24th Australasian Finance & Banking Conference

The 24th Australasian Finance and Banking Conference was held from 14-16 December, 2011 at the Shangri-La Hotel in Sydney.

Keynote Speakers

- Professor Viral Acharya, New York University
  Topic: Guaranteed to Fail: Fannie Mae, Freddie Mac and the Debacle of Mortgage Finance
- Mr. Ric Battellino, Deputy Governor of the Reserve Bank of Australia
  Topic: Recent Financial Developments
- Professor Andrew Karolyi, Cornell University
  Topic: Are assets still priced locally, not globally?
- Professor Richard Roll, UCLA
  Topic: Volatility, Correlation, and Spread ETFs as Factors
- Professor Rene Stulz, Ohio State University
  Topic: Understanding bank performance during the crisis

Selection Committee

The Chairman of the Selection Committee is Fariborz Moshirian from UNSW.

Members of the Selection Committee included:

- Renee Adams, University of Queensland
- Allen Berger, University of South Carolina
- Michael Brennan, University of California LA
- Stijn Claessens, International Monetary Fund
- J. David Cummins, Temple University
- Asli Demirguc, Kunt World Bank
- Robert Faff, University of Queensland
- Mark Flannery, University of Florida
- Kenneth French, Dartmouth University
- Bruce Grundy, University of Melbourne
- Steven Kaplan, The University of Chicago
- Andrew Karolyi, Cornell University
- Larry H. P. Lang, Chinese University of Hong Kong
- Florencio Lopez De Silanes, EDHEC Business School
- Ike Mathur, Southern Illinois University
- Ronald Masulis, Vanderbilt University
- Maureen O'Hara, Cornell University
- Jay Ritter, University of Florida
- Richard Roll, UCLA
- Anthony Saunders, New York University
- Henri Servaes, London Business School
- Andrei Shleifer, Harvard University
- Tom Smith, Australian National University
- Bruno Solnik, HEC School of Management
- Avanidhar Subrahmanyam, UCLA
- Paul Wachtel, New York University

Thursday 15 December — 9:00am – 11:00am
Session 4 — Cambridge I & II

Corporate Finance 3

Stocking Up: Executive Optimism and Share Retention
Rik Sen, Hong Kong University of Science & Technology
Robert Tumarkin, University of New South Wales
Discussant: Daniel Kim, Indiana University Bloomington

Performance Shares: Valuation, Optimal Design, and Empirical Evidence
Daniel Kim, Indiana University Bloomington
Discussant: Robert Tumarkin, University of New South Wales

Institutional Ownership and Firm Cash Holdings
Christine Brown, University of Melbourne
Yangyang Chen, Monash University
Chander Shekhar, University of Melbourne
Discussant: Wei-Lin Liu, Nanyang Technological University

The Even-Odd Effects of Corporate Board
Xin Deng, Nanyang Technological University
Huasheng Gao, Nanyang Technological University
Wei-Lin Liu, Nanyang Technological University
Discussant: Chander Shekhar, University of Melbourne

Session Chair: Jan Bena, University of British Columbia

Thursday 15 December — 9:00am – 11:00am
Session 4 — Cambridge III

Financial Institutions 2

Analyzing Bank Ratings: Key Determinants and Procyclicality
Elisabeth Van Laere, National University of Singapore
Bart Baesens, Katholieke Universiteit Leuven
Discussant: Tao Chen, Chinese University of Hong Kong

Asset Securitizations and Audit Effort
Yuyu Zhang, University of New South Wales
Gary Monroe, University of New South Wales
Dominic Gasbarro, Murdoch University
Grant Stewart Cullen, Murdoch University
Greg Shailer, Australian National University
Discussant: Elisabeth Van Laere, National University of Singapore

Optimal Deposit Pricing in Competitive, Oligopolistic Markets
Basile Maire, Cantonal Bank of Zurich
Andreas Bloechlinger, Cantonal Bank of Zurich
Discussant: Yuyu Zhang, University of New South Wales

Financial Innovation: The Bright and the Dark Sides
Thorsten Beck, Tilburg University
Tao Chen, Chinese University of Hong Kong
Chen Lin, Chinese University of Hong Kong
Frank Song, University of Hong Kong
Discussant: Basile Maire, Cantonal Bank of Zurich

