

The House of Finance • 2nd Quarter 2010

Newsletter Q2

- RESEARCH: Credit Rating Announcements – The Impact of the Agency's Reason, Public Information, and M&A_4
- RESEARCH: Toward a New European Financial Architecture in the Rating Sector – an Economic Analysis and Legal Solutions_6
- RESEARCH: Where Finance Meets Macro_8
- INTERVIEW: Clear Enforcement rules for the Stability and Growth Pact_10

IMPRINT

PUBLISHER:

Prof. Dr. Wolfgang König • Executive Director
House of Finance
Goethe University Frankfurt

EDITORS:

Prof. Dr. Wolfgang König
Bettina Stark-Watzinger

CONTACT:

info@hof.uni-frankfurt.de
www.hof.uni-frankfurt.de

DESIGN:

Novensis Communication GmbH
Bad Homburg

5th Edition
Number of Copies: 3.500

Copyright © by House of Finance, Frankfurt am Main

Printed in Germany

NEWSLETTER SUBSCRIPTION

The House of Finance opened in 2008. It integrates Goethe University's interdisciplinary research on finance, monetary economics, and corporate and financial law under one umbrella. Eight academic research and training units work together in the House of Finance.

As part of its aim to disseminate research results and to promote an exchange between academics and practitioners, the House of Finance issues a newsletter on a quarterly basis.

To subscribe to a printed version of this newsletter, please e-mail:
printed-newsletter@hof.uni-frankfurt.de

To subscribe to an internet version, please e-mail:
internet-newsletter@hof.uni-frankfurt

Dear Friends of the House of Finance,

There is no doubt that the liberalization of trade and services, including financial services, has delivered very positive results for the economy and employment, both in Germany and around the world. However, in the case of financial markets, liberalization and deregulation went too far. It has become evident that the financial markets need explicit rules. Current and future financiers need to pay greater attention to the main purposes of the financial sector, as well as the impact and interdependencies their actions have: potential profits, viability, responsibility and liability have to be integral to their business models.

Policy makers need to thoroughly reform the rules governing financial markets in order to create a stable, less volatile financial sector; one offering fair conditions for every market participant. This, in turn, is a necessary condition for long-term, sustainable growth. However, given the rebound in the world economy, the momentum for reform is weakening. That is why it is the German government's ambition for the G20 to follow through on the global reform agenda, while Germany moves ahead with corresponding measures at the national and European level.

Against this background, the German government has already undertaken important measures and reforms. In order to address the "too big to fail" problem, we have decided to introduce a bank restructuring regime aimed at:

- Enhancing the leeway for intervention prior to a bank's insolvency.
- Permitting the transfer of the systemically important parts of a bank, with the objective of keeping them running.
- Enabling reorganisation and restructuring by way of negotiation and without prior initiation of insolvency proceedings.

These measures will be complemented by the levying of a stability fee on banks, the proceeds of which will accrue in a restructuring fund. This fund will allow us to make financial institutions contribute to the costs of crises, as well as enable us to create a cushion against any potential future financial market turbulence.

Our efforts also focus on investor protection. Many investors lost a substantial part of their savings in the course of the financial crisis. To prevent a replication of such losses, we are currently drafting a bill that extends the scope of financial instruments covered by the investor protection provision of the Markets in

Financial Instruments Directive, and which aims to implement further measures to prevent mis-selling.

False incentives in the financial sector also need to be tackled. As a matter of fact, inappropriate compensation structures in the sector rewarded financial actors with short-term success at the expense of the stability of institutions and the very financial system itself. The German government has, therefore, moved ahead with implementing the new international guidelines on responsible compensation practices agreed at the G20 summit in Pittsburgh.

Perhaps most importantly, the financial crisis has revealed the inadequacy of existing capital and liquidity requirements for financial institutions. G20 member states have thus rightly called for higher capital and liquidity margins for banks, so that they can safely weather larger losses and longer 'dry spells' in financial markets without any risk of collapse. Here again, Germany's implementation of the new guidelines under the amendment to the EU Banking Directive and Capital Adequacy Directive will improve capital standards at European banks while work is underway to further raise the quality and level of capital and liquidity requirements globally. A final

package of measures will be decided by end of this year.

To bring new momentum to the debate on how to further enhance and strengthen financial market regulation and oversight, I hosted an international conference in Berlin this May. The event brought together high-level experts from finance ministries, central banks, international financial institutions, regulatory authorities and academia. Participants agreed that while great progress has been made in a number of areas, it is clear that the reform agenda cannot be put aside yet, and that the remaining challenges need to be addressed in a collective and consistent way.

Germany is committed to implementing the required reforms, and it is my ambition to assume a leading role in the discussions with our international partners.

