Fire-sales and Information Advantage when Bank-Affiliation Helps

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DISCUSSION

by

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The paper's place in the literature

It looks at **global financial market instability** issues (fire-sales) through the role of:

- International institutional investors:
  - Bartram et al (2011), Hau & Lai (2011), Jotikasthira et al (2012), Ng et al (2011)
- Banking sector information:
  - Dass & Massa (2009), Ivashina & Sun (2010), Massa & Rehman 2008), Schenone (2004)

Major findings

- Bank-affiliated funds **invest more** in firms with close relation to their banks, and this investment **delivers higher return**.

- Bank-affiliated funds **increase liquidity** and **reduce negative skewness**, especially among stocks with more fire-sales pressures in crises.

Other results

- The explanatory power of CDS spreads for stock returns increases with bank-affiliated ownership.
- Bank-affiliated trades are related (unrelated) to stock returns before (during) the crisis.
- Bank-affiliated trades are unrelated to future price reversals.

Methodology highlights

- Sample period: 2001-2009
- Data types:
  - International institutional ownership
  - Firm-level accounting and stock market
  - Bank loans
  - CDS spreads for international bond issuers
- Estimation: Panel-based regressions

C1: The unbalanced samples problem

- On average, it should be more difficult to find statistical support for bank-affiliated foreign ownership than for other foreign ownership.
  - **Reason**: The average fraction of bank-affiliated foreign holdings is less than 30%.
  - **Solution**: Adjust the estimation and inferences (especially economic) for large cross-sample differences.

C1: Example

- From Table 5 (contemporaneous returns):

	3-factor adjustment		4-factor adjustment	
	2006-07	2008-09	2006-07	2008-09
Drop in BA ownership	-0.114*** (3.95)	-0.065 (1.41)	-0.129*** (4.45)	-0.063 (1.17)
Drop in other ownership	-0.050*** (4.31)	-0.092*** (5.23)	-0.042*** (3.59)	-0.086*** (4.41)

C2: Do bank-affiliated foreign investors have true advantage?

- Bank-affiliated foreign investors may hold on to their ownership in crisis years for reasons other than genuine informational advantage.
  - **Reason**: Familiarity or some type of affinity to securities they hold can lead to the same behavior.
  - **Solution**: If information is useful, then dropped stocks should exhibit negative abnormal returns, but this is not strongly observed.

C2: Example

- From Table 5 (future returns):

	3-factor adjustment		4-factor adjustment	
	2006-07	2008-09	2006-07	2008-09
Drop in BA ownership	-0.044*	0.032	-0.050*	0.037
	(1.82)	(0.87)	(1.95)	(0.95)
Drop in other ownership	-0.010	0.048***	-0.012	0.051***
	(0.89)	(2.89)	(1.11)	(3.03)

C3: Levels versus changes

- Does an increase in the fraction of borrowing in the specific country raises stock holdings by bank-affiliated funds in that country?
  - **Reason**: Bank-affiliated funds invest more in countries in which borrowers have a close relation with their banks (Table 3).
  - **Solution**: Conduct similar tests using changes in the variables.

Other comments

- How sensitive the results for non-bank affiliated funds are to the inclusion of Norges Bank?
- Are pre-crisis results stable across time?
- Risk-adjust for liquidity.
- Include hedging as another control variable based on Massa & Zhang (2012).
- Standard errors are not clustered everywhere.

Conclusion

- Pros:
  - Rich dataset
  - Generally convincing results
- Cons (minor):
  - Some estimation issues
  - Small editorial issues

Overall: Very interesting paper!