). Therefore, the optimal family ownership is an outcome of a trade-off between alleviating over-conservatism and reducing excessive risk-taking. The model

generates several novel empirical predictions and policy implications.

*The Differences between Public and Private Firms: Agency, Financing and Technology*

Nan Xiong, Carnegie Mellon University, United States

*Discussant:* Iraj Fooladi, Dalhousie University

I quantify the economic differences in manager-shareholder conflicts and financing cost between U.S. public and private firms by estimating a dynamic model of investment. My estimates indicate that public and private firms differ significantly in agency and financing frictions. Public firm value would rise by 3.52% and private firm value would rise by 0.65% if we eliminated all agency conflicts. Privately-held firms face external financing costs equal to 15.4% of capital, and public firms face financing costs of 7.2% of capital raised. The estimated financing frictions decrease private firm value by 3.63% and public firm value by 1.15%. My estimates show that the differences in public and private firms are not simply due to agency and financing frictions, since the productivity shock volatility and the capital stock adjustment cost also play substantial roles in explaining the differences between public and private firms. The model also provides insight why privately-held firms do not go public nor why publicly held firms do not go private.

*Who Captures the Power of the Pen?*

Jiaxing You, Xiamen University, China

Bohui Zhang, UNSW Australia, Australia

Le Zhang, UNSW Australia, Australia

*Discussant:* Paul Calluzzo, Queen's University

We study how political capture affects the corporate governance role of the media. Relying on a unique media market in China that is characterized by the prevalence of both state-controlled and market-oriented media, we manually construct a comprehensive financial news sample containing 80,008 articles during the 2004-2010 period and provide evidence that negative coverage by the market-oriented media significantly increases the chance of forced top executive turnover, whereas similar coverage by the state-controlled media has no such impact. A multi-pronged approach that includes an instrumental variable test, an exogenous event, firm fixed effects, and change-in-change specifications provides positive evidence of the causal link. Further analysis reveals that the disciplinary effect of the market-oriented media is stronger for firms that are less likely to be influenced by political capture, such as non-state-owned firms or firms located in provinces with good institutions.

*Spillover Effects from US Class Action Lawsuits: Evidence from Foreign Firms Cross-listed in the US*

Yi Ding, Queen's University, Canada

Louis Gagnon, Queen's University, Canada

Xiaoqiao Wang, Queen's University, Canada

*Discussant:* Wendy Rotenberg, University of Toronto

In this paper, we document that US cross-listed firms experience negative return spillovers in the three-day event window centered on the filing of US class action lawsuits launched against their country peers. This spillover effect is both economically large (-0.139%) and statistically significant at the 1% level. We find that firms domiciled in jurisdictions endowed with weak institutions, as well as firms monitored by

weaker reputational intermediaries, are considerably more vulnerable to these adverse spillovers. Our evidence demonstrates that the mitigating power of external market monitors is especially high for firms domiciled in countries endowed with weak institutions. Foreign firms choosing to cross-list their shares in the US can reduce their vulnerability to this class action lawsuit spillover risk by selecting higher quality reputational intermediaries and by communicating with investors more effectively.

## Empirical Issues (Room 104)

**Session Chair: Ilias Tsiakas, University of Guelph**

### *Do Options Volatility Skew and Spread Really Predict Stock Returns?*

Jason Wei, University of Toronto, Canada

*Discussant:* Maksim Isakin, University of Calgary

This study shows that the predictability of stock returns established in Xing, Zhang and Zhao (2010), and Cremers and Weinbaum (2010) is spurious and thus one cannot conclude that volatility skew and spread contain information for future stock returns. The apparent predictive power of volatility skew for future earnings surprises is also spurious. The spurious predictability results from the persistence in the predicted (i.e., stock returns and earnings surprises) and the predictors (i.e., the volatility skew and spread). Although the study only focuses on two representative studies, it is meant to send a broader message, namely, the onus of proof shouldn't be taken lightly if/when one attempts to conclude that options contain information for future returns or the outcome of other corporate events. At the very minimum, every effort should be made to ensure that the claimed causality and predictability are not spurious due to various hidden dynamics in the predicted and the predictors.

### *Maximum Likelihood Estimation of the Equity Premium*

Efstathios Avdis, University of Alberta, Canada

Jessica Wachter, University of Pennsylvania, United States

*Discussant:* Alex Maynard, University of Guelph

The equity premium, namely the expected return on the aggregate stock market less the government bill rate, is of central importance to the portfolio allocation of individuals, to the investment decisions of firms, and to model calibration and testing. This quantity is usually estimated from the sample average excess return. We propose an alternative estimator, based on maximum likelihood, that takes into account information contained in dividends and prices. Applied to the postwar sample, our method leads to an economically significant reduction from 6.4% to 5.1%. Simulation results show that our method produces tighter estimates under a range of specifications.

