University of Florida
Finance 7808 (Autumn 2017)
Doctoral Corporate Finance

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Matherly 118
MW 9:35am-11:30am

This is an advanced doctoral corporate finance class. The prerequisite is Finance 7447, Financial Theory II (introductory doctoral corporate finance). Some knowledge of game theory and econometrics is also required. Most of the articles can be downloaded from the University of Florida's business library website.

The articles marked with an r are required reading, and those with an asterisk are recommended. There will be a midterm exam, a final exam, and weekly homework assignments during the semester. The presentation of a paper, chosen by the student, will be required. In empirical papers, various econometric techniques will be emphasized, including Logit, Nested Logit, GMM, system GMM, self selection [Heckman (1979)], Tobit, long differencing and unit roots. Each student will be expected to make one presentation.

The midterm exam will be on Monday, Oct. 16 in class. The final exam will be on Wednesday, December 13 from 3-5pm.

I. Game Theory Applications in Corporate Finance

r 1. Daniel, Kent, and Sheridan Titman, "Financing Investment Under Asymmetric Information" in Jarrow, Maksimovic, and Ziemba's 1995 North-Holland *Handbooks of Operations Research and Management Science: Finance.*

r 2. Lucas, Deborah J. and Robert L. McDonald, "Equity Issues and Stock Price Dynamics," *Journal of Finance* (September 1990), Vol. 45, No. 4, pp. 1019-1043. [Read pp. 1019-1029 only.]

r 3. Welch, Ivo, "Sequential Sales, Learning, and Cascades" *Journal of Finance* (June 1992), Vol. 47, No 2, pp. 695-732. [Skip subsection F on pp. 709-712, and note that figure 3 on p. 705 has errors. Use the version that I distribute in class, rather than downloading the published article.]

r 4. Grossman, Sanford J. and Oliver D. Hart, "Takeover Bids, the Free Rider Problem, and the Theory of the Corporation," *Bell Journal of Economics* (Spring 1980) Vol. 11, No. 1, pp. 42-64.

* 5. Shleifer, Andrei and Robert Vishny, "Large Shareholders and Corporate Control," *Journal of Political Economy* (June 1986), Vol. 94, No. 3, pp. 461-488.

* 6. Diamond, Douglas W., and Philip Dybvig "Bank Runs, Deposit Insurance, and Liquidity," *Journal of Political Economy* (June 1983) Vol. 91, No. 3, pp. 401-419.

* 7. Dutta, Prajit, and Ananth Madhavan, "Competition and Collusion in Dealer Markets," *Journal of Finance* (March 1997), Vol. 52, No. 1, pp. 245-276.

r 8. Rajan, Raghuram, "Insiders and Outsiders: The Choice between Informed and Arm's Length Debt," *Journal of Finance* (September 1992) Vol. 47, No. 4, pp. 1367-1400. [Read pp. 1367-1379 only.]

* 9. Chen, Hsuan-Chi and Jay R. Ritter, “The Seven Percent Solution,” *Journal of Finance* (June 2000), Vol. 55, No. 3, pp. 1105-1131.

* 10. Abrahamson, Mark, Tim Jenkinson, and Howard Jones, “Why Don’t U.S. Issuers Demand European Fees for IPOs?” *Journal of Finance* (December 2011), Vol. 66, No. 6, pp. 2055-2082

* 11. Hoberg, Gerard, “The Underwriter Persistence Phenomenon,” *Journal of Finance* (June 2007), Vol. 62, No. 3, pp. 1169-1206.

r 12. Liu, Xiaoding, and Jay R. Ritter, “Local Underwriter Oligopolies and IPO Underpricing,” *Journal of Financial Economics* (December 2011), Vol. 102, No. 3, pp. 579-601.

II. Capital Structure

A. Theory

* 1. Harris, Milton and Artur Raviv, "The Theory of Capital Structure," *Journal of Finance* (March 1991) Vol. 46, No. 1, pp. 297-355.

* 2. Townsend, Robert M., "Optimal Contracts and Competitive Markets with Costly State Verification," *Journal of Economic Theory* (October 1979), Vol. 21, pp. 265-293.

* 3. Shleifer, Andrei, and Robert Vishny, 1992, "Liquidation Values and Debt Capacity: A Market Equilibrium Approach" *Journal of Finance* (September 1992) Vol. 47, pp. 1343-1366.

* 4. Zwiebel, Jeffrey, "Dynamic Capital Structure under Managerial Entrenchment," *American Economic Review* (December 1996) Vol. 86, No. 5, pp. 1197-1215.