Yours sincerely,



Dr. Wolfgang Schäuble
Federal Minister of Finance

Fotoquelle: BMF / Laurence Chaperon

CREDIT RATING ANNOUNCEMENTS – THE IMPACT OF THE AGENCY’S REASON, PUBLIC INFORMATION, AND M&A



Prof. Mark Wahrenburg
Goethe University



Björn Imbierowicz
Goethe University

Rating agencies are now in the limelight, both for academics and the general public. Many people seem to believe that rating agencies have become too powerful and caused undue distress by lowering ratings. The opposite view states that rating agencies are merely followers of financial market prices and have only a limited impact on market prices. In our paper, we take a closer look at the interaction between rating agency actions and market prices for stocks and credit default swaps. As a novel feature, we incorporate the reasoning behind rating agency actions into our analysis. Indeed, we find that the specific reason for a rating change matters substantially for securities markets. Furthermore, we find that other developments at the time, such as the amount of publically available information and the contemporaneous involvement of firms in M&A transactions, influence how capital markets react to rating announcements.

We are interested in the factors that induce abnormal returns in the stock market, as well as abnormal changes in spreads in the credit default swap (CDS) market, and consider not only rating changes but also rating reviews by Moody's. Rating reviews, which are usually concluded within a 3-month period, are often considered a superior source of data, as it is less likely that they are anticipated by the market.

Since ratings are intended to be an indicator of credit-related bond price risk, rating downgrades should be “bad” news for bond holders (protection sellers in the CDS market) and rating upgrades should be “good” news for bond holders. For the stock market, the situation is ambiguous. Rating downgrades could be bad news for stockholders if they are due to the weakened ability of a firm to generate future cash flows. However, they could be good news if they are the result of an increase in leverage which, according to Modigliani and Miller (1958), should increase shareholder wealth at the expense of bondholder wealth (wealth transfer hypothesis). Goh and Ederington (1993) test for this wealth transfer but are unable to confirm it.

The presence of new public information is incorporated into this study by analyzing the amount of general and rating-related newswire stories, and by investigating their impact on market prices and differences between the reason categories. These data are also used to construct a proxy measure for “surprise” which allows for testing the differing level of surprise for each type of credit rating announcement.

The paper also takes into account the fact that firms may be involved in M&A transactions at the time of rating announcements. Since this is true for roughly 40% of the sample firms concerned, involvement in M&A activity can clearly affect the overall results. This may be the case when a rating announcement is made on the very same day as an M&A announcement and the observed market reaction cannot be attributed to just the rating event.

STRONG HETEROGENEITY IN THE MARKET RESPONSE TO RATING ANNOUNCEMENTS

First, we show that our data set is marked by the same patterns found in prior research. Negative rating events induce anticipation and announcement effects in stock and CDS mar-

kets for both rating reviews and rating changes, but no post-announcement effects. Positive rating events, on the other hand, generate only an either statistically or economically insignificant outcome. For this reason, we concentrate fully on negative rating events in the subsequent analysis.

When the data are analyzed, including with respect to the specific reason given by the rating agency for its announcement, we find considerable heterogeneity. Effects prior to negative rating events in both the stock and the CDS market are mainly a result of rating actions due to one single reason only: changes in a firm's operating performance. At the same time, firms in this reason category also experience significantly higher media coverage in the pre-announcement period. It seems that the market's ability to anticipate the rating event is a result of new publically available information. On the day an announcement is made, significant abnormal returns in most reason categories can be observed. Thus, the rating agencies seem to increase the flow of valuable information to the market across all categories. However, the magnitude and even the sign of these effects differ across reason categories. When rating events are prompted by a weakening capital structure and an announcement comes as a surprise to the market, stocks even

show positive returns. The corresponding abnormal CDS spread change is positive and indicates that a wealth transfer effect may be taking place, from bondholders to stockholders, as conjectured by Jorion and Zhang (2007).

M&A INVOLVEMENT HELPS EXPLAIN MARKET REACTIONS

In the final part of the analysis, the sample is broken down further, with a separate analysis of each firm involved in M&A activity at the time of the rating announcement and vice versa: the results are striking. As regards the anticipation effect previously detected in one category, we find that this is generated by only firms with no involvement in M&A activity. The results for the announcement period surprisingly show that a weakening firm capital structure is no longer associated with significantly positive stock price reactions. Only target firms in M&A transactions are responsible for the previously stated evidence in favor of the wealth transfer hypothesis. Overall, the findings suggest that the true underlying reason for rising stock prices is not any wealth transfer from bondholders to stockholders, but the impact of M&A-related news.

The results have important implications for the interpretation of prior research and provide new insights for investors. Studies which do not

ceivably merge significant with insignificant influences, and even incorporate opposite effects, and should thus be interpreted with great caution. The detected data heterogeneity is important, not only statistically but also economically. Besides the rating itself, the reason for a rating change seems to serve as a proxy for important price-relevant information that is not incorporated in the rating information.