### *Does Realized Skewness Predict the Cross-Section of Equity Returns?*

Diego Amaya, UQAM, Canada

Peter Christoffersen, Rotman, CBS and CREATES, Canada

Kris Jacobs, University of Houston and Tilburg University, United States

Aurelio Vasquez, ITAM Mexico City, Mexico

*Discussant:* Ilias Tsiakas, University of Guelph

We use intraday data to compute weekly realized variance, skewness, and kurtosis for equity returns and study the realized moments time-series and cross-sectional properties. We investigate if this week's realized moments are informative for the cross-section of next week's stock returns. We need a very strong negative relationship between realized skewness and next week's stock returns. A trading strategy that buys stocks in the lowest realized skewness decile and sells stocks in the highest realized skewness decile generates an average weekly return of 24 basis points with a t-statistic of 3.65. Our results on realized skewness are robust across a wide variety of implementations, sample periods, portfolio weightings, and firm characteristics, and are not captured by the Fama-French and Carhart factors. We find some evidence that the relationship between realized kurtosis and next week's stock returns is positive, but the evidence is not always robust and statistically significant. We do not find a strong relationship between realized volatility and next week's stock returns.

## Behavioural Finance (Room 105)

**Session Chair: Alli Nathan, Providence College**

### *Mutual Fund Window Dressing: Prevalence, Flow Reaction, and Limited Attention*

Xiaolu Wang, Iowa State University, United States

*Discussant:* Lisa Kramer, University of Toronto

We estimate the prevalence of mutual fund window dressing and examine whether and how investors respond to disclosed portfolios to provide window dressing incentives to fund managers. Our estimation results confirm the existence of the window dressing practice. The flow reaction tests show that investors positively react to the largest ten holdings of a disclosed portfolio and that a higher number of big stocks among the largest-10 exacerbates the reaction, consistent with the hypothesis that due to limited attention, investors focus on certain salient features of a portfolio to evaluate managers. Finally, we provide evidence that managers realize investors' bias and window dress their portfolios accordingly.

### *Peer Pressure: Does Social Interaction Explain the Disposition Effect?*

Rawley Heimer, Federal Reserve Bank of Cleveland, United States

*Discussant:* Andreanne Tremblay Simard, York University

This paper provides evidence that social interaction contributes to the disposition effect. I analyze a unique database drawn from a social network for retail traders. Participating in the social network requires an agreement between the social network and a trader's brokerage. The introduction of roughly fifty retail-specific brokerages into the social networking environment was staggered over time, which provides an opportunity to causally identify the impact of social interaction. Traders are almost twice as susceptible to the disposition effect

after entering the social network. Relative to the formation of a simulated network, traders who are similarly prone to the disposition effect tend to form friendships with one another, which suggests a feedback effect. A number of alternative theories -- adverse selection, transaction costs, blame delegation, learning, and a belief in mean-reversion -- while valid on their own, are unlikely to explain the detrimental impact of social influence. The social network increases (has little effect on) the propensity to hold onto losses (gains), which supports the simplest explanation for the disposition effect: individuals are loss-averse, and it can be even more painful to admit defeat in the presence of others.

#### *The Blame Game*

Dexin Zhou, Emory University, United States

*Discussant:* Stéphane Chrétien, Université Laval

Executives often blame external factors for their own bad performance. I propose a textual analysis-based measure to detect when corporate executives blame bad performance on external factors such as industry and economy (referred as BLAME measure). Using this methodology to analyze quarterly earnings announcement conference call transcripts, I find that: (1) these attribution behaviors are negatively related to the financial performance, indicating a higher desire to attribute bad performance to external factors; (2) a high BLAME measure predicts low returns subsequent to the conference call date after controlling for the tone of the transcripts and other known predictive variables. The hedged portfolio that takes long positions in companies with low BLAME measure and short positions in companies with high BLAME measure generates abnormal returns as high as 7% per year; (3) BLAME measure negatively predicts SUE and analyst recommendation revision in the subsequent quarter, indicating underreaction to firm-specific negative information; (4) a high BLAME measure reduces turnover performance sensitivity. Overall, the evidence suggests that investors underreact to negative information when managers attribute bad performance to negative external factors.

#### **Energy Derivatives (Room 106)**

**Session Chair: Kenneth Vetzal, University of Waterloo**

##### *Macroeconomic Drivers of Crude Oil Futures Risk Premia*

Ron Alquist, Bank of Canada, Canada

Gregory H. Bauer, Bank of Canada, Canada

Antonio Diez de los Rios, Bank of Canada, Canada

*Discussant:* Gabriel Power, Université Laval

We derive an affine term structure model to assess how macroeconomic risks drive risk premia on short and long-term crude oil futures. New to the literature, we construct the term structure of convenience yields to obtain insight into the theory of storage. While the short-term convenience yield is related to contemporaneous crude oil scarcity, the slope of the curve reflects anticipated changes in the availability of future physical oil. Macroeconomic risks are unspanned by both the risk free and convenience yield term structures. Both the unspanned macroeconomic risks and the slope of the convenience yield curve are important drivers of the oil futures risk premia.

#### *Short-Term Hedging For An Electricity Retailer*

Debbie Dupuis, HEC Montréal, Canada

Genevieve Gauthier, HEC Montréal, Canada

Frederic Godin, HEC Montréal, Canada

*Discussant:* Perry Sadorsky, York University

A dynamic global hedging procedure making use of futures contracts is developed for a retailer of the electricity market facing price, load and basis risk. Statistical models reproducing stylized facts are developed for the electricity load, the day-ahead spot price and futures prices in the Nord Pool market. These models serve as input to the hedging algorithm, which also accounts for transaction fees. Backtests with market data from 2007 to 2012 show that the global hedging procedure provides considerable risk reduction when compared to hedging benchmarks found in the literature.

