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Seminar

TOPIC R1: **Investor Inattention and Friday Earnings Announcements**
Advisor: Florens Focke

TOPIC R2: **Investor Attention and Price Momentum**
Advisor: Florens Focke

TOPIC R3: **Investor Attention and the Post-Earnings Announcement Drift**
Advisor: Florens Focke

TOPIC R4: **Short Interest and Stock Returns**
Advisor: Pavel Lesnevski

TOPIC R5: **Short Interest, Investor Sentiment and Anomalies**
Advisor: Pavel Lesnevski

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Advisor: Pavel Lesnevski

TOPIC R7: **Liquidity, flights and asset prices**
Advisor: Zorka Simon

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Advisor: Zorka Simon

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Advisor: Zorka Simon

TOPIC R1: Investor Inattention and Friday Earnings Announcements

Classification: Empirical topic
Advisor: Florens Focke

Investors, and in particular retail investors, only have limited attention available. They therefore need to decide which stocks to pay attention to, and whether to focus attention on the stock market at a particular time at all. DellaVigna and Pollet (2009) argue that investors might be distracted on Fridays due to the upcoming weekend. This could reduce the amount of attention they pay to financial markets and the quality of their decision making. Earnings announcements are situations in which a substantial amount of information on a firm tends to be revealed. At the same time, the post earnings announcement drift is one of the most long-standing anomalies in financial markets. This drift might in part be explained by investors not paying enough attention to an earnings announcement, thereby not fully incorporating the information in the announcement immediately into stock prices. As this underreaction is gradually corrected, the drift occurs.
In this study, the student should provide a brief overview of the literature on investor attention and the post earnings announcement drift. In the empirical part, the purpose of the thesis is to replicate the main findings in DellaVigna and Pollet (2009) on the market reaction to earnings announcements that take place on Fridays. As an extension, a more recent time period could be considered and the attention hypothesis could be directly tested via Google Search Volume, which is a proxy for investor attention. Access to financial markets data from CRSP, Compustat and IBES will be provided. Moreover, a dataset of Google Search Volume can also be provided.

Introductory Literature:

DellaVigna, Stefano, and JM Pollet, 2009, Investor inattention and Friday earnings announcements, *Journal of Finance* 64, 709–749.

Hirshleifer, David, Sonya Seongyeon Lim, and Siew Hong Teoh, 2009, Driven to Distraction : Extraneous Events and Underreaction to Earnings News, *Journal of Finance* LXIV, 2289–2325.

Hirshleifer, David, and Siew Hong Teoh, 2009, Limited attention, information disclosure, and financial reporting, *Journal of Accounting and Economics* 36, 337-386.

TOPIC R2: Investor Attention and Price Momentum

Classification: Empirical topic
Advisor: Florens Focke

Price momentum, or simply momentum, is one of the most pervasive anomalies in financial markets. According to the findings in Jegadeesh and Titman (1993), past winner stocks tend to outperform, while past loser stocks tend to underperform. This phenomenon has been linked to investors' behavioral biases that lead them to overreact to information. Hou et al. (2009) remark that it is a necessary condition for any overreaction story that investors pay attention to a stock in the first place. Using turnover as a proxy for investor attention, they find that momentum profits are larger for stocks with higher turnover.
In this study, the student should provide a brief overview of the literature on investor attention and the price momentum anomaly. In the empirical part the purpose of the thesis is to replicate the main findings in Hou et al. (2009) on the relationship between price momentum profits and turnover. As an extension, a more recent time period could be considered and the attention hypothesis could be directly tested via Google Search Volume, which is a proxy for investor attention. Access to financial markets data from CRSP and Compustat will be provided. Moreover, a dataset of Google Search Volume can also be provided.

Introductory Literature:

Hirshleifer, David, Sonya Seongyeon Lim, and Siew Hong Teoh, 2009, Driven to Distraction : Extraneous Events and Underreaction to Earnings News, *Journal of Finance* LXIV, 2289–2325.

Hirshleifer, David, and Siew Hong Teoh, 2009, Limited attention, information disclosure, and financial reporting, *Journal of Accounting and Economics* 36, 337-386.

Hou, Kewei, Lin Peng, and Wei Xiong, 2009, A Tale of Two Anomalies: The Implications of Investor Attention for Price and Earnings Momentum, *Working Paper*.

Jegadeesh, Narasimhan, and Sheridan Titman, 1993, Returns to buying winners and selling losers: Implication for stock market efficiency, *Journal of Finance* 48, 65-91.