REFERENCES

- Goh, J. C., Ederington, L. H.** (1993) "Is a Bond Rating Downgrade Bad News, Good News, or No News for Stockholders?", *The Journal of Finance*, Vol. 48, pp. 2001–2008.
- Jorion, Ph., Zhang, G.** (2007) "Good and Bad Credit Contagion: Evidence from Credit Default Swaps", *Journal of Financial Economics*, Vol. 84, pp. 860–883.
- Modigliani, F., Miller, M.H.** (1958) "The Cost of Capital, Corporation Finance and the Theory of Investment", *The American Economic Review* 48, pp. 261–297.

The full article is available at:
<http://ssrn.com/abstract=1363920>

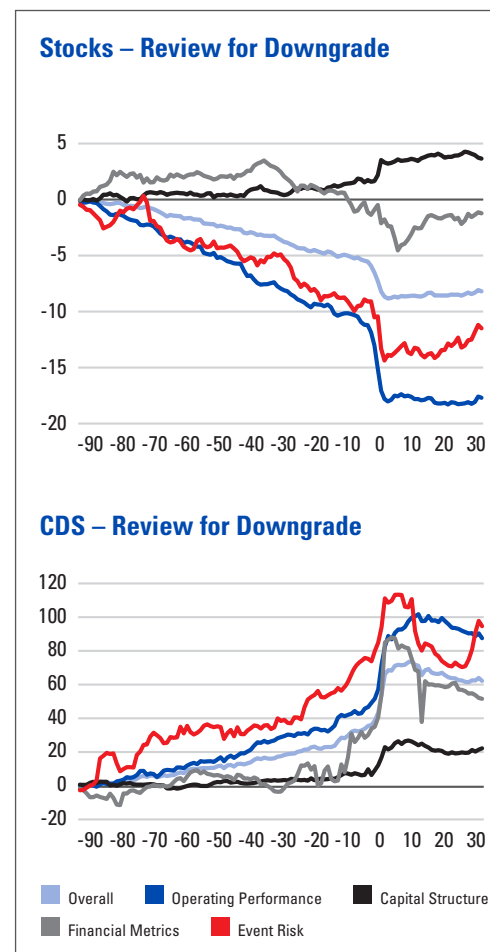


Figure 1: Average Cumulative Abnormal Performance for Rating Reviews for Downgrade and Rating Downgrades conditional on the Reason stated by Moody's

account for the reasoning behind rating events and contemporaneous M&A involvement con-

TOWARD A NEW EUROPEAN FINANCIAL ARCHITECTURE IN THE RATING SECTOR – AN ECONOMIC ANALYSIS AND LEGAL SOLUTIONS



Brigitte Haar
Goethe University

The latest downgrades of Greece, Portugal and Spain have led to renewed calls for curbs on credit rating agencies. However, economic research reveals that there are insurmountable obstacles to effective oversight. This is why legislative attempts to regulate rating agencies have been unsuccessful. Due to the recent global financial crisis and the related failure of rating agencies, new proposals in this field have been put forward. A new European regulation on rating agencies has just entered into force, which raises anew questions about regulatory effectiveness and the necessary financial architecture.

I. THE LIMITS OF REPUTATIONAL MECHANISMS

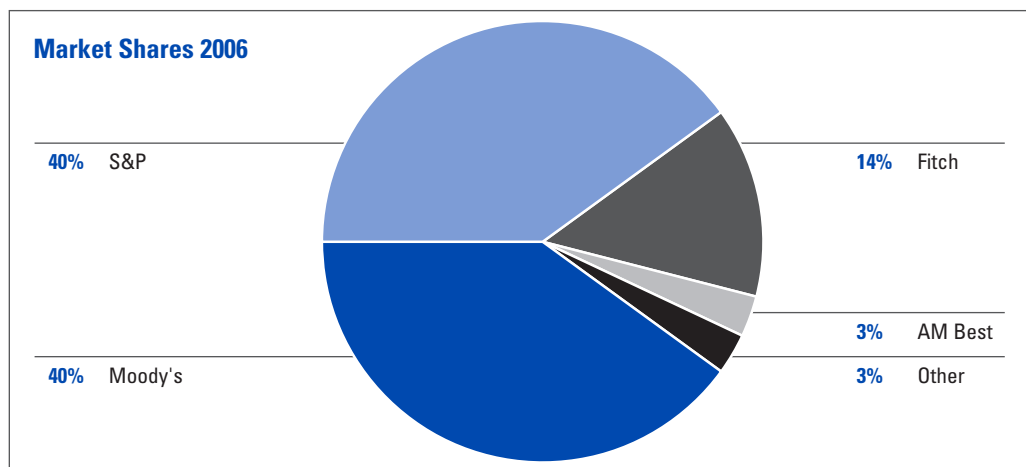
The economic problems in the rating sector are rather unique in comparison to those for other financial intermediaries. To begin with, one would expect rating agencies to be controllable ex post because their ratings can be correlated with actual defaults. Nevertheless, the functioning and potentially disciplinary

