

University of Florida
Finance 7447 (Spring 2017)
Financial Theory-II

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Stuzin 327

Mon Wed 9:35-11:30am
Heavener 260
December 23, 2016

This is an introductory doctoral corporate finance class. For this introductory course, I am assuming that you have some previous exposure to finance (the CAPM, etc.), microeconomics, and statistics. Most if not all students will have taken Fin 7446 (Financial Theory-I) in Autumn 2016, taught by Farid AitSahlia. During Autumn 2017, I will be offering an advanced doctoral corporate finance class (Fin 7808) that requires game theory and econometrics.

The articles marked with an r are required, and those with an asterisk are recommended. There will be a midterm exam, a final exam, and weekly homework assignments during the semester. Most articles can be downloaded. The midterm will be on Monday, February 27.

I. Capital Structure

A. Exogenous Operating Decisions

- * 1. Modigliani, Franco, and Merton Miller, "The Cost of Capital, Corporation Finance, and the Theory of Investment," *American Economic Review* (1958), Vol. 48, pp. 261-297.
- r 2. Miller, Merton, "Debt and Taxes," *Journal of Finance* (May 1977), Vol. 32, No. 2, pp. 261-275.
- * 3. Berens, James L., and Charles J. Cuny, "The Capital Structure Puzzle Revisited," *Review of Financial Studies* (Winter 1995), Vol. 8, No. 4, pp. 1185-1208.
- * 4. DeAngelo, Harry and Ronald Masulis, "Optimal Capital Structure Under Corporate and Personal Taxation," *Journal of Financial Economics* (March 1980), Vol. 8, No. 1, pp. 3-30.
- * 5. Graham, John R., "How Big Are the Tax Benefits of Debt?" *Journal of Finance* (October 2000), Vol. 55, No. 5, pp. 1901-1941. [This uses Tobit regression in Table VI.]
- * 6. Binsbergen, Jules H. van, John R. Graham, and Jie Yang, "The Cost of Debt," *Journal of Finance* (December 2010), Vol. 65, No. 6, pp. 2089-2136.
- * 7. Korteweg, Arthur, "The Net Benefits to Leverage," *Journal of Finance* (December 2010), Vol. 65, No. 6, pp. 2137-2170.
- r 8. Myers, Stewart C., and Nicholas Majluf, "Corporate Financing and Investment Decisions When Firms Have Information that Investors Do Not Have," *Journal of Financial Economics* (June 1984), Vol. 13, No. 2, pp. 187-222.
- r 9. Myers, Stewart C., "The Capital Structure Puzzle," *Journal of Finance* (July 1984), Vol. 39, No. 3, pp. 575-592.
- * 10. Leland, Hayne, "Corporate Debt Value, Bond Covenants, and Optimal Capital Structure," *Journal of Finance* (1994) Vol. 49, pp. 1213-1252.

B. Primarily Endogenous Operating Decisions

- r 1. Jensen, Michael, and William Meckling, "Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure," *Journal of Financial Economics* (October 1976), Vol. 3, No. 4, pp. 305-360. Read pp. 305-319 carefully, and skim over the rest.
- * 2. Ross, Stephen A., "The Economic Theory of Agency: The Principal's Problem," *American Economic Review* (May 1973) Vol. 63, No. 2, pp. 134-139.
- r 3. Stulz, René M., "Managerial Control of Voting Rights: Financing Policies and the Market for Corporate Control," *Journal of Financial Economics* (January 1988), Vol. 20, pp. 25-54.
- r 4. Myers, Stewart C., "The Determinants of Corporate Borrowing," *Journal of Financial Economics* (June 1977), Vol. 5, No. 2, pp. 146-175.
- r 5. Jensen, Michael, "Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers," *American Economic Review* (May 1986), Vol. 76, No. 2, pp. 323-29.
- * 6. Stulz, René M., "Managerial Discretion and Optimal Financing Policies," *Journal of Financial Economics* (July 1990), Vol. 26, No. 1, pp. 3-27.
- * 7. Myers, Stewart C., "Still Searching for Optimal Capital Structure," *Journal of Applied Corporate Finance* (Spring 1993), Vol. 6, pp. 4-14.
- * 8. Harris, Milton and Artur Raviv, "The Theory of Capital Structure," *Journal of Finance* (March 1991) Vol. 46, No. 1, pp. 297-355.