Session Chair: Irene Tutticci, University of Queensland

Thursday 15 December — 9:00am – 11:00am
Session 4 — Cambridge IV

Corporate Finance 4

Managerial Attitudes Toward to Market Valuations
Toshio Serita
Peng Xu, Hosei University
Discussant: Madhu Veeraraghavan, Monash University

National Culture and Cash Holdings in International Markets
Yangyang Chen, Monash University
Paul Dou, Macquarie University
S. Ghon Rhee, University of Hawaii
Cameron Truong, Monash University
Madhu Veeraraghavan, Monash University
Discussant: Peng Xu, Hosei University

The Impact of Product Warranties on the Capital Structure of Australian Firms
Bayan Arqawi, Bond University
William Bertin, Bond University
Laurie Prather, Bond University
Discussant: Anup Menon Nandialath, HEC Paris

The Impact of Buyouts on the Performance of Acquired Firms: A Re-Examination of the French Case
Anup Menon Nandialath, HEC Paris
Kerstin Peschel, HEC Paris
Discussant: Bayan Arqawi, Bond University

Session Chair: Russell Poskitt, University of Auckland

Thursday 15 December — 9:00am – 11:00am
Session 4 — Essex I

Capital Markets 4

Liquidity Management Around Seasoned Equity Offerings
David Siu, University of Queensland
Robert Faff, University of Queensland
Discussant: Yaw-Huei Wang, National Taiwan University

Natural Disasters - Blessings in Disguise?
Hardjo Koerniadi, Auckland University of Technology
Chandrasekhar Krishnamurti, University of Southern Queensland
Alireza Tourani Rad, Auckland University of Technology
Discussant: Lei Zhou, Northern Illinois University

European Financial Market Integration in the Wake of the Sovereign Debt Crisis: An Industry Analysis
Söhnke Bartram, University of Warwick
Yaw-Huei Wang, National Taiwan University
Discussant: David Siu, University of Queensland

The Determinants of Treasury Bond Stripping Level
Marck Bulter, Dutch Central Bank
Miles Livingston, University of Florida
Lei Zhou, Northern Illinois University
Discussant: Hardjo Koerniadi, Auckland University of Technology

Session Chair: Basma Majerbi, University of Victoria

Australian School of Business
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The 24th Australasian Finance and Banking Conference

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Paper Abstracts

14 - 16 December 2011

Asset Securitizations and Audit Effort

Yuyu Zhang, University of New South Wales (UNSW)

Gary Monroe, University of New South Wales (UNSW) - Australian School of Business

Dominic Gasbarro, Murdoch University

Abstract

Asset securitizations increase audit complexity and audit risks, which are expected to increase audit effort. We predict auditors became more sensitive to banks asset securitization risks in light of their role in bank failures and the financial downturn that commenced in 2007. Using bank holding company data from 2003 to 2009, we find that asset securitization risks (retained interests) are associated with bank audit fees during, but not before, the global financial crisis. This suggests auditors were previously less attentive to securitization risks before the GFC. The results are consistent with auditors previously treating securitizations as asset sales rather than recourse debt.

Estimation of Operational Risks Using Non-Parametric Approaches with an Application to US Business Losses

Param Silvapulle, Monash University - Department of Econometrics & Business Statistics

Ainura Tursunalieva, Monash University - Department of Econometrics & Business Statistics

Abstract

Following the recent global financial crisis, many banks and other businesses in the industrialized countries incurred notably heavy losses. As a consequence, reliable estimation of operational risk (OR) is becoming increasingly important to all internationally active banks and other financial institutions. The OR is the unexpected loss, which is the difference between the 99:9 per cent quantile and the mean of the loss distribution. This paper adapts non-parametric methods based on heavy-tailed distributions and constructs point and 95 per cent confidence interval (CI) estimates for ORs. The main advantage of these nonparametric methods is that there are no assumptions made about the shape of loss distributions and that data determines their shapes, providing robust estimates for ORs. Employing these methods, we construct point as well as interval estimates for ORs for US businesses. The noteworthy observation is that the CIs are asymmetric with huge upper bounds, highlighting the extent of uncertainties associated with the point estimates of ORs. The estimates of expected shortfalls lie within these intervals. The nonparametric methods introduced in this paper will have much wider applications, for example, in estimating another popular measure of risk, credit risk.