effect of the resulting reputational mechanism requires free market entry. In the rating sector, however, there seem to be insurmountable entry barriers. First, the rating industry is marked by considerable network effects. This is because investors benefit from the comparability of different ratings and the underlying rating categories and, therefore, prefer ratings from larger agencies. Over time, the two rating norm has evolved and the majority of big bond issues are now rated by both Moody's and Standard & Poor's. Secondly, if an issuer wants to switch from a known rating agency to a new market entrant, he may be subject to lock-in effects arising from the reputation value of ratings and may also face suspicions of rating shopping by going away from the well-established Moody's and Standard & Poor's. A third obstacle to competition in the rating sector is the lack of product differentiation that makes it impossible for newcomers to specialize in a certain niche market. Since investors demand very high service quality for any type of debt issue, a new entrant cannot focus on certain levels of credit risk, but at best can specialize on certain regions or industries.

II. REGULATORY RESPONSES AND REMAINING PROBLEMS

In light of these high entry barriers, it comes as no surprise that regulatory efforts have turned out to be not very effective. In Europe, there was no binding regulation until very recently. Instead, self-regulation on the basis of the IOSCO (International Organization of Security Commissions) Code of Conduct issued in 2004, which was subsequently refined in 2007 and 2008, has been implemented by most, including the major rating agencies. The IOSCO Code follows an input-oriented approach. It prescribes rigorous, systematic methodologies open to objective validation and the provision of adequate personnel and financial resources for developing, monitoring and updating ratings. During the global credit crisis, the goal to improve rating quality by way of increased competition was increasingly attacked, since competition may raise the prospect of rating shopping, and thus lead to a decrease in quality.

Such negative repercussions of serious conflicts of interest have not been adequately addressed by legislators so far. One of the most important is the issuer pay model, with about



Graph 1: Market Structure of the Rating Industry

90% of rating agency revenues coming from issuers who pay for their ratings. In addition, further concerns with respect to another conflict of interest are expressed, when rating agencies offer consulting or advisory services to issuers they rate and practically become part of the underwriting team.

III. A NEW EUROPEAN FINANCIAL ARCHITECTURE AS A WAY TOWARDS REFORM

The European Regulation (EC) No. 1060/2009 on rating agencies of 16 September 2009, which was implemented under German law on May 6, 2010, aims to diminish such conflicts of interest by focusing on improvements

to corporate governance and on timely disclosure. Rating agencies are now obliged to have independent compliance departments and to review their rating methodologies periodically. Analysts are also excluded from making any proposals or recommendations regarding the design of structured finance instruments due for a rating by their agency. Transparency is required with respect to models, methodologies, and details about both agencies' financial figures and the rotation systems to be installed under the regulation.

It is beyond doubt that the regulation addresses important questions by focusing on typical

conflicts of interest. As stipulated, enforcement is left to the member states' authorities, which have jurisdiction to register rating agencies and can, among other things, withdraw their registration and take other necessary enforcement measures. The latter have to be suitable, proportionate, have a deterrent effect, and include fines of considerable amounts in Germany. Having said this, given the intricate economic problems present in the rating market, it is clear that a public regulator can only implement second best solutions for improved rating quality. This raises the question whether there should not also be additional private enforcement possibilities. Up until now, national liability rules have failed to take hold. This failure could be overcome by rules that prescribe the disgorgement of profits made from ratings that were given in violation of the new European regime. The idea of private and public enforcement mechanisms working side by side would most probably contribute to an improvement in rating quality.

Following the de Larosi re report on EU financial market supervision, the European Commission's proposal for a regulation to establish a European Banking Authority envisages a far-reaching competence for this authority in the rating sector. How effective

this would be, of course, remains to be seen. It may be that additional complementary mechanisms, such as the private enforcement considered above or supplementary quality control by independent experts, will also be needed. Nonetheless, the new European regulation on rating agencies will soon be revised. Thus, the rating sector could be the first branch of the banking industry to constitute an important building block of a truly European financial supervisory architecture; one with, however, further potential for improvement.

REFERENCES

- Haar, B.** (2009) *"Nachhaltige Ratingqualit t durch Gewinnabsch pfung? – Zur Regulierung und ihrer Implementierung im Ratingsektor"*, Zeitschrift f r Bankrecht und Bankwirtschaft, Vol. 21, pp. 177–187.
- Hunt, J.** (2009) *"Credit Rating Agencies and the 'Worldwide Credit Crisis'"*, The Limits of Reputation, the Insufficiency of Reform, and a Proposal for Improvement, Columbia Business Law Review, Vol. 2009, pp. 109–161.