C. Behavioral Approaches

- * 1. Roll, Richard "The Hubris Hypothesis of Corporate Takeovers" *Journal of Business* (April 1986) Vol. 59, No. 2, Part 1, pp. 197-216.
- r 2. Heaton, J.B., 2002 "Managerial Optimism and Corporate Finance," *Financial Management* (Summer 2002), Vol. 31, No. 2, pp. 33-45.
- r 3. Graham, John R., and Campbell R. Harvey, "The Theory and Practice of Corporate Finance: Evidence from the Field," *Journal of Financial Economics* (May/June 2001) Vol. 60, No. 2-3, pp. 187-243.

D. Empirical Evidence

- r 1. Baker, Malcolm, and Jeffrey Wurgler, "Market Timing and Capital Structure" *Journal of Finance* (February 2002) Vol. 57, No. 1, pp. 1-32.
- * 2. Baker, Malcolm, Robin Greenwood, and Jeff Wurgler, 2003, "The Maturity of Debt Issues and Predictable Variation in Bond Returns," *Journal of Financial Economics* (November 2003) Vol. 70, No. 2, pp. 261-291.
- r 3. Welch, Ivo, "Capital Structure and Stock Returns," *Journal of Political Economy* (Feb. 2004) Vol. 112, No. 1, pp. 106-131. [Use the corrected version, to be distributed in class.]
- * 4. Rajan, Raghuram, and Luigi Zingales, "What Do We Know about Capital Structure? Some Evidence from International Data," *Journal of Finance* (December 1995), Vol. 50, No. 5, pp. 1421-1460.

- * 5. Fan, Joseph P.H., Sheridan Titman, and Garry Twite, "An International Comparison of Capital Structure and Debt Maturity Choices," *Journal of Financial and Quantitative Analysis* (February 2012), Vol. 47, No. 1, pp. 23-56.
- * 6. Denis, David J., "The Persistent Puzzle of Corporate Capital Structure: Current Challenges and New Directions," *The Financial Review* (2012) Vol. 47, pp. 631-643.
- * 7. Kisgen, Darren, "Do Firms Target Credit Ratings or Leverage Levels?" *Journal of Financial and Quantitative Analysis* (2009) Vol. 44, pp. 1323-1344.

II. Signaling Models

- r 1. Leland, Hayne and David Pyle, "Information Asymmetries, Financial Structure, and Financial Intermediation," *Journal of Finance* (May 1977), Vol. 32, No. 2, pp. 371-387.
- * 2. Ross, Stephen, "The Determinants of Financial Structure: The Incentive Signalling Approach," *Bell Journal of Economics* (Spring 1977), Vol. 8, No. 1, pp. 23-40.
- r 3. Flannery, Mark "Asymmetric Information and Risky Debt Maturity Choice," *Journal of Finance* (March 1986) Vol. 41, No. 1, pp. 19-37.
- * 4. Miller, Merton and Kevin Rock, "Dividend Policy under Asymmetric Information," *Journal of Finance* (September 1985), Vol. 40, No. 4, pp. 1031-52.
- * 5. Ambarish, R., Kose John, and Joseph Williams, "Efficient Signalling with Dividends and Investments," *Journal of Finance* (1987), Vol. 42, No. 2.
- * 6. Kumar, Praveen, "Shareholder-Manager Conflict and the Information Content of Dividends," *Review of Financial Studies* (Summer 1988), Vol. 1, No. 2, pp. 111-136