Market Uncertainty and Sentiment, and the Post-Earnings Announcement Drift

Ronald Geoffrey Bird, University of Technology, Sydney (UTS) - School of Finance and Economics

Daniel Choi, The University of Waikato

Danny Yeung, University of Technology, Sydney (UTS)

Abstract

The post-earnings announcement drift (PEAD) first identified over 40 years ago seems to be as much alive today as it ever was. Numerous attempts have been made to explain its continued existence. In this paper we provide evidence to support a new explanation: that the PEAD is a reflection of the level of market uncertainty and sentiment that prevails during the post-announcement period. The finding that uncertainty plays a role in explaining how investors respond to information suggests that it should be included as a factor in pricing models while the fact that market sentiment also has a role is another instance of the importance of human behaviour in establishing prices.

Benchmark Replication Portfolio Strategies

Paskalis Glabadanidis, University of Adelaide Business School

Leon Zolotoy, Melbourne Business School

Abstract

We propose a novel approach to the benchmark replication problem which uses a minimum tracking error variance as an objective subject to a target expected outperformance. When no budget constraint is imposed on the replicating portfolio, the solution involves that standard hedge portfolio and the tangent portfolio constructed from the replicating securities. In the presence of a budget constraint as well, the solution also includes the minimum variance portfolio constructed from the replicating securities. We implement our theoretical results using recent data for three widely followed US stock indices with very good out-of-sample performance.

Stock Market Fragility and the Quality of Governance of the Country

Chunmei Lin, National University of Singapore (NUS) - Department of Finance

Massimo Massa, INSEAD - Finance

Hong Zhang, INSEAD - Finance

Abstract

We study the relationship between the quality of governance of a country and its degree of financial fragility. We argue that bad governance affects the market by amplifying the reaction of fund manager to public information. This induces funds' rebalancing swings that create price fragility and excess market volatility for the assets hold by the funds. We test this hypothesis using data on international mutual funds and on stocks over the period 2000-2009. We show that the reaction of the fund managers to public information increases the worse the governance of the country of the stock they hold. We exploit this information by defining a variable (RPIW) that represent the incremental mutual fund reaction to public information in the presence of bad country governance and we use it to study the relation between stock value and the quality of governance of the country. We show that bad governance is related to a more positive stock reaction to good news and a more negative stock reaction to bad news. Also, stocks of countries with bad governance display a higher total volatility, idiosyncratic volatility, skewness and lower liquidity. This effect is stronger during crises. During the 2008-2009 period, stocks of bad governance countries over-react to public information, displaying higher volatility, skewness and illiquidity and overall stock price reaction to information.

The Role of Covenants in Mitigating Conflicts of Interest Within Lending Syndicates

Nishant Dass, Georgia Institute of Technology

Vikram Nanda, Georgia Institute of Technology - College of Management

Qinghai Wang, Georgia Institute of Technology

Abstract

We study the role of covenants in syndicated bank loans. We argue that, in addition to being a device for monitoring the borrower, covenants can help mitigate conflicts of interest between the lead arranger and participating banks in the syndicate. Such disagreements can arise when, for instance, a lead arranger has the incentive to support a poorly performing borrower and/or offer loan modifications while other syndicate lenders may prefer to discipline the borrower by accelerating the loan or enforcing default. We develop a simple model reflecting such conflicts and find empirical support for its predictions that covenants are less likely to be present: (i) in non-syndicated versus syndicated loans; (ii) when the lead's loan allocation is greater; and (iii) when participating bank affiliates hold substantial equity in the borrower. Consistent with this evidence, we find that lead arrangers are more likely to syndicate with banks that hold borrower's equity through affiliated entities.

How Smooth Is Price Discovery? Evidence from Cross-Listed Stock Trading

Haiqiang Chen, Xiamen University - Wang Yanan Institute for studies in Economics

Moon Sub Choi,

Yongmiao Hong, Cornell University - Department of Economics

Abstract

The adjustment to parity can be nonlinear for a cross-listed pair: Convergence may be quicker when the price deviation is sufficiently profitable. We propose a threshold error correction model (ECM) to gauge the market-respective information shares of Canadian listings traded on the Toronto Stock Exchange (TSX) and the New York Stock Exchange (NYSE). Since dynamics may alternatively be gradual, we further generalize the threshold framework to a smooth transition ECM. The empirical implications are as follows: First, the TSX and the NYSE have integrated over time. Second, parity-convergence accelerates upon discounts on the cross-listings on the NYSE. Third, we find a larger feedback from the NYSE if the price gap exceeds the threshold (required arbitrage return). Fourth, informed traders tend to cluster on the NYSE upon discounts on the cross-listings. Fifth, the information share and threshold are affected by the relative degree of private information, market friction and liquidity measures, and firm-level characteristics.