WHERE FINANCE MEETS MACRO



Ester Faia
Goethe University

The crisis of 2007-2009 has shown that banking and financial market structures can at times interact with macroeconomic conditions and monetary policies in ways that generate financial disruptions and systemic instability. Existing macro models are not well-equipped to capture these phenomena. The next generation of macro models, however, should be capable of expressing the interaction between finance and macroeconomics, and of incorporating the risks stemming from the interplay between the banking sector, financial



Ignazio Angeloni
Adviser to the Executive Board
of the ECB and a
BRUEGEL Visiting Fellow

markets and monetary policy. What implications do expansionary monetary policies have for the risk taking behavior of banks? What role do secondary markets play in terms of igniting and fostering systemic risk? What is the optimal combination vis-à-vis macro-prudential regulation and monetary policy? And what are the consequences of financial globalization for the stability of financial markets? These, among others, are the questions that remain to be answered following the financial crisis.

A recent research program by Ester Faia responds to these questions by building up a benchmark for macro models which include different aspects of the banking sector. This program involves three main lines of research.

The first of these is a work co-authored with Ignazio Angeloni (ECB and BRUEGEL), titled **“A Tale of Two Policies: Prudential Regulation and Monetary Policy with Fragile Banks”**, which studies the optimal combination of monetary and macro-prudential policies. In this paper, Angeloni and Faia introduce optimizing banks, modeled along the lines of Diamond and Rajan (JoF 2000 or JPE 2001), into a macro (dynamic stochastic general equilibrium) model. This framework is then used to study the role of banks in the transmission of shocks, the effects of monetary policy when banks are exposed to runs, and the interplay between monetary policy and Basel-like capital ratios. Banks in the model choose the optimal capital structure in order to maximize the expected return for outside investors, namely uninformed investors and bank capitalists. In equilibrium, bank leverage depends positively on the uncertainty of proj-

ects and on the bank's "relationship lender" skills, and negatively on short-term interest rates. A monetary restriction reduces leverage, while a productivity or asset price boom increases it. The transmission of all shocks points in the direction of a risk-taking channel: low interest rates, as induced by lax monetary policies or productivity booms, encourage banks to take on too much risk, thereby leading to the phenomena of exuberance and over-reaction. In this environment, pro-cyclical capital ratios are destabilizing; monetary policy can only partly offset this effect. The optimal (utility maximizing) policy combination includes mildly anti-cyclical capital ratios and a monetary policy response to asset prices or leverage.

The results of the aforementioned paper are of great policy relevance. In fact, they were recently presented to the Executive Board of the European Central Bank in a policy seminar.

A second line of research pursued by Ester Faia is the role of the secondary market for asset-backed securities (ABS) in the transmission of shocks in macro models. The financial

crisis has highlighted the limits of the "originate-to-distribute" banking model, but its nexus with the macroeconomy and monetary policy remains unexplored. In a paper titled **"Credit Risk Transfer and the Macroeconomy"**, Ester Faia builds a macro (dynamic stochastic general equilibrium) model with banks, and examines its properties with and without active secondary markets for ABS. In this model, it is assumed that banks are subject to liquidity shocks which may induce them to sell loan claims on unfinished projects in secondary markets. Both the origination and the selling activity are subject to moral hazard problems. Firms, after having obtained loans from the bank, might choose to exert a low effort and thus undermine the success of a project unless properly monitored. Through monitoring, banks acquire private information about firms' projects. This leads to a second moral hazard problem between depositors ("uninformed investors") and banks; one which becomes even more severe when the bank has the possibility of selling loans on the secondary market. The bank is inclined to offer the loan on the secondary market in the case of a liquidity shock or if it

knows that the loan is non-performing. The possibility of transferring credit not only reduces the impact of liquidity shocks on bank balance sheets, but also the bank incentive for monitoring. As a result, secondary markets free up bank capital and exacerbate the impact of productivity and other macroeconomic shocks on output and inflation. By offering the possibility of capital recycling and by reducing bank monitoring, secondary credit markets in general equilibrium allow banks to take on more risk. This research has been awarded the prestigious **Lamfalussy award**.

The last line of research refers to a paper which explores the consequences of financial globalization for an optimal policy: part of a bigger research project sponsored by an **FP7 grant** from the **European Community**, whose team leaders are Michel Juilliard, Ester Faia, Paul Levine, Albert Marcet, Joe Pearlman, Marco Ratto and Volker Wieland. More specifically, the paper is co-authored by Ester Faia and Eleni Iliopoulos and titled **"Financial Globalization, Financial Frictions and Monetary Policy"**. It studies the optimal setting of monetary policy in an envi-

ronment in which foreign lending finances expenditure on housing. The authors find that monetary policy should target the exchange rate rather than the domestic inflation rate in order to contain persistent global imbalances.