#### *The Price of Oil Risk*

Steven Baker, University of Virginia, United States

Bryan Routledge, Carnegie Mellon University, United States

*Discussant:* Alexander David, University of Calgary

We solve a Pareto risk-sharing problem with heterogeneous agents with recursive utility over multiple goods. We use this optimal consumption allocation to derive a pricing kernel and the price of oil and related futures contracts. This gives us insight into the dynamics of risk premia in commodity markets for oil. As an example, in a calibrated version of our model we show how rising oil prices and falling oil risk premium are an outcome of the dynamic properties of the optimal risk sharing solution. We also compute portfolios that implement the optimal consumption policies and demonstrate that large and variable open interest is a property of optimal risk sharing.

#### **Capital Structure and Debt (Room 107)**

**Session Chair: Laurence Booth, University of Toronto**

##### *Common Factors in Corporate Capital Structure*

Murray Frank, University of Minnesota Twin Cities, United States

Tao Shen, Tsinghua University, China

*Discussant:* Redouane Elkamhi, University of Toronto

This paper reexamines the controversy over capital structure adjustment speed. We show that firms move leverage towards target much faster than generally understood. To do this we use reduced rank regressions to extract 4 common factors for corporate leverage using 146 variables, including value weighted aggregates of standard firm attributes, and macroeconomic variables. Firm specific factor loadings on all of these are estimated. The model provides estimates of time varying leverage targets. More than half of the leverage variation by the median firm is explained, and there is significant predictive ability for several years out-of-sample. Firms actively adjust both debt and equity to move leverage in the direction of the estimated targets. A straw man null hypothesis of purely random financing actions is easily rejected. Slow speeds of adjustment reported in previous studies may reflect the use of static leverage targets while firms actually care about time varying targets.

*Financing as a Supply Chain: The Capital Structure of Banks and Borrowers*

Will Gornall, Stanford University, United States

Ilya Strebulaev, Stanford University, United States

*Discussant:* Egor Matveyev, University of Alberta

We develop a model of the joint capital structure decisions of banks and their borrowers. Strikingly high bank leverage emerges naturally from the interplay between two sets of forces. First, seniority and diversification reduce bank asset volatility by an order of magnitude relative to that of their borrowers. Second, previously unstudied supply chain effects mean that highly levered financial intermediaries can offer the lowest interest rates. Low asset volatility enables banks to take on high leverage safely; supply chain effects compel them to do so. Firms with low leverage also arise naturally, as borrowers internalize the systematic risk costs they impose on their lenders. Because risk assessment techniques from the Basel II framework underlie our model, we can quantify the impact capital regulation and other government interventions have on leverage and fragility. Deposit insurance and the expectation of government bailouts increase not only bank risk taking, but also borrower risk taking. Capital regulation lowers bank leverage but can lead to compensating increases in the leverage of borrowers, which can paradoxically lead to riskier banks. Doubling current capital requirements would reduce the default risk of banks exposed to high moral hazard by up to 90% with only a small increase in bank interest rates.

*Reputation and Loan Contract Terms: the Role of Principal Customers*

Ling Cen, University of Toronto, Canada

Sudipto Dasgupta, HKUST, Hong Kong

Redouane Elkamhi, University of Toronto, Canada

Raunaq Pungaliya, Sungkyunkwan University, Republic Of Korea

*Discussant:* Einar Kjenstad, University of Rochester, Simon School of Business

Principal customers have strong incentives and ability to monitor suppliers to ensure supply-chain stability; consequently, the existence of long-term relationships with principal customers allows suppliers to build reputation that spills over to other markets. We argue that banks “free-ride” on the reputation building and cross monitoring effects of principal customers, resulting in smaller loan spreads and looser loan covenants due to lower bonding and monitoring costs. We carefully address endogeneity concerns via a variety of tests and find consistent results. Our study suggests that the presence of non-financial stakeholders can have important effects on the decisions of financial stakeholders.

**Microstructure (Room 108)**

**Session Chair: Akiko Watanabe, University of Alberta**

*Dynamic Dispersed Information and the Credit Spread Puzzle*

Elias Albagli, Central Bank of Chile, Chile

Christian Hellwig, Toulouse School of Economics, France

Aleh Tsyvinski, Yale University, United States

*Discussant:* Murray Carlson, University of British Columbia

We develop a dynamic nonlinear, noisy REE model of credit risk pricing under dispersed information that can theoretically and quantitatively account for the credit spread puzzle.

The first contribution is a sharp analytical characterization of the dynamic REE equilibrium and its comparative statics. Second, we show that the nonlinearity of the bond payoff in the environment with dispersed information and limits to arbitrage leads to underpricing of corporate debt and to spreads that over-state the probability of default. This underpricing is most pronounced for high investment grade, short maturity bonds. Third, we calibrate to the empirical data on the belief dispersion and show that the model generates spreads that explain between 16 to 42% of the empirical values for 4-year high investment grade, and 35 to 46% for 10-year, high investment grade bonds. These magnitudes are in line with empirical estimates linking bond spreads to empirical measures of investor disagreement, and substantially higher than most structural models of credit risk. The primary contribution of our paper in moving NREE models towards a more realistic asset pricing environment - dynamic, nonlinear, and quantitative - that holds significant promise for explaining empirical asset pricing puzzles.