Prior Relationship, Industry Expertise, Information Leakage, and the Choice of M&A Advisor

Xin Chang, Nanyang Technological University (NTU) - Nanyang Business School

Chander Shekhar, University of Melbourne

Lewis Tam, University of Macau - Faculty of Business Administration

Abstract

This paper examines the impact of prior bank-firm relationships, bank s industry expertise and information leakage concerns on acquirers and targets choice of financial advisors in mergers and acquisitions. We show that prior bank-firm merger advisory relationship and bank's industry expertise increase the likelihood of a bank being chosen as an advisor. In addition, banks with prior relationship with acquirers (targets) are more likely to be chosen by targets (acquirers), suggesting that information leakage through advisors is at work between acquirers and targets. Due to concerns of information leakage to product-market rivals, experienced acquirers are found to be reluctant to share advisors with rival firms in the same industry. We also document that advisors charge higher fees if they have prior relationship with merging firms' product-market rivals. Unlike acquirers, targets pay a fee premium to retain ongoing advisors.

Information Asymmetry and the Timing of Capital Issuance: An International Examination

April Knill, Florida State University

Bong-Soo Lee, Florida State University

Abstract

Using issuance data across 50 countries from 1996 through 2009, we examine the role of information asymmetry in market timing globally. We utilize a model that takes into account the possible feedback of security issues to past market returns allowing us to ascertain whether timing of capital issuance around the world is based on information asymmetry. We find evidence of both market timing and pseudo market timing. The evidence for (pseudo) market timing is (not) significantly stronger in international sub-samples with greater levels of information asymmetry when capital issuance is measured by (changes in equity) equity share. These results suggest that information asymmetry plays an important role in the ability of managers to time capital issuance and that counter to the implications of extant literature, market timing and pseudo market timing are not mutually exclusive, i.e., existence of one does not nullify the other.

Characteristic Liquidity, Systematic Liquidity and Expected Returns

M. Reza Baradarannia, University of Sydney

Maurice Peat, University of Sydney

Abstract

This paper investigates whether the effect of liquidity on equity returns can be attributed to the liquidity level, as a stock characteristic, or a market wide systematic liquidity risk. We employ a new low frequency liquidity measure, develop a CAPM liquidity-augmented risk model and test the characteristic hypothesis against the systematic risk hypothesis for the liquidity effect. We find that the two-factor systematic risk model explains the liquidity premium. The hypothesis that the liquidity characteristic is compensated irrespective of liquidity risk loadings is not supported in the data. This result is robust over 1930-2008 data and sub-samples of pre-1963 and post-1963 data. The results demonstrate that the liquidity augmented CAPM approach is the correct way to incorporate the liquidity risk.

The Impact of Derivatives Hedging on Stock Market: Evidence from Taiwan Covered Warrants Market

San-Lin Chung, National Taiwan University - Department of Finance

Wen-Ranq Liu, National Taiwan University

Wei-Che Tsai, National Taiwan University - Department of Finance

Abstract

This paper examines the hedging impact on the underlying stock market using a comprehensive dataset of covered warrants traded in the Taiwan Stock Exchange (TWSE). Since TWSE requires the warrant issuers to conduct dynamic hedging over the life of warrants, we can estimate the number of shares bought or sold for rebalancing the hedging portfolio and measure its impact. We find significant positive abnormal returns and trading volumes before the announcement day of warrants issuance, suggesting that issuers establish their hedging portfolios before the announcement day. The magnitude of the price effect is positively related to the size of the hedging portfolio. Moreover, there is a significantly positive relationship between stock return volatility and the price elasticity of hedging demand (defined as the percentage of shares needed for rebalancing hedge portfolio when the underlying stock price changes 1%). Finally, we also observe significantly negative price effect to the underlying stock before (after) the expiration date for call warrants that are expired out-of-the-money (in-the-money). For call warrants expired in-the-money, the negative price impact is due to the fact that warrants traded in TWSE are cash settlement when exercised, and thus the issuers have to liquidate the hedging portfolio after expiration, which results in selling pressure on the underlying stock.