III. Corporate Governance

- r 1. Shleifer, Andrei, and Robert Vishny, "A Survey of Corporate Governance," *Journal of Finance* (June 1997) Vol. 52, No. 2, pp. 737-783.
- r 2. LaPorta, Rafael, Florencio Lopez-de-Silanes, Andrei Shleifer, and Robert Vishny, "Law and Finance," *Journal of Political Economy* (1998) Vol. 106, pp. 1113-1155.
- * 3. LaPorta, Rafael, Florencio Lopez-de-Silanes, Andrei Shleifer, and Robert Vishny, "Legal Determinants of External Finance," *Journal of Finance* (July 1997) Vol. 52, No. 3, pp. 1131-1150.
- * 4. Demircug-Kunt, Asli, and Vojislav Maksimovic "Law, Finance, and Firm Growth" *Journal of Finance* (December 1998) Vol. 53, pp. 2107-2137
- * 5. Grossman, Sanford, and Oliver Hart, "Corporate Financial Structure and Managerial Incentives," in J. J. McCall, ed., *The Economics of Information and Uncertainty*. Chicago: U of Chicago Press, 1982.
- * 6. Bettis, J. Carr, John M. Bizjak, and Michael L. Lemmon, "Managerial Ownership, Incentive Contracting, and the Use of Zero-Cost Collars and Equity Swaps by Corporate Insiders," *Journal of Financial and Quantitative Analysis* (September 2001) Vol. 36, No. 3, pp. 345-370.

- * 7. Claessens, Stijn, Simeon Djankov, and Larry H.P. Lang, "Separation of Ownership from Control of East Asian Firms," *Journal of Financial Economics* (Oct.-Nov. 2000) Vol. 58, No. 1-2, pp. 81-112.
- * 8. Bhagat, Sanjai and Bernard Black, "The Uncertain Relationship Between Board Composition and Firm Performance," in *The Power and Influence of Pension and Mutual Funds* (ed. R. Smith), 1998.
- * 9. Wurgler, Jeffrey, "Financial Markets and the Allocation of Capital," *Journal of Financial Economics* (Oct.-Nov. 2000), Vol. 58, 187-214.
- * 10. LaPorta, Rafael, Florencio Lopez-de-Silanes, Andrei Shleifer, and Robert Vishny, "Investor Protection and Corporate Governance," *Journal of Financial Economics* (January 2000) Vol. 58, pp. 3-27.
- * 11. Kaplan, Steven N., and Joshua Rauh, "Wall Street and Main Street: What Contributes to the Rise in the Highest Incomes?" *Review of Financial Studies* (March 2010), Vol. 23, No. 3, pp. 1004-1050.
- * 12. Djankov, Simeon, Rafael La Porta, Florencio Lopez-de-Silanes, and Andrei Shleifer, "The Law and Economics of Self-dealing," *Journal of Financial Economics* (June 2008) Vol. 88, No. 3, pp 430-465.
- * 13. Adams, Renee, Benjamin E. Hermalin, and Michael S. Weisbach, "Boards of Directors and their Role in Corporate Governance: A Conceptual Framework and Survey," *Journal of Economic Literature* (March 2010) Vol. 48, No. 1, pp. 58-107.
- * 14. Bebchuk, Lucian A., and Michael S. Weisbach, "The State of Corporate Governance Research," *Review of Financial Studies* (March 2010) Vol. 23, No. 3, pp. 939-961.
- * 15. Claessens, Stijn, Simeon Djankov, Joseph P.H. Fan, and Larry H.P. Lang, "Disentangling the Incentive and Entrenchment Effects of Large Shareholdings," *Journal of Finance* (December 2002) Vol. 57, No. 6, pp. 2741-2771.
- * 16. Lin, Chen, Yue Ma, Paul Malatesta, and Yuhai Xuan, "Ownership Structure and the Cost of Corporate Borrowing," *Journal of Financial Economics* (April 2011) Vol. 100, No. 1, pp. 1-23.
- * 17. Leuz, C., D. Nanda, and P.D. Wysocki, "Earnings Management and Investor Protection: An International Comparison," *Journal of Financial Economics* (September 2003) Vol. 69, No. 3, pp. 505-527.

IV. Payout Policy

- r 1. La Porta, Rafael, Florencio Lopez-de-Silanes, Andrei Shleifer, and Robert W. Vishny, "Agency Problems and Dividend Policies Around the World," *Journal of Finance* (February 2000) Vol. 55, No. 1, pp. 1-33.
- * 2. Lang, Larry H.P., Mara Faccio, and Leslie Young, "Dividends and Expropriation," *American Economic Review* (March 2001) Vol. 91, No. 1, pp. 54-78.
- * 3. Denis, D. J., and I. Osobov, "Why Do Firms Pay Dividends? International Evidence on the Determinants of Dividend Policy," *Journal of Financial Economics* (July 2008) Vol. 89, No. 1, pp. 62-82.