*High Frequency Trading, Price Efficiency, and the Cost of Immediacy: Evidence from the 2008 Short Sale Ban*

Jonathan Brogaard, University of Washington, United States

Terrence Hendershott, University of California at Berkeley, United States

Ryan Riordan, University of Ontario Institute of Technology, United States

*Discussant:* Andriy Shkilko, Wilfrid Laurier University

We examine the effects of high frequency traders (HFTs) on liquidity and price efficiency using the September 2008 short sale ban as an exogenous event. To disentangle the separate impacts of short selling by HFTs and non-HFTs (nHFTs) we use an instrumental variables approach exploiting the difference in the ban's cross sectional impact. HFTs' liquidity demand is responsible for the ban's negative liquidity and price efficiency effects. HFTs' liquidity supply has a positive impact on liquidity and price efficiency. Overall, we find that HFTs' demand effects outweigh HFTs' supply effects. HFTs decrease liquidity and increase both the information and transitory volatility of prices, while nHFTs increase liquidity and dampen both types of volatility. The findings illustrate a tradeoff when evaluating the contribution of HFTs to market quality: HFTs' liquidity demand impounds information into prices, but also reduces liquidity and adds noise to prices, while HFTs' liquidity supply increases liquidity and has little effect on volatility.

*Comparing Trade Flow Classification Algorithms in the Electronic Era: the Good, the Bad, and the Uninformative*

Marios Panayides, University of Pittsburgh, United States

Thomas Shohfi, University of Pittsburgh, United States

Jared Smith, University of Pittsburgh, United States

*Discussant:* Akiko Watanabe, University of Alberta

We use recent low-latency data from Euronext Paris for which we can identify the true trade initiator to test the performance of the Lee and Ready (1991) and tick test classification algorithms, as well as the newly developed bulk volume classification method (Easley et al. (2013)). We find that, despite the use of quote data, Lee and Ready underperforms the other methods, particularly during intervals of high trade and/or quote frequency. The bulk volume algorithm (BVC) demonstrates superiority with respect to data efficiency, accu-

racy, and the ability to capture informative trade flow. Consistent with Chakrabarty et al (2013), we find that the BVC benefits from the netting of misclassified trades and it underperforms the "bulk" tick test at comparable bar sizes. Nevertheless, we show that the magnitude of this accuracy underperformance is driven by systematic biases related to both volume and time bar choices, as well as the characteristics of the price change distribution. We explore several BVC calibrations that significantly mitigate, and in some cases alleviate, the accuracy advantage of the bulk tick test while capturing the data efficiency and informational advantage of the BVC.

## 9.30 AM - 10.00 AM

Refreshment Break (Colonel By Foyer)

## 10.00 AM - 11.30 AM

Equity Valuation (Room 101)

Session Chair: Carlton Osakwe, Mount Royal University

*Asset Pricing and the 1%*

Alexis Akira Toda, University of California, San Diego, United States

Kieran Walsh, Yale University, United States

*Discussant:* Gregory Bauer, Bank of Canada

We find that when the income share of the top 1% income earners in the U.S. rises above trend by one percentage point, subsequent one year market excess returns decline on average by 5.6%. This negative relation remains strong and significant even when controlling for classic return predictors such as the price-dividend and the consumption-wealth ratios. To explain this stylized fact, we build a general equilibrium asset pricing model with heterogeneity in wealth and risk aversion across agents. Our model admits a testable moment condition and a novel two factor covariance pricing formula, where one factor is inequality. Intuitively, when wealth shifts into the hands of rich and risk tolerant agents, average risk aversion falls, pushing down the risk premium. Our model is broadly consistent with data and provides a novel positive explanation of both market excess returns over time and the cross section of returns across stocks.

*Perceived Crash Risk and Cross-Sectional Stock Returns*

George P Gao, Cornell University, United States

Zhaogang Song, Federal Reserve Board, United States

Liyan Yang, University of Toronto, Canada

*Discussant:* Mark Potter, Babson College

The ex ante perception of an individual stock crash can substantially deviate from the stock crash risk implied from ex post historical observations. We use individual equity and S&P 500 index out-of-the-money puts to measure such perceived crash risk: co-crash, a systematic component capturing the covariation between a stock's crash perception and the market's crash perception; and idiosyncratic crash, a stock-specific component capturing the part of stock's crash perception unexplained by the market. Perceived crash risk is strongly priced, with the average annual Sharpe ratios of long-short hedge portfolios formed on perceived co-crash and idiosyn-

cratic crash risks being 0.9 and 1.1, respectively. We construct a simple asset pricing model to rationalize our findings. We also show that perceived crash risk largely helps explain returns on the quality-minus-junk, the betting-against-beta, and the profitable-minus-unprofitable portfolios.

*Is Idiosyncratic Volatility Risk Priced? Evidence from the Physical and Risk-Neutral Distributions*

Ali Boloorforoosh, Concordia University, Canada

*Discussant:* Carlton Osakwe, Mount Royal University

We use simultaneous data from equity, index and option markets in order to estimate a single factor market model in which idiosyncratic volatility is allowed to be priced. We model the index dynamics' P-distribution as a mean-reverting stochastic volatility model as in Heston(1993), and the equity returns as single factor models with stochastic idiosyncratic volatility terms. We derive theoretically the underlying assets' Q-distributions and estimate the parameters of both P- and Q-distributions using a joint likelihood function. We document the existence of a common factor structure in option implied idiosyncratic variances. We show that the average idiosyncratic variance, which proxies for the common factor, is priced in the cross section of equity returns, and that it reduces the pricing error when added to the Fama-French model. We find that the idiosyncratic volatilities differ under P- and Q-measures, and we estimate the price of this idiosyncratic volatility risk, which turns out to be always significantly different from zero for all the stocks in our sample. Further, we show that the idiosyncratic volatility risk premiums are not explained by the usually equity risk factors. Finally, we explore the implications of our results for the estimates of the conditional equity betas.