REFERENCES

- Diamond, D. W., Rajan, R. G.** (2000) *"A Theory of Bank Capital"*, Journal of Finance, Vol. 55(6), pp. 2431–2465.
- Diamond, D. W., Rajan, R. G.** (2001) *"Liquidity Risk, Liquidity Creation and Financial Fragility: A Theory of Banking"*, Journal of Political Economy, Vol. 109 (2), pp. 287–327.
- Holmström, B., Tirole, J.** (1997) *"Financial Intermediation, Loanable Funds and the Real Sector"*, Quarterly Journal of Economics, Vol. 112, pp. 663–691.

The full articles are available at:
<http://www.wiwi.uni-frankfurt.de/profs/faia/>

CLEAR ENFORCEMENT RULES FOR THE STABILITY AND GROWTH PACT

Dr. Wolf Klinz is a Member of the European Parliament (Group of the Alliance of Liberals and Democrats for Europe). Among his manifold responsibilities Dr. Klinz chairs the Special Committee on the Financial, Economic and Social Crisis and is a Member of Committee on Economic and Monetary Affairs.

The single currency was introduced without a single economic and fiscal policy. The Stability and Growth Pact was supposed to make up for this. Has the treaty proven to be a flop?

Dr. Klinz: The basic idea that states joining the single currency area have to meet specific requirements, as laid down in the Stability and Growth Pact, is still right. The challenge is that the Pact was not respected from the very onset by two founding members (i.e. Germany and France) and that a lack of discipline has also permeated other member states. If anything, the Pact has to be strengthened with a clearly defined sanction mechanism and clear enforcement rules, ranging from the 'naming

and shaming' of those who violate the Pact to loss of voting rights and penalty payments.

Has the aspect of competitiveness been sufficiently in focus?

Dr. Klinz: Clearly not! In fact, even if the Stability and Growth Pact had been respected, a loss in competitiveness would have caused serious problems for members of the European Monetary Union. Therefore, developments in the competitiveness of European Monetary Union member states have to be monitored closely and the impact of budgets on economic policy evaluated regularly.

Greece has accumulated a massive debt mountain – one which will increase even further in the coming years, regardless of what belt-tightening measures the government takes. Do the erratic price movements in financial markets demonstrate that investors doubt the prospect of a long-term consolidation?

Dr. Klinz: Indeed, markets seem to lack confidence that Greece will be able to turn the corner. This is, in my opinion, mainly due to the fact that the Greek government does not

communicate convincingly how it wants to overcome the problems caused by: 1) tax evasion; 2) corruption; and 3) the shadow economy. Statements that are precise and concrete about how progress will be made in each of these areas are vital for calming the markets.

Due to the turbulence caused by the financial crisis, the European Central Bank (ECB) made extensive use of "quantitative easing" last year. From a political perspective, how would you evaluate this step, and will the central bank be in a position to take appropriate measures for tightening monetary channels when necessary?

Dr. Klinz: The use of "quantitative easing" by the ECB last year was timely and useful. I never had any doubts that the ECB would start exiting these special measures when it no longer considered them to be necessary. I am more worried about the ECB's recent decision to accept "junk" government bonds as collateral and to buy these bonds on the secondary market. Whether the "sterilisation" of this extra money supply will happen in a timely manner and be successful remains to be seen.



Dr. Wolf Klinz
Member of the
European Parliament

KNOWLEDGE TRANSFER BETWEEN THE HOUSE OF FINANCE AND POLITICAL PRACTICE

The global financial crisis has underlined the lack of profound research results in key financial subjects and the dearth of overarching, interdisciplinary solutions for the complex, multi-layered problems we face today – for example, regarding how the capital markets can be better regulated – but also highlighted the tremendous gap between the knowledge derived from research and how this is actually used and applied in political practice – in the work, for example, of politicians, policy makers and public servants. The House of Finance sees itself as not only obliged to generate new research results, but also to improve the “translation” of these results for political practice.