TOPIC R3: Investor Attention and the Post-Earnings Announcement Drift

Classification: Empirical topic
Advisor: Florens Focke

The post-earnings announcement drift is one of the most long-standing anomalies in financial markets (it goes back at least to Ball and Brown (1968)). The drift is found in stocks after their earnings announcements, where stocks with surprisingly positive earnings tend to outperform in the future and stocks with surprisingly low earnings tend to underperform. This phenomenon implies an underreaction to earnings news that might be due to investors not paying (enough) attention to the announcement. Hou et al. (2009) use turnover as a proxy for investor attention and find that the post-earnings announcement drift is larger for stocks with lower turnover.
In this study, the student should provide a brief overview of the literature on investor attention and the post-earnings announcement drift anomaly. In the empirical part the purpose of the thesis is to replicate the main findings in Hou et al. (2009) on the relationship between post-earnings announcement drift profits and turnover. As an extension, a more recent time period could be considered and the attention hypothesis could be directly tested via Google Search Volume, which is a proxy for investor attention. Access to financial markets data from CRSP, Compustat and IBES will be provided. Moreover, a dataset of Google Search Volume can also be provided.

Introductory Literature:

Ball, R. and P. Brown , 1968, An empirical evaluation of accounting income numbers, *Journal of Accounting Research* 6, 159-177

Hirshleifer, David, Sonya Seongyeon Lim, and Siew Hong Teoh, 2009, Driven to Distraction : Extraneous Events and Underreaction to Earnings News, *Journal of Finance* LXIV, 2289–2325.

Hirshleifer, David, and Siew Hong Teoh, 2009, Limited attention, information disclosure, and financial reporting, *Journal of Accounting and Economics* 36, 337-386.

Hou, Kewei, Lin Peng, and Wei Xiong, 2009, A Tale of Two Anomalies: The Implications of Investor Attention for Price and Earnings Momentum, *Working Paper*.

TOPIC R4: Short Interest and Stock Returns

Classification: Empirical topic
Advisor: Pavel Lesnevski

Investors that participate in short selling are typically sophisticated. According to Goldman Sachs (2008), 85% of short interest comes from hedge fund industry. The most widely used measure of short sellers' activity is short interest ratio, defined as short interest over all shares outstanding. Desai et al. (2002) is one of the first studies to show consistent relationship between this measure and future stock returns. In particular, they find that heavily shorted firms at the NASDAQ exchange experience abnormally negative future returns. Boehmer, Huszar, and Jordan (2010) contribute by showing that low level of short interest ratio is a positive signal about stock future returns. In the recent working paper, Hong et al. (2015) argue that days-to-cover, which divides short interest ratio by average daily share turnover, is a theoretically better motivated measure of arbitrageurs' opinion about stock's overpricing. They show empirically that this measure outperforms short interest ratio in predicting stock future abnormal returns.
The purpose of the seminar paper is first to replicate the major results of Boehmer, Huszar, and Jordan (2010). A number of extensions are recommended. First, sample time period could be extended. Second, days-to-cover could be used as a measure of shorting activity. Finally, a number of additional risk and mispricing factors could be implemented to explain abnormal performance of shorted stocks. Access to financial markets data from CRSP and Compustat will be provided.

Introductory Literature:

Boehmer, Ekkehart, Zsuzsa R. Huszar, and Bradford D. Jordan, 2010, The good news in short interest, *Journal of Financial Economics* 96, 80–97.

Desai, Hemang, K. Ramesh, S. Ramu Thiagarajan, and Bala V. Balachandran, 2002, An Investigation of the Informational Role of Short Interest in the Nasdaq Market, *The Journal of Finance* 57, 2263–2287.

Goldman Sachs, 2008, Hedge Fund Trend Monitor, *Goldman Sachs Report*.

Hong, Harrison, Weikai Li, Sophie X. Ni, Jose A. Scheinkman, and Philip Yan, 2015, *NBER Working Paper*

TOPIC R5: **Short Interest, Investor Sentiment and Anomalies**

Classification: Empirical topic
Advisor: Pavel Lesnevski

In the presence of sentiment-driven investors stock prices can deviate from their fundamentals. Baker and Wurgler (2006) introduce a new comprehensive market-wide measure of investor sentiment. They show that this measure impacts the cross-sectional variation of stocks' mispricing. By taking long position in underpriced stock and short position in overpriced stocks investor might earn significant abnormal return. Stambaugh, Yu, and Yuan (2012) consider relation of investor sentiment to a broad set of anomalies. They hypothesize that those anomalies that are related to stock mispricing should be stronger after the periods of high sentiment. They show that this is the case for 11 anomalies they analyze. Moreover, consistent with the short sale impediments, the authors observe that the short leg of considered strategies is more profitable than the long leg.
The purpose of the seminar paper is first to replicate the major results of Stambaugh, Yu, and Yuan (2012). The student is expected to construct most but not necessary all strategies and analyze their performance at different levels of sentiment. As an extension, short interest data could be used to see whether short sellers indeed exploit profitability of these strategies. Access to financial markets data from CRSP and Compustat will be provided.

