

Master's Thesis Topics FSS 2020

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Advisor: Leah Zimmerer

S1: The Exploitation of Market Power and Stock Returns

Classification: Empirical Topic

Advisor: Frederik Horn

“So we think in terms of that moat and the ability to keep its width and its impossibility of being crossed as the primary criterion of a great business.” This is how Warren Buffet, one of the most successful investors of all times, characterizes a good investment. The moat refers to a company’s competitive advantage over others – how it keeps competitors from closing in. However, there are two different kind of moats. Either a company is more innovative and efficient than others, or it creates a moat by exploiting its market power to keep competitors out.

In a recent paper, Bessembinder (2018) finds that only an abysmal fraction (4 percent) of stocks provide higher abnormal returns to investors than investing in the treasury bills. This is at odds with conventional Finance wisdom that investing in the stock market will provide higher returns than holding bonds. It seems like equity markets only outperform treasury bills because of a few selected stocks. Furthermore, the share of firms outperforming the market has decreased since the 1980s, coincidentally the time since when concentration of market power has massively increased (Grullon et al., 2019).

This raises the question whether these firms outperform not necessarily because of innovativeness but by exploiting market power? Market power is notoriously difficult to estimate. However, De Loecker, Eeckhout, and Unger (2019) propose to estimate a firm’s markup using accounting level data. In economics, the markup a firm can charge is directly related to its market power and thereby constitutes a perfect proxy for market power.

The student should replicate the main findings of Bessembinder (2018). In a next step, the student should calculate firm markups following the methodology of De Loecker et al. (2019) and test whether the outperformance of these superstar companies is rooted in market power. Due to the difficulty of the De Loecker et al. (2019) paper, the student will be extensively supported by me regarding the methodology of that paper.

Requirements:

The empirical work requires the use of large databases, i.e. CRSP/Compustat. The databases are readily accessible for affiliates of the University of Mannheim. The candidate should feel comfortable with the use of a statistical software program (such as STATA) and econometric methods.

Introductory Literature:

Bessembinder, H. (2018). Do stocks outperform treasury bills?. *Journal of Financial Economics*, 129(3), 440-457.

Grullon, G., Larkin, Y., & Michaely, R. (2019). Are US industries becoming more concentrated?. *Review of Finance*, 23(4), 697-743.

De Loecker, J., Eeckhout, J., Unger, G. (2019), The Rise of Market Power and the Macroeconomic Implications, *The Quarterly Journal of Economics*, Forthcoming.

S2: Bargaining Power of Labor and the Exploitation of Workers

Classification: Empirical Topic

Advisor: Frederik Horn

In a recent paper, Barkai (2019) documents that since the early 1980s the US economy has experienced an enormous decline in the labor share, i.e. the share of the national income that goes to wages. Surprisingly, this is not offset by an increase in the capital cost, but rather a large increase in pure profits. This suggests a huge reallocation of wealth from workers to shareholders. Similarly, Autor et al. (2020) propose that the labor share has fallen due to the rise of so called “superstar firms”. These firms dominate the market and have a low labor share added. They argue that these are the most productive firms with the highest markups, which automatically leads to a lower labor share.

Yet, one could think of another explanation. If markets become more concentrated, firms do not only gain power over customers, but also over their employees. Thereby, real wages fall. This is problematic as it can contribute to an increase in income inequality within a country.

A perfect setting to test this hypothesis is the introduction of the “Inevitable Disclosure Doctrine” (IDD) by several US states over time. The IDD prevents key employees with insight knowledge of a firm to work for a competing firm. Thus, companies gain a lot more power over their workers. For example, Chen, Gao, and Ma (2018) exploit this setting to show that firms in these states acquire other firms with increased probability in these states as it is more difficult to hire workers on the labor market. In this case, we can test whether a decrease in labor power leads to a decrease in the labor share.

In a first step, the student should replicate the main result of Autor et al. (2020). Next, following the methodology of Chen et al. (2018), the student should explore how the introduction of the IDD affected the labor share in these states. Depending on the results, the student could utilize accounting level data to gain a deeper understanding of the nature of these firms that become superstars. Alternatively, other labor market deregulations could be exploited to further strengthen the link between power of labor and the labor share.

Requirements:

The empirical work requires the use of large databases, i.e. CRSP/Compustat. The databases are readily accessible for affiliates of the University of Mannheim. The candidate should feel comfortable with the use of a statistical software program (such as STATA) and econometric methods. The student will be provided with census data.