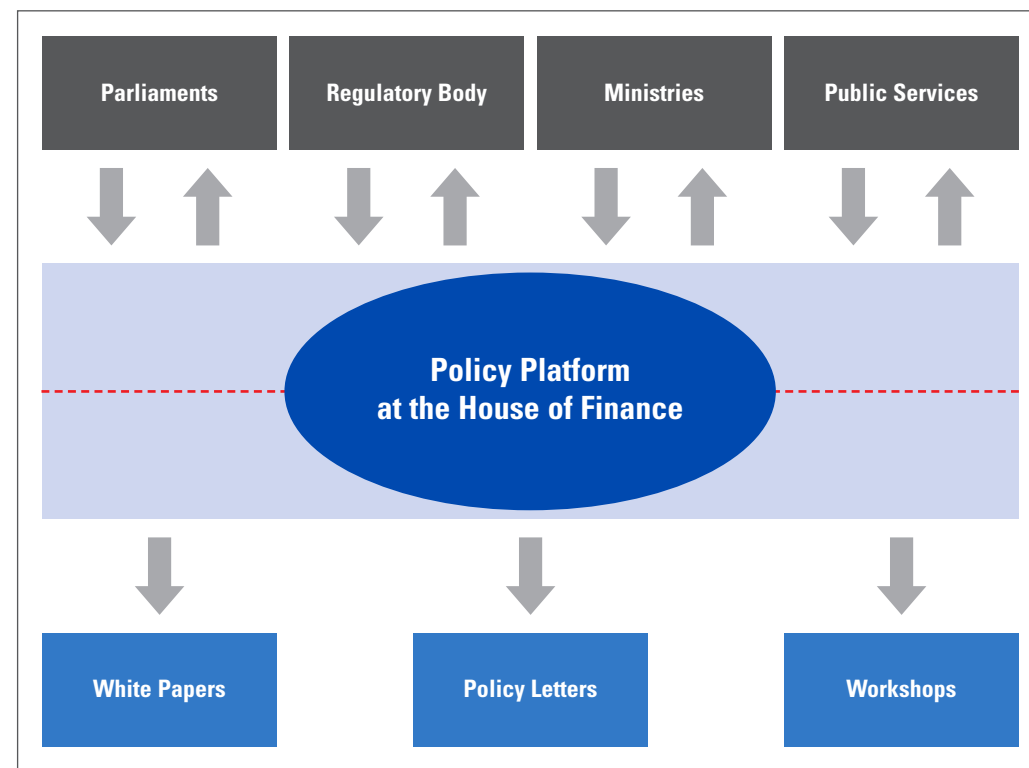
Thus, the Center for Financial Studies (CFS), the Institute of Law and Finance (ILF), and the Institute of Monetary and Financial Stability (IMFS) have jointly initiated the House of Finance Policy Platform. Recently complemented by the E-Finance Lab, this pools together the policy-relevant contributions of researchers at the House of Finance and at Goethe University’s Faculty of Economics and Business Administration and Faculty of Law.

KNOWLEDGE AT A CLICK ...

The policy-relevant publications of participating scholars can be downloaded from the Policy Platform website (www.hof.uni-frankfurt.de/de/Policy-Platform/About-us.html). These are either available as “Policy Letters”, i.e. short essays or commentaries on current policy topics usually written for the media, or as “White Papers”, which consist of research-based contributions to ongoing policy debates. The overall aim of these two products is to inform political practice – and also the general public – in a non-technical way, about issues currently pertinent to financial markets, monetary economics and central banking, and financial law. This website presently offers 40 Policy Letters and 26 White Papers and is continuously expanding.

... PLUS A MORE PERSONAL DIALOGUE

In addition, the Policy Platform has established a series of workshops with renowned policy makers. Researchers want to learn more about the specifics of real-world problems and also the results of investigations carried out by public agencies. In return, they explain their own results – as well as those of their peers around the globe – and “translate” these for political



Graph 1: Knowledge dissemination at the House of Finance Policy Platform

practice. This exchange enriches not only political practice but also academia, as evidenced by the new research projects inspired by such workshops. Prof. Axel Weber, Dr. Jens Weidmann und Jochen Sanio have all participated in

Policy Platform workshops.

For more information, please visit:

<http://www.hof.uni-frankfurt.de/de/Policy-Platform/About-us.html>

or contact info@hof.uni-frankfurt.de

SELECTED HOUSE OF FINANCE PUBLICATIONS

Bannier, C., Behr, P., Güttler, A. (2010)
“Rating Opaque Borrowers: Why are Unsolicited Ratings Lower?”,
Review of Finance, Vol. 14(2), pp. 263–294

Baums, T. (2010)
“Tim Florstedt, Zur organhaftungsrechtlichen Aufarbeitung der Finanzmarktkrise”,
in Die Aktiengesellschaft, pp. 315–323

Bruggen, G. H., Spann, M., Lilien, G. L., Skiera, B. (2010)
“Prediction Markets as Institutional Forecasting Support Systems”,
forthcoming in Decision Support Systems

Cahn, A. (2010)
“Intra-Group Loans under German Law”,
European Company Law 7, pp. 44–50

Faia, E., Campolmi, A. (2009)
“Labor Market Institutions and Inflation Volatility in the Euro Area”,
forthcoming in Journal of Economic Dynamics and Control

Gerlach, S., Assenmacher-Wesche, K. (2009)
“Monetary policy and financial imbalances: Facts and fiction”,
forthcoming in Economic Policy

Haar, B. (2010)
“Anlegerschutz in geschlossenen Fonds – Kapitalmarkteffizienz, Behavioral Finance und Anlegerkoordination als Bausteine eines neuen Regulierungsparadigmas”,
forthcoming in Festschrift für Klaus J. Hopt.