Introductory Literature:

Asquith, Paul, Parag A. Pathak, and Jay R. Ritter, 2005, Short interest, institutional ownership, and stock returns, *Journal of Financial Economics* 78, 243–276.

Baker, Malcolm, and Jeffrey Wurgler, 2006, Investor Sentiment and the Cross-Section of Stock Returns, *The Journal of Finance* 61, 1645–1680.

Desai, Hemang, K. Ramesh, S. Ramu Thiagarajan, and Bala V. Balachandran, 2002, An Investigation of the Informational Role of Short Interest in the Nasdaq Market, *The Journal of Finance* 57, 2263–2287.

Stambaugh, Robert F., Jianfeng Yu, and Yu Yuan, 2012, The short of it: Investor sentiment and anomalies, *Journal of Financial Economics* 104. Special Issue on Investor Sentiment, 288–302.

TOPIC R6: Short Interest and Corporate Earnings

Classification: Empirical topic
Advisor: Pavel Lesnevski

Financial literature finds evidence that short interest contains information about stocks' future returns (Desai et al. (2002), Asquith, Pathak, and Ritter (2005)). The question is whether the abnormal returns earned by short sellers are the result of their ability to generate superior information about firm's fundamentals or of purely speculative nature? The dissemination of value-relevant information about the firm is concentrated around the day of earnings announcements. Investors that possess superior information about firm's prospects might be able to earn high abnormal returns over the short period that day. Christophe, Ferri, and Angel (2004) are the first to use daily frequency data on short sales to uncover a significantly negative relationship between unusual levels of short selling in the days before the announcement and the post-announcement stock returns. In their recent working paper, Akbas et al. (2015) show that short sellers build their positions several months prior to the earnings announcements. Moreover, the authors argue that the ability of short interest to predict future returns disappears after controlling for changes in future fundamentals. This result is consistent with short sellers trading on the mispricing based on fundamentals.

The purpose of the seminar paper is first to replicate some major results of Akbas et al. (2013). The student is expected to work only with earnings surprises and changes in analysts' consensus earnings forecasts as proxies for fundamental news. A number of extensions are recommended. Regulation Fair Disclosure (Reg FD), introduced in October 23, 2000, restricted firm managers from privately disclosing material information to financial analysts. The student could test whether this change in regulation had an impact on the informativeness of short interest. Additionally, days-to-cover could be used as a better proxy of shorting activity as proposed by Hong et al. (2015). Access to financial markets data from CRSP, Compustat and IBES will be provided.

Introductory Literature:

Asquith, Paul, Parag A. Pathak, and Jay R. Ritter, 2005, Short interest, institutional ownership, and stock returns, *Journal of Financial Economics* 78, 243–276.

Akbas, Ferhat, Ekkehart Boehmer, Bilal Erturk, and Sorin M. Sorescu, 2013, Short Interest, Returns, and Fundamentals, *Working Paper*.

Christophe, Stephen E., Michael G. Ferri, and James J. Angel, 2004, Short-Selling Prior to Earnings Announcements, *The Journal of Finance* 59, 1845–1876.

Desai, Hemang, K. Ramesh, S. Ramu Thiagarajan, and Bala V. Balachandran, 2002, An Investigation of the Informational Role of Short Interest in the Nasdaq Market, *The Journal of Finance* 57, 2263–2287.

Hong, Harrison, Weikai Li, Sophie X. Ni, Jose A. Scheinkman, and Philip Yan, 2015, Days to Cover and Stock Returns, National Bureau of Economic Research.

TOPIC R7: Liquidity, flights and asset prices

Classification: Empirical topic
Advisor: Zorka Simon

Liquidity is a complex concept. In short, it measures the ease of trading a security. One source of illiquidity is the cost of trading. For instance, this cost can occur in the form of fees incurred at a transaction or it can be the transaction's impact on market prices of that asset. However, liquidity is not only an asset characteristic, it is well-documented in the literature that liquidity has a common component. This commonality, often referred to as liquidity risk, is priced risk factor (Pastor and Stambaugh, 2003; Acharya and Pedersen, 2005). Investors demand compensation for illiquidity, which is reflected in prices of stocks, bonds and other assets, both in the cross-section and the time series their returns (Amihud, 2002, among many others). However, some work suggests that this compensation is time varying and that liquidity of individual assets or market segments matters the most when market liquidity dries up or other increasing risks force investors into flights to safety or liquidity.

The purpose of the seminar paper is to examine one of the above topics based on chosen asset class, preferably a market of fixed income or derivative security. Ideally one can construct different measures of liquidity for the selected asset class and run a horse run between those. Alternatively, it is possible to study flight to safety or flight to liquidity flows, focusing on economically turbulent periods, following Beber, Brandt, and Kavajecz (2009) or Baele et al. (2015). And lastly, an equally interesting approach is to replicate the study of Pastor and Stambaugh (2003) or Acharya and Pedersen (2005) to see whether liquidity is priced in the chosen market segment and what policy implications can we derived from that.