V. Initial Public Offerings and Analysts

A. Short-run Underpricing

- * 1. Rock, Kevin, "Why New Issues Are Underpriced," *Journal of Financial Economics* (Jan-Feb 1986), Vol. 15, No. 1-2, pp. 187-212.
- r 2. Beatty, Randolph P. and Jay R. Ritter, "Investment Banking, Reputation, and the Underpricing of Initial Public Offerings," *Journal of Financial Economics* (Jan-Feb 1986), Vol. 15, No. 1-2, pp. 213-232.
- r 3. Benveniste, Lawrence M. and Paul A. Spindt, "How Investment Bankers Determine the Offer Price and Allocation of New Issues," *Journal of Financial Economics* (October 1989), Vol. 24, No. 2, pp. 343-361.
- * 4. Sherman, Ann E., and Sheridan Titman, "Building the IPO Order Book: Underpricing and Participation Limits with Costly Information," *Journal of Financial Economics* (July 2002) Vol. 65, No. 1, pp. 3-29.
- * 4. Hanley, Kathleen Weiss, "The Underpricing of IPOs and the Partial Adjustment Phenomenon," *Journal of Financial Economics* 34 (October 1993), pp. 231-250.
- * 5. Hoberg, Gerard, "The Underwriter Persistence Phenomenon," *Journal of Finance* (June 2007) Vol. 62, No. 3, pp. 1169-1206.
- * 6. Hao, (Grace) Qing, "Laddering in Initial Public Offerings," *Journal of Financial Economics* (July 2007) Vol. 85, No. 1, pp. 102-122.
- * 7. Ritter, Jay R., "Equilibrium in the IPO Market," *Annual Review of Financial Economics* (2011) Vol. 3, pp. 347-374.

B. The Role of Analysts

- * 1. Dunbar, Craig, "Factors Affecting Investment Bank Initial Public Offering Market Share," *Journal of Financial Economics* (January 2000), Vol. 55, No. 1, pp. 3-41.
- * 2. Krigman, Laurie, Wayne Shaw, and Kent Womack, "Why Do Firms Switch Underwriters?" *Journal of Financial Economics* (May/June 2001) Vol. 60, Nos. 2-3, pp. 245-284.
- r 3. Loughran, Tim, and Jay R. Ritter, "Why Has IPO Underpricing Changed Over Time?" *Financial Management*, (Autumn 2004) Vol. 33, No. 3, pp. 5-37.
- * 4. Cliff, Michael, and David Denis, "Do IPO Firms Purchase Analyst Coverage with Underpricing?" *Journal of Finance* (December 2004) Vol. 59, No. 6, 2871-2901. [Logit analysis is used in Tables VI and IX.]
- * 5. Liu, Xiaoding, and Jay R. Ritter, "The Economic Consequences of IPO Spinning," *Review of Financial Studies* (May 2010) Vol. 23, No. 5, pp. 2024-2059.
- * 6. Joel Houston, Christopher James, and Jason Karceski, "What a Difference a Month Makes: Security Analyst Valuations After Initial Public Offerings," *Journal of Financial and Quantitative Analysis* (March 2006) Vol. 41, No. 1, 111-137.
- * 7. Jegadeesh, N., Joonghyuk Kim, Susan D. Krische, and Charles M.C. Lee, "Analyzing the Analysts: When Do Recommendations Add Value?" *Journal of Finance* (June 2004) Vol. 59, No. 3, pp. 1083-1124.

- r 8. Bradley, Daniel J., Bradford D. Jordan, and Jay R. Ritter, "Analyst Behavior Following IPOs: The 'Bubble Period' Evidence," *Review of Financial Studies* (January 2008) Vol. 21, No. 1, pp. 101-133. [This uses Poisson regressions in Table 7. To interpret a Poisson regression coefficient, the slope should be multiplied by the mean of the dependent variable.]

