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Master Theses FFS 2021: Topics

TOPIC NR1: **Mutual fund managerial ownership and capital gains taxes**
Advisor: Chia-Yi Yen

TOPIC NR2: **Q&As at Earnings Conference calls and analyst forecasts**
Advisor: Mengqiao Du

TOPIC NR3: **Closing decisions of Chinese mutual funds**
Advisor: Mengqiao Du

TOPIC NR4: **Stated investment styles in mutual funds' prospectus**
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Advisor: Mengqiao Du

TOPIC NR1: Mutual fund managerial ownership and capital gains taxes

Advisor: Chia-Yi Yen

Because of agency problems between fund managers and investors, mutual fund managers are often asked to own a number of shares in the funds they manage, known as "skin-in-the-game." Empirical studies have shown that this design helps realign the interests of managers and investors. For example, Ma and Tang (2018) show that managerial ownership is affiliated with less agency-induced risk-taking in portfolio holdings. However, when taking into account capital gains taxes, the existence of such a tax may distort fund managers' decisions against shareholders' best interests. Though this issue is relatively less discussed in the mutual fund literature, a number of recent papers discuss how managerial taxes distort the decisions of CEOs, which can be interpreted analogously for the behavior of fund managers.

Inspired by the literature on CEO incentives, this thesis shall investigate if similar effects of capital gains taxes on managerial behavior exist for fund managers. There are two potential hypotheses regarding fund managers' decision on risk-taking. First, fund managers may take less risk in the presence of capital gains taxes due to a lock-in effect. Yost (2017) predicts that CEOs with significant ownership are reluctant to sell their shares in order to circumvent the tax liabilities resulting from capital gains; as a result, they tend to make less risky decisions and hence limit the personal risk of their ownership. Second, fund managers may take more risk in the presence of a capital gains tax due to a substitution effect. Armstrong et al. (2018) argue that, with the existence of taxation, the government is basically sharing risk with firms. That is, when firms make profits, the government takes part of the profits as taxes; when firms lose, they can offset their tax liability later. As a result, CEOs do not bear that much risk after-tax, and they may turn to more risky projects in order to achieve the desired level of risk-taking. In addition to risk-taking decisions, tax distortion effects on other decisions of fund managers belong to the scope of this topic, such as fund performance and turnover. For example, Evans (2008) finds that fund performance is increasing in the level of managerial ownership. Whether tax distortion changes this finding is also a sub-issue to be investigated.

In this thesis, the student is expected to conduct a literature review on the tax distortion effect on mutual fund managers' decisions and further examine how unrealized tax burdens on fund managers influence fund-level activities, such as riskiness, performance, turnover, and flows. The student is expected to apply the empirical designs of Yost (2018) to the mutual fund settings and investigate the impact of capital gains taxes on top of Ma and Tang (2018).

Requirements:

The empirical work requires the use of databases on mutual funds, such as the CRSP Mutual Fund database and the Thomson Reuters Ownership database. These data are accessible at the University of Mannheim or will be provided by the supervisor. In addition, the student has to manually collect data from the SEC EDGAR website. We recommend that the candidate has at least basic knowledge of a statistical software program (e.g., Stata, R, or Python) and econometrics.

Introductory Literature:

- Armstrong, Christopher S., et al. "The economics of managerial taxes and corporate risk-taking." The Accounting Review 94.1 (2018): 1-24.
- Evans, Allison L. "Portfolio manager ownership and mutual fund performance." Financial Management 37.3 (2008): 513-534.
- Ma, Linlin, and Yuehua Tang. "Portfolio manager ownership and mutual fund risk taking." (2018). Management Science, forthcoming
- Yost, Benjamin P. "Locked-In: The Effect of CEOs' Capital Gains Taxes on Corporate Risk-Taking." The Accounting Review (2017).

TOPIC NR2: Q&As at Earnings Conference calls and analyst forecasts

Advisor: Mengqiao Du

Earnings conference calls generate considerable intraday stock price movements, most of which occur during the discussion period (or Q&A) of the call (e.g., Frankel et al. (1999) and Matsumoto et al. (2011)). In addition Chen et al. (2018) find that an analyst's tone during these calls predicts his or her future price target, stock recommendation, and earnings forecast for the firm, which suggests that analysts are revealing their beliefs about the firm during the discussion.

Prior studies on earnings calls focus on the attributes of managers and analysts individually. Analysts are expected to get information from the interaction with the management at earnings conference calls. Hence, it is plausible to expect that analysts who ask questions and get answers from earnings conference calls, especially those who get informative answers, improve their forecast accuracy.