B. Empirical Evidence

* 1. Fischer, E., R. Heinkel, and J. Zechner, “Dynamic Capital Structure Choice: Theory and Tests,” *Journal of Finance* (1989) Vol. 44, pp. 19-40.

* 2. 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.

* 3. Andrade, Gregor, and Kaplan, Steven, “How Costly Is Financial (Not Economic) Distress? Evidence from Highly Leveraged Transactions That Became Distressed,” *Journal of Finance* (October 1998) Vol. 53, No. 5, pp. 1443-1493.

* 4. Hovakimian, Armen, Gayane Hovakimian, and Hassan Tehranian, “Determinants of Target Capital Structure: The Case of Dual Debt and Equity Issues,” *Journal of Financial Economics* (March 2004), Vol. 71, No. 3, pp. 517-540.

* 5. Hennessy, Christopher A. and Toni Whited, “Debt Dynamics,” *Journal of Finance* (June 2005) Vol. 60, No. 3, pp. 1129-1165.

* 6. Hovakimian, Armen, “Are Observed Capital Structures Determined by Equity Market Timing?” *Journal of Financial and Quantitative Analysis* (March 2006) Vol. 41, No. 1, pp. 221-243.

* 7. Strebulaev, Iyla, “Do Tests of Capital Structure Mean What They Say?” *Journal of Finance* (August 2007) Vol. 62, No. 4, pp. 1747-1787.

* 8. Chen, Long, and Xinlei Zhao, “Mechanical Mean Reversion of Leverage Ratios,” *Economics Letters* (2007), Vol. 95, pp. 223-229.

* 9. Lemmon, Michael L., Michael R. Roberts, and Jaime F. Zender, “Back to the Beginning: Persistence and the Cross-section of Corporate Capital Structure,” *Journal of Finance* (August 2008) Vol. 63, No. 4, pp. 1575-1608. [This paper uses system GMM.]

* 10. Petersen, Mitchell, “Simulating Standard Errors in Finance Panel Data Sets: Comparing Approaches,” *Review of Financial Studies*, (January 2009) Vol. 22, No. 1, pp. 435-480. [This paper analyzes the computation of standard errors. An important paper, but covered in another class.]

* 11. Kayhan, Ayla, and Sheridan Titman, “Firms’ Histories and Their Capital Structures,” *Journal of Financial Economics* (2007) Vol. 83, pp. 1-32.

* 12. Fama, Eugene, and Kenneth French, “Financing Decisions: Who Issues Stock?” *Journal of Financial Economics* (June 2005) Vol. 76, 549-582.

* 13. DeAngelo, Harry, Linda DeAngelo, and René M. Stulz, “Seasoned Equity Offerings, Market Timing, and the Corporate Lifecycle,” *Journal of Financial Economics* (March 2010) Vol. 95, No. 3, pp. 275-295.

* 14. Flannery, Mark, and Kasturi Rangan, “Partial Adjustment Toward Target Capital Structures,” *Journal of Financial Economics* (March 2006) Vol. 79, No. 3, pp. 469-506. [The appendix discusses some of the econometric issues.]

r 15. Chang, Xin, and Sudipto Dasgupta, “Target Behavior and Financing: How Conclusive Is the Evidence?” *Journal of Finance* (August 2009), Vol. 64, No. 4, pp. 1767-1796.

r 16. Huang, Rongbing and Jay R. Ritter, “Testing Theories of Capital Structure and Estimating the Speed of Adjustment” *Journal of Financial and Quantitative Analysis* (April 2009) Vol. 44, No. 2, pp. 237-271. [This paper uses the long differencing technique to deal with biases in estimating the coefficient on a lagged dependent variable in a dynamic panel.]

* 17. Elsas, Ralf, and David Florysiak, “Dynamic Capital Structure Adjustment and the Impact of Fractional Dependent Variables” *Journal of Financial and Quantitative Analysis* (October 2015) Vol. 50, No. 5, pp 1105-1133.

r 18. Yin, Xie (Ellie), “The Market Value Speed of Adjustment Is Slower Than You Think,” (2017) unpublished University of Florida working paper.

* 19. Öztekin, Özde, and Mark J. Flannery, “Institutional Determinants of Capital Structure Adjustment Speeds,” *Journal of Financial Economics* (January 2012) Vol. 103, No. 1, pp. 88-112.

r 20. Faulkender, Michael, Mark J. Flannery, Kristine W. Hankins, and Jason M. Smith, “Cash Flows and Leverage Adjustments,” *Journal of Financial Economics* (March 2012), Vol. 103, No. 3, pp. 632-646.