Governance (Room 103)

Session Chair: Lynnette Purda, Queen's University

*Institutional Investment Horizon, the Information Environment and Firm Credit Risk*

Lorne Switzer, Concordia University, Canada

Jun Wang, Concordia University, Canada

*Discussant:* Mohammad Rahaman, Saint Mary's University

We provide evidence that the impact of the investment horizon of institutional investors on the credit risk of U.S. industrial firms is both statistically and economically significant. Ceteris paribus, a one percent increase in the ownership by short-term (long-term) institutions leads to a 0.227 (.065) percentage point decrease (increase) of a firm's credit spread. However, during the financial crisis period, higher ownership by long-term institutional investors is associated with lower credit risk. Hence, long-term institutions play an important role in enhancing financial stability during the crisis period by mitigating risk. These results are robust to estimation with endogenous institutional ownership.

*Explaining The Association Between Monitoring And Controversial CEO Pay Practices: An Optimal Contracting Perspective*

Pierre Chaigneau, HEC Montréal, Canada

Nicolas Sahuguet, HEC Montréal, Canada

*Discussant:* Alexander Dyck, University of Toronto

Puzzling associations between low levels of ownership concentration and CEO pay practices such as pay-for-luck, a low pay-performance sensitivity, a more asymmetric pay-



performance relation, and high salaries, have been documented. They have been interpreted as evidence that CEO pay is not set optimally. We explain these associations in a model in which firms design contracts optimally to attract and retain CEOs. The results are driven by the matching process: firms with greater ownership concentration have a higher monitoring capacity, and can better handle the downside risk of hiring CEOs with more uncertain ability. The outside option of these CEOs is more sensitive to their performance net of luck, which generates a higher pay-performance sensitivity and less pay-for-luck. If managerial skills are sufficiently transferable across firms and the cost of CEO dismissal is sufficiently high, these CEOs are less valuable and therefore receive relatively lower salaries

*Director Network and IPO Performance*

Yi Feng, Ryerson University, Canada  
Keke Song, Dalhousie University, Canada  
Yisong Tian, York University, Canada

*Discussant:* Lynnette Purda, Queen's University

Director network is an important determinant of IPO performance. Firms with a well-connected board of directors are more likely to experience a higher first-day stock return, a greater probability of upward revision to the offer price, and larger proceeds from the IPO. Directors with extensive social, educational and professional networks help generate more interest in the IPO from informed (e.g., institutional) investors and facilitate information exchange between the IPO firm and informed investors. Indeed, the value of these connections is manifested in attracting and retaining more institutional investors to the IPO.

**Institutions (Room 104)**

**Session Chair: Kent Womack, University of Toronto**

*Do Analysts' Preferences Affect Corporate Policies?*

Francois Degeorge, University of Lugano, Switzerland  
Francois Derrien, HEC Paris, France  
Ambrus Kecskes, York University, Canada  
Sebastien Michenaud, Rice University, United States

*Discussant:* Mohamed Al Guindy, Queen's University

Equity research analysts tend to cover firms about which they have favorable views. We exploit this tendency to infer analysts' preferences for corporate policies from their coverage decisions. We then use exogenous analyst disappearances to examine the effect of these preferences on corporate policies. After an analyst disappears, firms change their policies in the direction opposite to the analyst's preferences. The influence of analyst preferences on policies is stronger for firms for which analyst coverage is likely to matter more: young firms, and firms with higher market valuations. Our results suggest that firms choose their corporate policies, in part, to be consistent with the preferences of their analysts.

*Investor Attrition and Mergers in Mutual Funds*

Susan Christoffersen, University of Toronto and Copenhagen Business School, Canada  
Haoyu Xu, University of Toronto, Canada

*Discussant:* Laleh Samarbakshsh, Ryerson University

We explore the properties of equity mutual funds experiencing a large loss of assets and argue these funds are left with a group of price-insensitive investors who exhibit different

flow characteristics than funds in early growth phases. Funds with higher attrition exhibit lower flow-performance sensitivities and managers respond to increased attrition levels by increasing fees above current levels. We also examine whether the stability of a self-selected investor base makes for an attractive acquisition. Consistent with this intuition, high attrition funds and families are more likely to become merger targets even after controlling for poor performance.

*Rollover Risk and the Maturity Transformation Function of Banks*

Teodora Paligorova, Bank of Canada, Canada  
Joao Santos, Federal Reserve Bank of New York and NOVA, United States

*Discussant:* Michael King, Ivey Business School at Western University

This paper shows that banks that increase their use of short-term funding engage in less maturity transformation in an attempt to decrease their exposure to rollover risk. These banks shorten both the maturity of newly issued loans as well as the maturity of their portfolio of loans. We also find that the loan yield curve becomes steeper with banks' increasing use of short-term funding. The loan maturity shortening is driven by banks and affects borrowers' financing choices--they turn to the bond market for long-term funding. To the extent that borrowers do not manage to compensate for the 'undesirable' shortening of loan maturities by going to the bond market, they may become more exposed to rollover risk due to banks. This potential synchronization of banks' and borrowers' rollover risk can be a source of financial instability once short-term funding suddenly disappears.