Corporate Governance, Diversification, and Firm Value: Evidence from 'Spin-Ins'

Yoon Choi, University of Central Florida - College of Business Administration - Department of Finance

Seung Han, Korea Advanced Institute of Science and Technology (KAIST)

Abstract

We analyze the impact of corporate restructuring on firm value using a unique internal corporate restructuring created between the years of 2001 and 2003 in Japan. We show that excess value significantly increases after the internal restructuring even when the degree of diversification has not changed. This result supports the argument that diversification itself may not drive discounts or premiums.

We also explore these events to examine the effect of bank governance and keiretsu affiliation. Our results are consistent with the argument that recent Japanese restructuring reduces information asymmetries and agency problems, thus improving the efficiency of internal capital markets and firm value.

Information Asymmetry and Momentum Anomalies

Xiaolin Qian, Univeristy of Macau

Chuan-Yang Hwang, Nanyang Technological University (NTU)

Abstract

In this paper, we construct an information asymmetry factor (VECINF) based on the price discovery of large trades. VECINF is significantly negatively correlated with market excess return, indicating that market-wide information asymmetry is lower in bull markets, which is consistent with the view that more uninformed investors are attracted into stock markets when the markets offer high returns. In addition, VECINF has the most significant pricing effect among the considered risk factors (MKT, SMB, HML, and UMD), which suggests that ignoring the risk of information asymmetry may give rise to false discoveries of anomalies. As a case in point, we show that momentum anomalies disappear once we control for the risk of information asymmetry. This is because there are fewer informed traders, and hence lower risk of information asymmetry, in bad news firms (past losers or low earning surprise firms) than in good news firms (past winners or high earning surprise firms). The larger cost and risk of arbitrage in taking short positions makes bad news firms less attractive to informed traders. Consistent with this explanation, we find that the loading on VECINF is lower in bad news firms than in good news firms; and is lower only in the holding periods when momentum exists. This difference in loadings increases significantly with idiosyncratic volatility, and this explains why momentum is stronger in firms with large idiosyncratic volatility. Regardless of the level of idiosyncratic volatility, the significantly positive Fama-French factors risk-adjusted returns of zero investment momentum portfolios are no longer significant once we include VECINF as an additional factor for risk adjustment.

Managerial Attitudes Toward to Market Valuations

Toshio Serita, Aoyama Gakuin University - Department of Economics

Peng Xu, Hosei University - Department of Economics

Abstract

We use a survey-based approach to provide new insight on managerial attitudes toward to market valuations whether a corporate officer perceives her/his firm s stock price is undervalued or overvalued by the market. Our findings suggest that corporate officers are prone to attribute poor equity returns and poor industry adjusted market valuation to being undervalued by the market. Also managerial perceptions persist over time. Finally, we link managerial attitudes to payout policies.

Natural Disasters - Blessings in Disguise?

Hardjo Koerniadi, Auckland University of Technology

Chandrasekhar Krishnamurti, University of Southern Queensland

Alireza Tourani-Rad, Auckland University of Technology - Faculty of Business

Abstract

This study examines the impact of natural disasters on market returns and on several industries that are likely to be affected by the disasters. We find that different natural disasters have different impacts on the returns of the market and on those of industries. Our evidence suggests that while earthquake, hurricane and tornado could negatively affect market returns several weeks after the events, other disasters such as flood, tsunami and volcanic eruption may have limited impact on market returns. We also find that construction and materials industry is positively affected by natural disasters but nonlife and travel industries are likely to suffer when a natural disaster strikes.

Liquidity and Price Discovery of Algorithmic Trading: An Intraday Analysis on the SPI Futures Contract

Tina Viljoen, The University of Sydney Business School

Hui Zheng, Discipline of Finance, The University of Sydney

P. Joakim Westerholm, The University of Sydney Business School

Abstract

We study the intra-day impact of algorithmic trading on the futures market to increase our understanding of algorithmic trading and its role in the price formation process. First, we find that algorithmic trading provides liquidity when the spread is wide and that algorithms enter the market at a series of intervals that decrease the spread. Second, we show that algorithmic trading is related to lower adverse selection and is unrelated to realised spreads. Third, we confirm that information asymmetry is highest at the beginning of the trading day, and as the price stabilises during the trading day, we find that the trade becomes the information carrier and algorithmic trading increases. Fourth, we find that algorithmic trades strategically enter the market during periods with less informed trading, while the period following exhibits higher public and private information. Our results suggest that algorithmic traders contribute to the price discovery process of financial markets.