* 21. Frank, Murray Z. and Vidhan K. Goyal, “Capital Structure Decisions: Which Factors Are Reliably Important?” *Financial Management* (Spring 2009), Vol. 38, No. 1, pp. 1-37.

r 22. DeAngelo, Harry, and Richard Roll, “How Stable Are Corporate Capital Structures?” *Journal of Finance* (February 2015), Vol. 70, No. 1, pp. 373-418.

r 23. Huang, Rongbing, and Jay R. Ritter, (2017) “Corporate Cash Shortfalls and Financing Decisions,” unpublished University of Florida working paper.

III. Informational Inefficiencies, Financial Intermediation, and Financial Contracting

* 1. Rothschild, Michael and Joseph Stiglitz, "Equilibrium in Competitive Insurance Markets: An Essay on the Economics of Imperfect Information," *Quarterly Journal of Economics* (November 1976), Vol. 90, No. 4, pp. 629-49.

r 2. Scharfstein, David S. and Jeremy C. Stein, "Herd Behavior and Investment," *American Economic Review* (June 1990), Vol. 80, No. 3, pp. 465-479.

* 3. Narayanan, M.P., "Managerial Incentives for Short-term Results," *Journal of Finance* (December 1985) Vol. 40, pp. 1469-1484.

* 4. Stein, Jeremy C., "Efficient Capital Markets, Inefficient Firms: A Model of Myopic Corporate Behavior," *Quarterly Journal of Economics* (1989), pp. 655-669.

r 5. Bebchuk, Lucian, and Lars Stole, "Do Short-term Objectives Lead to Under- or Over-investment? *Journal of Finance* (June 1993) Vol. 48, pp. 719-729.

* 6. Houston, Joel, Chen Lin, and Yue Ma, “Regulatory Arbitrage and International Bank Flows,” *Journal of Finance* (October 2012) Vol. 67, No. 5, pp. 1845-1895.

* 7. Grossman, Sanford J. and Oliver D. Hart, "The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration,” *Journal of Political Economy* (August 1986), Vol. 94, No. 4, pp. 691-719.

* 8. Aghion, Philippe, and Patrick Bolton, “An Incomplete Contracts Approach to Financial Contracting” *Review of Financial Studies* (July 1992), Vol. 59, No. 3, pp. 473-494.

IV. Endogeneity in Corporate Finance

r 1. Lamont, Owen, “Cash Flow and Investment: Evidence from Internal Capital Markets," *Journal of Finance* (March 1997) Vol. 52, No. 1, pp. 83-109.

* 2. Lamont, Owen, and Christopher Polk, “Does Diversification Destroy Value? Evidence from Industry Shocks," *Journal of Financial Economics* (Jan. 2002) Vol. 63, No. 1, 51-77.

* 3. Villalonga, Belen, “Diversification Discount or Premium? New Evidence from the Business Information Tracking Series” *Journal of Finance* (April 2004) Vol. 59, No. 2.

* 4. Heckman, James J., "Sample Selection Bias as a Specification Error," *Econometrica* (1979) Vol. 47, No. 1, pp. 153–162.

r 5. Habib, Michel A., and Alexander Ljungqvist, "Underpricing and Entrepreneurial Wealth Losses in IPOs: Theory and Evidence," *Review of Financial Studies* (Summer 2001) Vol. 14, No. 2, pp. 433–458. [We will focus on the Table 3 instrumental variable regressions.]

r 6. Ljungqvist, Alexander, and William J. Wilhelm, Jr., "IPO Pricing in the Dot-com Bubble" *Journal of Finance* (April 2003) Vol. 58, No. 2, pp. 723–752. [We will focus on the 2SLS regressions in Table VI.]

r 7. Loughran, Tim, and Jay R. Ritter, "Why Has IPO Underpricing Changed Over Time?" *Financial Management* (Autumn 2004) Vol. 33, No. 3, pp. 5-37. [We will focus on the regressions in Tables 5 and 6 using instrumental variables.]

* 8. Murray, Michael P., "Avoiding Invalid Instruments and Coping with Weak Instruments," *Journal of Economic Perspectives* (Fall 2006) Vol. 20, No. 4, pp. 111–132.