**Behavioural Finance (Room 105)**

**Session Chair: Lisa Kramer, University of Toronto**

*Informational Herding by Institutional Investors: Evidence from Analyst Recommendations*

Jonathan Clarke, Georgia Institute of Technology, United States  
Chayawat Ornthanalai, University of Toronto, Canada  
Ya Tang, Peking University, China

*Discussant:* Anna Scherbina, UC Davis

We study daily institutional herding around the release of sell-side analyst recommendations. We find that institutional herding on the recommendation release date is short-lived and specific to high turnover stocks suggesting that institutional investors herd during periods of significant disagreement. We do not find that institutional herding around recommendations destabilizes prices, but rather herding helps to speed up the information incorporated into stock prices. Consistent with investigative herding models, our results suggest that institutional investors herd upon the arrival of correlated information signals, and that such action improves market efficiency. This is in clear contrast with non-informational herding models, which are associated with subsequent return reversals.

*Stock Market Overreaction to Management Earnings Forecasts*

Jean-Sebastien Michel, HEC Montreal, Canada

*Discussant:* Mark Kamstra, York University

I hypothesize that the stock market overreacts to management earnings forecasts. I find that negative management

forecast surprises lead to a -5.9% abnormal return around the forecast and a 1.9% correction in the 2-month period after earnings are announced. Positive surprises work in the opposite direction, with a 1.9% abnormal return and a -1.7% correction. The level of the stock market overreaction varies depending on forecast and firm characteristics, but the marginal impact remains the same: a 1% change in the stock market reaction around the forecast is associated with a 0.4% correction. These findings are consistent with the idea that investors overweight their recent experience in situations of increased uncertainty, leading to stock market overreaction.

*The Social Dynamics of Performance*

Julien Cujean, University of Maryland, United States

*Discussant:* Chi Liao, University of Toronto

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.

**Derivatives (Room 106)**

**Session Chair: Don Cyr, Brock University**

*Measuring Uncertainty in Monetary Policy Using Implied Volatility and Realized Volatility*

Bo Young Chang, Bank of Canada, Canada

Bruno Feunou, Bank of Canada, Canada

*Discussant:* Alexander David, University of Calgary

We measure uncertainty surrounding the central bank's future policy rates using implied volatility computed from interest rate option prices and realized volatility computed from intraday prices of interest rate futures. Both volatility measures show that uncertainty decreased following the most important policy actions taken by the Bank of Canada as a response to the financial crisis of 2007-08, such as the conditional commitment of 2009-10, the unscheduled cut in the target rate coordinated with other major central banks, and the introduction of term purchase and resale agreements. We also find that, on average, uncertainty decreases following the Bank of Canada's policy rate announcements. Furthermore, our measures of policy rate uncertainty improve the estimation of policy rate expectations from overnight index swap (OIS) rates by predicting the risk premium in the OIS market.

*The Term Structure of CDS Spreads and Sovereign Credit Risk*

Patrick Augustin, McGill University, Canada

*Discussant:* Mathieu Fournier, Rotman School of Management

The shape of the term structure of credit default swap spreads is an informative signal about the relative importance of global and domestic risk factors to the time variation of sovereign credit spreads. A model illustrates how global shocks

determine spread changes when the slope is positive, while a negative slope indicates that domestic shocks are relatively more important. These theoretically motivated results are empirically validated using a geographically dispersed panel of 44 countries. Overall, the results suggest that both global risk factors and country-specific fundamentals are important sources of sovereign credit risk. They simply matter at different times.

*What We Can Learn From Pricing 139,879 Individual Stock Options*

Lars Stentoft, University of Western Ontario, Canada

*Discussant:* Phelim Boyle, Wilfrid Laurier University

The GARCH framework has been used for option pricing with success. However, empirical applications have been limited to index options or options on only a few stocks and this using only few distributions and variance specifications. We test the GARCH framework on 30 stocks in the Dow Jones Industrial Average using two classical volatility specifications and 7 different underlying distributions. Our results provide clear support for using an asymmetric volatility specification together with non-Gaussian distribution, particularly of the Normal Inverse Gaussian type, and statistical tests show that this model is most frequently among the set of best performing models.

**Fixed Income (Room 107)**

**Session Chair: Alexandra MacKay, University of Toronto**

*Search-For-Yield In Canadian Fixed-Income Mutual Funds And Monetary Policy*

Sermin Gungor, Bank of Canada, Canada

Jesus Sierra, Bank of Canada, Canada

*Discussant:* Narat Charupat, McMaster University

This paper investigates the effects of monetary policy on the risk-taking behavior of fixed-income mutual funds in Canada. We consider different measures of the stance of monetary policy and investigate active variation in mutual funds' risk exposure in response to monetary policy. We find evidence in support of a systematic link between monetary conditions and intertemporal variation in the risk-taking behavior of mutual funds. Specifically, following an expansionary monetary shift, funds actively increase default-risk exposure (i.e., search-for-yield). This is particularly evident in the post-crisis period where interest rates were kept low for a prolonged period of time.