Introductory Literature:

Barkai, S. (2019). Declining labor and capital shares. *Journal of Finance*, Forthcoming.

Chen, D., Gao, H., & Ma, Y. (2018). Human capital driven acquisition: Evidence from the Inevitable Disclosure Doctrine. Available at SSRN 2713600.

Autor, D., Dorn, D., Katz, L.F., Patterson, C. & Van Reenen, J. (2020) The Fall of the Labor Share and the Rise of Superstar Firms. *The Quarterly Journal of Economics*, Forthcoming.

S3: Does Media Coverage of Stocks Affect Mutual Funds' Trading and Performance?

Classification: Empirical topic

Advisor: Leah Zimmerer

Managers of mutual funds are usually seen as rational agents making rational choices on the mutual fund investments. However, managers of mutual funds are humans as well who are subject to biases. They face limited attention, emotions and personal life experience at work when making their investment decisions for the mutual fund. For example, Lu et al. (2016) show that managers are impacted by distraction due to their marriage or divorce. For mutual fund manager attention is a scarce resource as well. Identifying stocks to trade from among thousands of potential listings still involves attention and high search costs. This raises the question how mutual fund managers make buying and selling decisions of stocks as those decisions require attention by the fund manager.

However, the question is how to measure attention. Fang et al. (2014) use the media coverage of stocks in the four major mass media printed newspapers as a proxy for attention for a stock. They show that mutual fund managers buy more stocks that have a high media coverage. Additionally, funds that buy more mass media covered stocks underperform funds that buy less covered stocks.

The first step of the thesis is to replicate the findings of Fang et al. (2014) for the period 2000-2018, i.e., to examine whether mutual fund managers make buying and selling decisions based on stock media attention. The second step to examine whether those decisions have an impact on the performance. Additionally, it can be examined whether the sentiment in the media articles has an impact. Furthermore, the impact of overall attention and/or attention grabbing events can be analyzed.

Requirements:

The empirical work requires the use of large databases, i.e. CRSP and/or COMPUSTAT. The databases are readily accessible for affiliates of the University of Mannheim. Additionally, the media coverage data will be provided. The candidate should feel comfortable in the use of a statistical software program (such as STATA) and econometric methods.

Introductory Literature:

Fang, L. H., Peress, J., & Zheng, L. (2014). Does media coverage of stocks affect mutual funds' trading and performance?. *The Review of Financial Studies*, 27(12), 3441-3466.

Lu, Yan, Sugata Ray, and Melvyn Teo. 2016, Limited Attention, Marital Events and Hedge Funds, *Journal of Financial Economics* 122 (3), 607–24.

S4: Do Google Searches for Stocks explain Mutual Funds' Trading and Performance?

Classification: Empirical topic

Advisor: Leah Zimmerer

Managers of mutual funds are usually seen as rational agents making rational choices on the mutual fund investments. However, managers of mutual funds are humans as well who are subject to biases. They face limited attention, emotions and personal life experience at work when making their investment decisions for the mutual fund. For example, Lu et al. (2016) show that managers are impacted by distraction due to their marriage or divorce. For mutual fund manager attention is a scarce resource as well. Identifying stocks to trade from among thousands of potential listings still involves a high search cost. This raises the question how mutual fund managers make buying and selling decisions of stocks as those decisions require attention.

However, the question is how to measure attention. Da et al. (2011) argue that Google Search Volume is a direct measure of investor attention. Because if you google a stock you are for sure paying attention to it. Thus, the question is whether mutual fund manager buy more stocks that have a high attention revealed by Google Search Volume. Additionally, do funds that buy more high attention stocks underperform funds that buy less high attention stocks?

The first step of the thesis is to examine whether mutual fund managers make buying and selling decisions based on attention measured by Google Search Volume. The second step, is to examine whether those decisions have an impact on the performance. Furthermore, the impact of overall attention and/or attention grabbing events can be analyzed.

Requirements:

The empirical work requires the use of large databases, i.e. CRSP and/or COMPUSTAT. The databases are readily accessible for affiliates of the University of Mannheim. Additionally, the Google Search Volume data will be provided. The candidate should feel comfortable in the use of a statistical software program (such as STATA) and econometric methods.

Introductory Literature:

Da, Z., Engelberg, J., & Gao, P. (2011). In search of attention. *Journal of Finance*, 66(5), 1461-1499.

Lu, Yan, Sugata Ray, and Melvyn Teo. 2016, Limited Attention, Marital Events and Hedge Funds, *Journal of Financial Economics* 122 (3), 607–24.