* 9. Angrist, Joshua D., Kathryn Graddy, and Guido W. Imbens, "The Interpretation of Instrumental Variables in Simultaneous Equations Models with an Application to the Demand for Fish," *Review of Economic Studies* (2000) Vol. 67, pp. 499–527.

r 10. Bertrand, Marianne, Esther Duflo, and Sendil Mullainathan, "How Much Should We Trust Differences-in-Differences Estimates?" *Quarterly Journal of Economics* (2004) Vol. 119, No. 1, pp. 249–275.

r 11. Flannery, Mark J., and Kristine W. Hankins, "Estimating Dynamic Panel Models in Corporate Finance," *Journal of Corporate Finance* (February 2013) Vol. 19, No. 1, pp. 1–19.

r 12. Roberts, Michael, and Toni Whited, "Endogeneity in Empirical Corporate Finance" (2013) North-Holland's *Handbook of the Economics of Finance, Vol. 2* edited by G. Constantinides, M. Harris, and R. Stulz (2013).

r 13. Denis, David, "Doing Empirical Corporate Finance in an Endogenous World: Tutorial Session from the 2014 FMA Annual Meeting, *Journal of Applied Finance* (2015) Vol. 25, No. 1, pp. 72–85.

V. Behavioral Finance

r 1. Shleifer, Andrei, and Robert Vishny, "The Limits of Arbitrage," *Journal of Finance* (March 1997) Vol. 52, No. 1, pp. 35–55.

r 2. Hirshliefer, David, "Investor Psychology and Asset Pricing," *Journal of Finance* (August 2001), Vol. 56, No. 4, pp. 1533–1597.

* 3. Barberis, Nicholas, and Richard Thaler, "A Survey of Behavioral Finance," chapter in Constantinides, Harris, and Stulz's 2003 North-Holland *Handbook of the Economics of Finance*.

r 4. Miller, Ed, "Risk, Uncertainty, and Divergence of Opinion," *Journal of Finance* (September 1977) Vol. 32, No. 4, pp. 1151–1168.

* 5. Merton, Robert C., “A Simple Model of Capital Market Equilibrium with Incomplete Information,” *Journal of Finance* (July 1987) Vol. 42, No. 3, pp. 483–510. [The “prologue” on pages 483–487 can be skipped.]

* 6. Huberman, Gur, “Familiarity Breeds Investment,” *Review of Financial Economics* (Fall 2001) Vol. 14, No. 3, pp. 659–680.

* 7. Zhang, Donghang, “Why Do IPO Underwriters Allocate Extra Shares When They Expect to Buy Them Back?” *Journal of Financial and Quantitative Analysis* (September 2004) Vol. 39, No. 3, pp. 571–594.

* 8. Kahneman, Daniel, and Amos Tversky, “Prospect Theory: An Analysis of Decision making Under Risk,” *Econometrica* (1979) Vol. 47, pp. 263–291.

r 9. Shefrin, H.M. and M. Statman, "Explaining Investor Preference for Cash Dividends," *Journal of Financial Economics* (June 1984), Vol. 13, No. 2, pp. 253–282.

* 10. Baker, Malcolm, and Jeffrey Wurgler, “Appearing and Disappearing Dividends: The Link to Catering Incentives,” *Journal of Financial Economics* (August 2004) Vol. 73, No. 2,pp. 271–288.

r 11. Loughran, Tim, and Jay R. Ritter, “Why Don’t Issuers Get Upset About Leaving Money on the Table in IPOs?” *Review of Financial Studies*, (2002) Vol. 15, No. 2, pp. 413–443.

* 12. Edelen, Roger, and Greg Kadlec, “Issuer Surplus and the Partial Adjustment of IPO Prices to Public Information,” *Journal of Financial Economics* (August 2005) Vol. 77, No. 2, pp. 347–373.

* 13. Ince, Ozgur S., “Why Do IPO Prices Only Partially Adjust?” *Quarterly Journal of Finance* (September 2014) Vol. 4, No. 3.

* 14. Baker, Malcolm, “Market-Driven Corporate Finance” *Annual Review of Financial Economics* (December 2009) Vol. 1, pp. 181–205.

r 15. Baker, Malcolm, and Jeffrey Wurgler, “Behavioral Corporate Finance: An Updated Survey,” in North-Holland’s 2013 *Handbook of the Economics of Finance, Vol. 2*, edited by G. Constantinides, M. Harris, and R. Stulz (2013).

* 16. Stein, Jeremy C., "Rational Capital Budgeting in an Irrational World," *Journal of Business* (October 1996), Vol. 69, No. 4, pp. 429–455.

* 17. Baker, Malcolm, Joshua Coval, and Jeremy Stein, 2007, “Corporate Financing Decisions When Investors Take the Path of Least Resistance,” *Journal of Financial Economics* (May 2007), Vol. 84, No. 2, pp. 266–298.

* 18. Duffie, Darrell, “Asset Price Dynamics with Slow-Moving Capital” *Journal of Finance* (August 2010) Vol. 65, No. 4, pp. 1237–1267.

r 19. Shao, Rong (Diana), (2017) “Closed-end Fund IPOs: Sold Not Bought,” unpublished Oregon State working paper.