As for this thesis, the student is asked to conduct a literature review on informativeness of earnings conference calls, especially the Q&A session. The discussion should include but is not limited to how earnings conference calls influence the stock market and analyst forecasts. Furthermore, the student is expected to empirically examine whether and what kinds of answers from the management improve analysts' forecast accuracy.

Requirements:

The empirical work requires the use of databases on sell-side analysts and financial markets (e.g., IBES and Compustat) as well as conference call transcripts. All data are accessible online or from databases at the University of Mannheim. We recommend that the candidate has at least basic knowledge of a statistical software program (e.g., Stata) and econometrics. Basic knowledge in Python is helpful in textual analysis.

Introductory Literature:

- Chen, J. V., Nagar, V., & Schoenfeld, J. (2018). Manager-analyst conversations in earnings conference calls. Review of Accounting Studies, 23(4), 1315-1354.
- Frankel, R., Mayew, W. J., & Sun, Y. (2010). Do pennies matter? Investor relations consequences of small negative earnings surprises. Review of Accounting Studies, 15(1), 220-242.
- Matsumoto, D., Pronk, M., & Roelofsen, E. (2011). What makes conference calls useful? The information content of managers' presentations and analysts' discussion sessions. The Accounting Review, 86(4), 1383-1414.

TOPIC NR3: Closing decisions of Chinese mutual funds

Advisor: Mengqiao Du

Some mutual funds choose to close to new investments. Fund families typically claim that closing a fund protects the fund's superior performance by preventing it from growing too large to be managed efficiently. Bris et al. (2006) show that funds close following a period of superior performance and abnormal fund inflows but find evidence consistent with the "cheap talk hypothesis": closing does not impose a cost on the fund because fund closing is accompanied by an increase in fees. Moreover, Zhao (2004) finds no evidence that closing a fund can protect its performance. Instead, fund closing decisions are more likely to be motivated by spillover effects – by closing a star fund, the fund family signals its superior performance and also brings investors' attention and investments to other funds in the family. Chen et al. (2012) further document that only those closed funds for which no new fund is subsequently launched continuously deliver positive abnormal returns.

Not many mutual funds in the US have closed to new investments. Thus, the above-mentioned studies are all based on a sample of 100-200 closing decisions. Mutual funds appear to close more often in China. A potential reason could be that the Chinese stock market is smaller compared to the US market and thus, it is hard for mutual funds to find new investment opportunities once faced with abnormal fund inflows. In this case, closing a fund in China may protect its investors by maintaining the fund's superior performance. Nevertheless, closing decisions of mutual funds in developing countries have not been examined by the literature.

As for this thesis, the student is asked to conduct a literature review on fund closing decisions. The discussions should also include related topics such as the influence of fund size and fund flows on fund performance, especially international evidence on these topics. Furthermore, the student is expected to examine the fund closing decisions of Chinese mutual funds. In the empirical part of this thesis, the student should develop and test new hypotheses, and replicate the analyses in Bris et al. (2006) and Zhao (2004) with Chinese mutual fund data.

Requirements:

The empirical work requires the use of databases on mutual funds (e.g., Morningstar). All data are accessible online or from databases at the University of Mannheim. We recommend that the candidate has at least basic knowledge of a statistical software program (e.g., Stata) and econometrics.

Introductory Literature:

- Bris, A., Gulen, H., Kadiyala, P., & Rau, P. R. (2007). Good stewards, cheap talkers, or family men? The impact of mutual fund closures on fund managers, flows, fees, and performance. Review of Financial Studies, 20(3), 953-982.
- Chen, H. L., Gao, S., & Hu, X. (2012). Closing and cloning in open-end mutual funds. Journal of Banking & Finance, 36(4), 1210-1223.
- Zhao, X. (2004). Why are some mutual funds closed to new investors?. Journal of Banking & Finance, 28(8), 1867-1887.

TOPIC NR4: Stated investment styles in mutual funds' prospectus

Advisor: Mengqiao Du

Mutual funds state their investment objectives in prospectuses. However, Sensoy (2009) shows that a fraction of size and value/growth benchmark indices disclosed in the prospectuses of U.S. equity mutual funds do not match the fund's actual style. Similarly, Chen et al. (2019) find misclassification of bond funds.