C. Quantity Rather than Price

- * 1. Lowry, Michelle B., "Why Does IPO Volume Fluctuate So Much?" *Journal of Financial Economics* (January 2003) Vol. 67, No. 1, pp. 3-40.
- * 2. Pastor, Lubos, and Pietro Veronesi, "Rational IPO Waves," *Journal of Finance* (August 2005) Vol. 60, No. 4, pp 1713-1757.
- r 3. Gao, Xiaohui, Jay R. Ritter, and Zhongyan Zhu, "Where Have All the IPOs Gone?" *Journal of Financial and Quantitative Analysis* (December 2013) Vol. 48, No. 6, pp. 1663-1692.

V. Supply and Demand in Finance

- r 1. Wurgler, Jeffrey, and Ekaterina Zhuravskaya, "Does Arbitrage Flatten Demand Curves for Stocks?" *Journal of Business* (October 2002) Vol. 75, No. 4, 583-608.
- r 2. Gao, Xiaohui, and Jay R. Ritter, "The Marketing of Seasoned Equity Offerings," *Journal of Financial Economics* (July 2010) Vol. 97, No. 1, pp. 33-52.
- * 3. Khan, Mozaffar, Leonid Kogan, and George Serafeim, "Mutual Fund Trading Pressure: Firm-level Stock Price Impact and the Timing of SEOs," *Journal of Finance* (August 2012) Vol. 67, No. 4, pp. 1371-1395.
- * 4. Greenwood, Robin, "Short- and Long-run Demand Curves for Stocks: Theory and Evidence from Cross-sectional Variation in Nikkei 225 Weights," *Review of Financial Studies* (2005), Vol. 75, pp. 607-649.

VI. Securities Offerings and Long-run Performance Measurement

- * 1. Smith, Clifford, "Investment Banking and the Capital Acquisition Process," *Journal of Financial Economics* (Jan-Feb 1986), Vol. 15, No. 1-2, pp. 3-29.
- * 2. Ritter, Jay R., "The Long Run Performance of Initial Public Offerings," *Journal of Finance* (March 1991), Vol. 46, No. 1, pp. 3-27.
- r 3. Loughran, Tim, and Jay R. Ritter, "The New Issues Puzzle," *Journal of Finance* (March 1995), Vol. 50, No. 1, pp. 23-51.
- * 4. Brav, Alon, Chris Geczy, and Paul Gompers, "Is the Abnormal Return Following Equity Issuance Anomalous?" *Journal of Financial Economics* (May 2000), Vol. 56, No. 2, pp. 209-249.
- * 5. Fama, Eugene F., "Market Efficiency, Long-term Returns, and Behavioral Finance" *Journal of Financial Economics* (September 1998), Vol. 49, No. 3, pp. 283-306.