*Impact of Sponsor Ownership on Fixed-income Fund Performance*

Mohamed Ayadi, Brock University, Canada

Lawrence Kryzanowski, Concordia University, Canada

Mahmood Mohebshahedin, Concordia University, Canada

*Discussant:* Stephen Szauro, University of Toronto

Mutual fund sponsors differ in their ownership structures (public/private; mutual, partnership, and limited). We provide evidence that agency issues and managerial abilities are important drivers of performance differences among Canadian fixed-income funds (FIF) differentiated by sponsor and fund types. Those sponsored by Banks (Professional Associations) exhibit superior (inferior) performances, on average, over those sponsored by Insurers, Financial Cooperatives, and Independ-

ents for the Canadian Bond category (over 70% of the Canadian FIF market). In contrast, funds sponsored by Financial Cooperatives strongly outperform the other sponsor types, on average, for the High-yield Bond category (10% of the Canadian FIF market).

*Bond Risk Premia and Gaussian Term Structure Models*

Bruno Feunou, Bank of Canada, Canada

Jean-Sébastien Fontaine, Bank of Canada, Canada

*Discussant:* Jia Shen, University of Calgary

Cochrane and Piazzesi (2005) show that (i) lagged forward rates improve the predictability of annual bond returns, adding to current forward rates, and that (ii) a Markovian model for monthly forward rates cannot generate the pattern of predictability in annual returns. These results stand as a challenge to modern Markovian dynamic term structure models (DTSMs). We develop the family of Conditional Mean DTSMs where the yield dynamics depend on current yields and their history. Empirically, we find that (i) current and past yields generate cyclical risk-premium variations, (ii) the model risk premia offer better returns forecasts, and (iii) the model coefficients are close to Cochrane-Piazzesi regressions of long-horizon returns. Yield decompositions differ significantly from what a standard model suggests – the expectation component decreases less in a recession and increases less in the recovery. A small Markovian factor “hidden” in measurement error (Duffee, 2011) explains some of the differences but is not sufficient to match the evidence.

**Microstructure (Room 108)**

**Session Chair: Tom McCurdy, University of Toronto**

*Catching Fire: An Anatomy of Information Diffusion using Retweets*

Mao Ye, University of Illinois, Urbana-Champaign, United States

Zhi Da, University of Notre Dame, United States

Nitesh Chawla, University of Notre Dame, United States

Jian Xu, University of Notre Dame, United States

*Discussant:* Xiaozhou Zhou, HEC Montreal

By tracking retweets of breaking news during trading hours, we are able to directly measure the rate of information diffusion across a large network of potential investors. We develop a model in which learning comes from this information diffusion. The model predicts that return and volatility increase with the diffusion rate and decrease with the proportion of people who already have information. Volume first increases and then decreases with diffusion. We measure liquidity by return divided by volume (the Amihud ratio) and predict that liquidity will be close to constant when the diffusion rate is low because price increases at the same speed as volume. A high diffusion rate, however, increases return but decreases the volume, which leads to a dramatic increase in the Amihud ratio. We find that these predictions are supported by the re-tweeting data.

*Liquidity-Adjusted Intraday Value At Risk Modeling And Risk Management: An Application To Data From Deutsche Börse*

Georges Dionne, HEC Montreal, Canada

Maria Pacurar, Dalhousie University, Canada

Xiao Zhou Zhou, HEC Montreal, Canada

*Discussant:* Bidisha Chakrabarty, St. Louis University

This paper develops a high-frequency risk measure, the Liquidity-adjusted Intraday Value at Risk (LIVaR). Our objective is to explicitly consider the endogenous liquidity dimension associated with order size. Taking liquidity into consideration when using intraday data is important because significant position changes over very short horizons may have large impacts on stock returns. By reconstructing the open Limit Order Book (LOB) of Deutsche Börse, the changes of tick-by-tick ex-ante frictionless return and actual return are modeled jointly using a Log-ACD-VARMA-MGARCH structure. This modeling helps to identify the dynamics of frictionless and actual returns, and to quantify the risk related to the liquidity premium. From a practical perspective, our model can be used not only to identify the impact of ex-ante liquidity risk on total risk, but also to provide an estimation of VaR for the actual return at a point in time. In particular, there will be considerable time saved in constructing the risk measure for the waiting cost because once the models have been identified and estimated, the risk measure over any time horizon can be obtained by simulation without re-sampling the data and re-estimating the model.

*The Dynamics of Trading in Commodity Futures*

Aditya Kaul, University of Alberta, Canada

Lorenzo Naranjo, ESSEC, France

Carmen Stefanescu, ESSEC, France

*Discussant:* Xuhui (Nick) Pan, Tulane University

We analyze the determinants and price effects of trading in commodity futures over 1986-2012. We find that speculator imbalances are positively autocorrelated and cross-autocorrelated with small investor imbalances. Both speculators and small traders sell after their long positions increase, especially when volatility is elevated. Second, imbalances have positive permanent price effects, which are larger for speculators. Finally, price volatility is related positively to lagged small trader imbalances, and negatively to lagged variability of speculator imbalances. Our findings are consistent with the view that speculators have limited risk-bearing capacity, and are short-term focused, with trades that are, in general, not destabilizing.

**12.00 PM - 2.00 PM**

**Meeting of Incoming and Outgoing NFA Boards (Jim Durrell Boardroom)**

**Chair: Gordon Sick, NFA**

This is a closed meeting for the New and Old NFA Board Members.

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Nominations for the Board of Directors closed on August 15, 2014. The following slate of Directors is appointed by acclamation or continuation of a two-year term:

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## **Wilfrid Laurier University - Tenure-Track Position – Finance**

The School of Business and Economics at Wilfrid Laurier University invites applications for a tenure-track faculty position at the rank of Assistant Professor in the Finance Area starting July 1, 2015.