Given the SEC regulations, in principle, mutual funds should not misstate their investment objective in the prospectus. Therefore, perspectives other than the stated investment objective in the mutual fund prospectus should contain important information. For example, two mid-cap value funds with a benchmark of Russell Midcap® Value Index may state different minimum percentages that the fund invests in medium-sized value companies.

As for this thesis, the student is asked to conduct a literature review on fund (mis)classifications. The discussions should include but is not limited to the impact of the classification on performance and fund flows. Furthermore, the student is expected to investigate the mismatch of stated benchmarks among equity funds as in Sensoy (2009) using updated data. In addition, the student should also download and check fund prospectuses on SEC Edgar to investigate the use of language in prospectuses for funds with mismatched benchmarks.

Requirements:

The empirical work requires the use of databases on mutual funds (e.g., Morningstar and Thomson Reuters Mutual Fund Holdings) as well as SEC Edgar. All data are accessible online or from databases at the University of Mannheim. We recommend that the candidate has at least basic knowledge of a statistical software program (e.g., Stata) and econometrics. Basic knowledge in Python is helpful in downloading data from SEC Edgar and textual analysis.

Introductory Literature:

- Sensoy, B. A. (2009). Performance evaluation and self-designated benchmark indexes in the mutual fund industry. Journal of Financial Economics, 92(1), 25-39.
- Chen, H., Cohen, L., & Gurun, U. (2019). Don't take their word for it: The misclassification of bond mutual funds (No. w26423). National Bureau of Economic Research.

TOPIC NR5: In-group Bias at Earnings Conference Calls

Advisor: Mengqiao Du

Access to the management of the companies they cover is among the most highly valued services sell-side analysts provide to their institutional-investor clients. Analysts who facilitate access to management can establish better relationships with institutional investors and gather greater trading and other commissions (e.g., Brown et al., 2016; Juergens and Lindsay, 2009). While Regulation Fair Disclosure prohibits the selective disclosure of material information, managers maintain considerable discretion in the level of access they grant to different analysts. For example, managers select analysts to participate in the Q&A sessions of the public earnings conference calls their companies host.

Previous literature finds that discrimination and favoritism exist in financial markets. In the setting of earnings conference calls, Mayew (2007) finds that the probability of an analyst asking a question during an earnings conference call is increasing in the favorableness of the analyst's outstanding stock recommendation. In a similar vein, Flam et al. (2020) find that managers are less likely to select minority analysts to participate in the Q&A session. In addition, Jannati et al. (2020) show in-group bias among analysts in their earnings forecasts. Compared with female analysts, male analysts have lower earnings forecasts and worse stock recommendations for firms headed by female CEOs than for firms headed by male CEOs.

As for this thesis, the student is asked to conduct a literature review on discrimination and favoritism in financial markets as well as on activities at earnings conference calls. Furthermore, the student is expected to examine whether there is any in-group bias at earnings conference calls and how this influences analysts' earnings forecasts. The student should replicate Mayew (2007) and examine whether in-group bias exists at earnings conference calls, e.g., whether male CEOs are more likely to select female analysts to ask questions in the Q&A session.

Requirements:

The empirical work requires the use of databases on sell-side analysts and financial markets (e.g., IBES and Compustat) as well as conference call transcripts. All data are accessible online or from databases at the University of Mannheim. We recommend that the candidate has at least basic knowledge of a statistical software program (e.g., Stata) and econometrics. Basic knowledge in Python is helpful in textual analysis.

Introductory Literature:

- Brown, L., Call, A., Clement, M., and Sharp, N. (2015). Inside the "black box" of sell-side financial analysts. *Journal of Accounting Research*, Vol. 53, pp. 1-47.
- Flam, R. W., Green, J., Lee, J. A., and Sharp, N. Y. (2020). A Level Playing Field? Empirical Evidence That Ethnic Minority Analysts Face Unequal Access to Corporate Managers. *Unpublished Working Paper*, 06.08.2020.
- Jannati, Sima and Kumar, Alok and Niessen-Ruenzi, Alexandra & Wolfers, Justin (2020). In-Group Bias in Financial Markets. *Unpublished Working Paper*, 21.02.2020.
- Juergens, J. L., & Lindsey, L. (2009). Getting out early: An analysis of market making activity at the recommending analyst's firm. *Journal of Finance*, Vol. 64, pp. 2327-2359.
- Mayew, W. J. (2008). Evidence of management discrimination among analysts during earnings conference calls. *Journal of Accounting Research*, Vol 46, No.3, pp. 627-659.