- r 6. Loughran, Tim, and Jay R. Ritter, "Uniformly Least Powerful Tests of Market Efficiency," *Journal of Financial Economics* (March 2000), Vol. 55, No. 3, pp. 361-389.
- * 7. Lyandres, Evgeny, Le Sun, and Lu Zhang, "The New Issues Puzzle: Testing the Investment-based Explanation," *Review of Financial Studies* (November 2008) Vol. 21, No. 6, pp. 2825-2855.
- * 8. Loughran, Tim, Jay R. Ritter, and Kristian Rydqvist, "Initial Public Offerings: International Insights," *Pacific-Basin Finance Journal* (June 1994), Vol. 2, No. 2, pp. 165-199. [Table 5 uses a Tobit regression.]
- * 9. Stambaugh, Robert F., "Predictive Regressions," *Journal of Financial Economics* (December 1999) Vol. 54, No. 3, pp. 375-421. [Addresses econometric issues with return regressions with lagged stochastic regressors. Theorem 2 of Amihud, Yakov, and Clifford M. Hurvich (December 2004 *JFQA* "Predictive Regressions: A Reduced-Bias Estimation Method" Vol. 39, No. 4, pp. 813-841) includes a second-order term in their equation 7, which gives a bias of $-(\sigma_{uv}/\sigma_v^2)[(1 + 3\rho)/T + 3(1 + 3\rho)/T^2]$, and also gives a formula for computing the standard errors. Appendix D of Henderson, Jegadeesh, and Weisbach (October 2006 *JFE* Vol. 82, No. 1, pp. 63-101 "World Markets for Raising New Capital" gives a brief description of the bias formula.]
- r 10. Baker, Malcolm, and Jeffrey Wurgler, "The Equity Share in New Issues and Aggregate Stock Returns," *Journal of Finance* (October 2000) Vol. 55, No. 5, 2219-2257. [Read pp. 2219-36 only.]
- r 11. Greenwood, Robin, and Samuel G. Hanson, "Share Issuance and Factor Timing," *Journal of Finance* (April 2012) Vol. 67, No. 2, pp. 761-798.
- * 12. Ritter, Jay R., and Ivo Welch, "A Survey of IPO Activity, Pricing, and Allocations," *Journal of Finance* (August 2002), Vol. 57, No. 4, pp. 1795-1828.
- * 13. Ritter, Jay R., "Investment Banking and Securities Issuance," chapter 5 in Constantinides, Harris, and Stulz's *North-Holland Handbook of the Economics of Finance* (2003).
- * 14. DeAngelo, Harry, Linda DeAngelo, and René Stulz, "Seasoned Equity Offerings, Market Timing, and the Corporate Lifecycle," *Journal of Financial Economics* (March 2010) Vol. 95, No. 3, pp. 275-295.
- * 15. McLean, R. David, Jeffrey Pontiff, and Akiko Watanabe, "Share Issuance and Cross-sectional Returns: International Evidence," *Journal of Financial Economics* (October 2009), Vol. 94, No. 1, pp. 1-17.
- * 16. Gompers, Paul, Anna Kovner, Josh Lerner, and David Scharfstein, "Venture Capital Investment Cycles: The Impact of Public Markets," *Journal of Financial Economics* (January 2008) Vol. 87, No. 1, pp. 1-23.
- * 17. Bessembinder, Hendrik, and Feng Zhang, "Firm Characteristics and Long-run Stock Returns after Corporate Events," *Journal of Financial Economics* (July 2013) Vol. 109, No. 1, pp. 83-102.
- * 18. Hou, Kewei, Chen Xue, and Lu Zhang, "Digesting Anomalies: An Investment Approach," *Review of Financial Studies* (2015), Vol. 28, No. 3, pp. 650-705.

- * 19. Fama, Eugene F., and Kenneth R. French, "A Five-factor Asset Pricing Model," *Journal of Financial Economics* (April 2015), Vol. 116, No. 1, pp. 1-22.
- * 20. Billett, Matthew T., Mark J. Flannery, and Jon A. Garfinkel, "Frequent Issuer's Influence on Long-run Post-issuance Returns," *Journal of Financial Economics* (February 2011) Vol. 99, No. 2, pp. 349-364.
- r 21. Huang, Rongbing, and Jay R. Ritter, "The Puzzle of Frequent and Large Issuers of Debt and Equity" (2017) unpublished University of Florida working paper.

VII. Covariances in Corporate Finance

- * 1. Sahlman, William A., "The Structure and Governance of Venture Capital Organizations," *Journal of Financial Economics* (October 1990), Vol. 27, No. 2, pp. 473-521.
- * 2. Schultz, Paul, "Unit Initial Public Offerings: A Form of Staged Financing," *Journal of Financial Economics* (October 1993), Vol. 34, No. 2, pp. 25-54.
- * 3. Mayers, David, "Why Firms Issue Convertible Bonds: The Matching of Financial and Real Investment Opportunities," *Journal of Financial Economics* (January 1998), Vol. 47, No. 1, pp. 83-102.
- r 4. Froot, Kenneth A., David S. Scharfstein, and Jeremy C. Stein "Risk Management: Coordinating Corporate Investment and Financing Policies," *Journal of Finance* (December 1993) Vol. 48, No. 5, pp. 1629-1658 [You will not be accountable for sections V-VII on pp. 1645-1655].
- * 5. Oyer, Paul, "Why Do Firms Use Incentives That Have No Incentive Effects?" *Journal of Finance* (August 2004), Vol. 59, No. 4, pp. 1619-1649.