Qualifications for the position include a Ph.D. in Finance although completion within a year will be considered. Successful candidates for the position must have exceptional research potential including the ability (a) to publish in top-tier journals and (b) to maintain a highly productive research agenda. The candidate should also be able to effectively teach finance courses at the undergraduate and graduate (MBA, MFin, and PhD) levels.

The Finance Area at Wilfrid Laurier University has a strong research focus and was ranked third among Canadian schools for research productivity. The School of Business and Economics has over one hundred full-time faculty and more than five thousand undergraduate and graduate students on campuses in Waterloo and Toronto, Ontario. Waterloo, where the main campus is located, is a highly innovative and dynamic region, and is home to a number of leading high-tech firms. With a mission to achieve excellence in management education, the school offers undergraduate and graduate degrees, including Honours BBA, MBA, MFin, and PhD. Laurier's undergraduate and graduate business programs are accredited by the AACSB. For more information, please visit [http://www.wlu.ca/homepage.php?grp\\_id=1820](http://www.wlu.ca/homepage.php?grp_id=1820).

Wilfrid Laurier University is committed to employment equity and values diversity. We welcome applications from qualified women and men, including persons of all genders and sexual orientations, persons with disabilities, Aboriginal persons, and persons of a visible minority. All qualified candidates are encouraged to apply; however, Canadians and permanent residents will be given priority. Members of the designated groups must self-identify to be considered for employment equity. Candidates may self-identify, in confidence, to Dr. Peter Carayannopoulos (contact details below). Further information on the equity policy can be found at [http://www.wlu.ca/page.php?grp\\_id=2465&p=10545](http://www.wlu.ca/page.php?grp_id=2465&p=10545).

All positions are subject to budgetary approval. Applicants should send a curriculum vitae, a job market paper and a teaching summary that includes a brief description of their teaching experience and effectiveness including teaching evaluations, if available. Applicants should arrange for at least three academic referees to submit reference letters to [finptac@wlu.ca](mailto:finptac@wlu.ca) at the time of application. Electronic applications are encouraged and all applications must include the Position Number in their application.

Faculty members will attend the NFA and FMA conferences. In your cover letter, please indicate your approximate availability at each of these conferences. Based on our assessment of your application and your availability, we may request an interview with you at one of the conferences.

The review of all applications will continue until the position is filled. Please direct your application quoting **Position Number 2014-06** to:

Dr. Peter Carayannopoulos  
Associate Dean of Business: Faculty Development & Research  
School of Business & Economics  
Wilfrid Laurier University  
75 University Avenue West  
Waterloo, Ontario N2L 3C5, CANADA  
Email: [finptac@wlu.ca](mailto:finptac@wlu.ca)

*Laurier Business & Economics wishes to thank all applicants for their interest. All nominations and applications shall be reviewed and considered under a set of criteria established by the Search Committee and a short list of candidates shall be interviewed. Only those applicants selected for the short list will be contacted.*

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Award Winners will be announced at the Saturday AGM Luncheon and posted on our website afterward.

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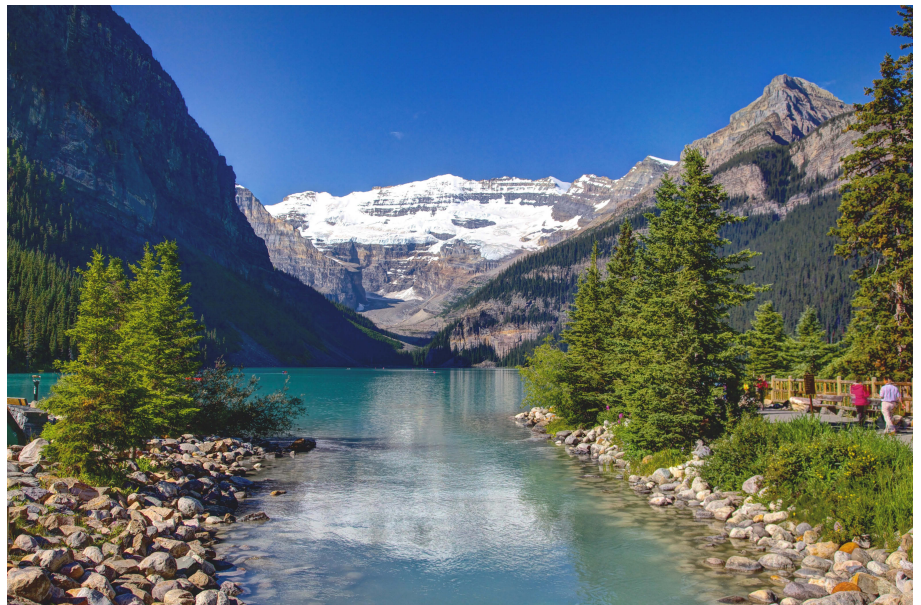
## The next NFA will be in Lake Louise, September 18-20, 2015

The Northern Finance Association Conference will be held at the Fairmont Chateau Lake Louise from September 18-20, 2015.

Lake Louise is in Banff National Park (Alberta) and is accessible from the Calgary International Airport.

The Program Chair will be Vikas Mehrotra of the University of Alberta.

The Paper Submission System will open on the NFA website in January 2015.



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