Introductory Literature:

Acharya, V. V. and L. H. Pedersen, 2005, Asset pricing with liquidity risk, Journal of Financial Economics 77, 375-410.

Amihud, Y., Mendelson, H. and L.H. Pedersen, 2005, Liquidity and Asset Prices, Foundations and Trends in Finance 1, 269-364.

Beale, L., Bekaert, G., Inghelbrecht, K. and M. Wei (2015), Flights to safety, NBER Working Paper 19095

Beber, A. Brandt, M. W. and K. A. Kavajecz, 2009, Fight-to-quality or flight-to-liquidity? Evidence from the euro-area bond market, Review of Financial Studies 22, 925-957.

Pastor, L. and R.F. Stambaugh, 2003, Liquidity risk and expected stock returns, The Journal of Political Economy 111, 642-685.

TOPIC R8: **Pricing of European sovereign bonds during the financial and euro crises**

Classification: Empirical topic
Advisor: Zorka Simon

Understanding the pricing of sovereign debt is important. These securities play an important role in the portfolio choice of a wide range of investors. For instance, pension funds, insurers and other institutional investors seek these assets to incorporate into their portfolios. Moreover, the adequate understanding of the risk profile of sovereign bonds is crucial not only from the risk management perspective of investors, but also from a monetary policy point of view. By identifying the risk premia in the yields of these securities, institutions can better manage their portfolios and comply with prudential regulation, whereas governments can issue bonds that are correctly priced.

The purpose of this seminar paper is to produce a study that is closest related to recent academic work on Euro area government bonds research that considers both liquidity and credit risks. Beber, Brandt and Kavajecz (2009) disentangle the effects of liquidity and credit quality in 10 Eurozone countries to identify flight to quality and liquidity episodes. They show that liquidity is a non-trivial determinant of yields with an increasing prominence when flights occur, whereas credit quality affects valuation. On the other hand, by means of market related measures, Schwarz (2015) separates the components of yields due to liquidity and credit risk. She estimates a model of liquidity risk and finds that liquidity is priced in the cross-section of (nominal) sovereign debt. In the seminar paper one has to construct measures of bond market liquidity and sovereign risk. The following step is to see how liquidity and credit risk of issuers change over time, in reaction to the crises, and whether and if so, how these changes affect the price of sovereign securities in the paper.

Introductory Literature:

Beber, A. Brandt, M. W. and K. A. Kavajecz, 2009, Fight-to-quality or flight-to-liquidity? Evidence from the euro-area bond market, Review of Financial Studies 22, 925-957.

Schwarz, K., 2015, Mind the gap: Disentangling Credit and Liquidity in Risk Spreads, Working paper

Simon, Z., 2015, Not risk free: The relative pricing of euro area inflation-indexed and nominal bonds, Working paper, Newest version available upon request

TOPIC R9: Flights to safety and liquidity

Classification: Empirical topic
Advisor: Zorka Simon

In times of market stress, investor wealth often flows from risky securities to safe haven assets. In particular, extreme market events such as the Lehman bankruptcy or the Euro crisis, seem to trigger risk averse investors to reallocate their portfolio holdings. This results in market wide flows to bond markets, government securities or bank deposits. The academic literature, as well as financial press refers to this phenomenon as flight-to-safety or flight-to-quality. Theoretical literature has studied flights treating these episodes as given. As opposed to this, similarly to Longstaff (2004), Beber et al. (2009) or Baele et al. (2015), one can identify flight periods based on information from financial markets.

The purpose of this seminar paper is to focus on market wide flows. There are many ways of identifying these events, doing so is the central task of this paper. One can examine articles in financial press (related to textual analysis), look at market wide asset flows and analyze price distortions of safe haven assets, or estimate probabilities of such occurrences using the elaborate methodology of Beale et al (2015). Once flights are identified, discovering the relationship of flights, volatility, investor sentiment, market funding conditions and the term structure of interest rates can help us better understand the nature and policy implications of such events.

Introductory Literature:

Beale, L., Bekaert, G., Inghelbrecht, K. and M. Wei (2015), Flights to safety, NBER Working Paper 19095

Beber, A. Brandt, M. W. and K. A. Kavajecz, 2009, Fight-to-quality or flight-to-liquidity? Evidence from the euro-area bond market, Review of Financial Studies 22, 925-957.

Longstaff, 2004, The Flight-to-Liquidity Premium in U.S. Treasury Bond Prices, Journal of Business 77, 511-526.

Schwarz, K. ,2015, Mind the gap: Disentangling Credit and Liquidity in Risk Spreads, Working paper