Hinz, O., Eckert, J. (2010)
“The Impact of Search and Recommendation Systems on Sales in Electronic Commerce”,
Business & Information Systems Engineering, Vol. 2 (2), pp. 67–77

Horneff, W., Maurer, R., Rogalla, R. (2010)
“Dynamic portfolio choice with deferred annuities”,
forthcoming in Journal of Banking and Finance

Kühn, C., Stroh, M. (2010)
“Optimal portfolios of a small investor in a limit order market: a shadow price approach”,
Mathematics and Financial Economics, in press

Langenbucher, K., Brenner, S., Gellings, M. (2010)
“Zur Nutzung von Insiderinformationen nach der Marktmissbrauchsrichtlinie”,
BKR – Zeitschrift für Bank- und Kapitalmarktrecht, Vol. 4, pp. 133

Vykoukal, J., Beck, R., Wolf, M. (2010)
“Impact of Pressure for Environmental Sustainability on Grid Assimilation – Empirical Results from the Financial Services Industry”,
forthcoming in Australian Journal of Information Systems

Wieland, V. (2010)
“Fiscal stimulus and the promise of future spending cuts”,
in International Journal of Central Banking, Vol. 6 (1)

Wandt, M., Sehrbrock, D. (2010)
“Regelungsziele der Solvency II-Rahmenrichtlinie”,
in Festschrift 50 Jahre Schweizerische Gesellschaft für Haftpflicht- und Versicherungsrecht, Schulthess 2010



RESEARCH OUTSIDE THE HOUSE OF FINANCE

DIE REGULIERUNG VON LEERVERKÄUFEN DE LEGE LATA UND DE LEGE FERENDA, Prof. Dr. Daniel Zimmer, LL.M., University of Bonn, and Thomas Beisen, LL.M., in Wertpapier-Mitteilungen (WM) 2010, 485–491.

By sending out wrong signals to market participants, short selling was held responsible for the excessive volatility of market prices as well as for panic sales. The authors, Professor Daniel Zimmer and Thomas Beisen, discuss the regulation of short selling. They contrast the possible risks with the potential economic benefits. This article was triggered by the prohibition on naked short selling in Germany, as discussed in a draft by the Federal Ministry of Finance. Short selling is legal here, as long as it does not violate the rules on market manipulation specified under §20 a WpHG. Nonetheless, the financial regulator BaFin prohibited naked short selling in response to the increased sensitivity of volatile markets and the massive price fluctuations that it causes. While Zimmer and Beisen view short selling as making an important contribution to the economic efficiency of capital markets, they point out the significant dangers leading up to systemic risks. They conclude that there was no legal basis for the measures BaFin adopted – none even in the draft from the Federal Ministry of Finance – and that BaFin even today lacks the legal authority for this type of action.

Sebastian Brenner, Marcel Gellings, Goethe University

GENDER AND CORPORATE FINANCE, Jiekun Huang and Darren J. Kisgen, March 16, 2009

In a recent working paper, Jiekun Huang and Darren J. Kisgen from Boston College analyze whether female chief financial officers (CFOs) differ from male CFOs in their corporate finance decisions. The authors use a difference-in-differences approach for executive transitions in order to answer this research question. They find that women make different corporate finance decisions than men. More specifically, firms with female CFOs are less likely to make acquisitions and issue debt than firms with male CFOs. These findings are found to provide evidence that women are apparently more scrutinous and exhibit less hubris when undertaking acquisition decisions. This is consistent with previous literature which finds that men are overconfident and women more risk averse. Capital markets also react favorably to significant corporate finance decisions made by firms with female CFOs. For instance, announcement returns are approximately 2 percent higher in the period around acquisitions made by firms with a female CFO compared to when acquisitions are made by firms with a male CFO. Additionally, announcement returns are higher around debt offerings and equity offerings when the firm concerned has a female CFO. These findings suggest that female CFOs do a better job of maximizing shareholder value, at least in the aforementioned context.

The full article is available at: <http://ssrn.com/abstract=1263990>

Dr. Patrick Behr, Goethe University



NEW HANDELSBLATT RANKING OF ECONOMISTS REITERATES EXCELLENCY OF HOUSE OF FINANCE RESEARCH

Prof. Roman Inderst retains his position as the best economist aged below 40 years in the new Handelsblatt ranking of economists in German-speaking areas. Also among the top 30 in this category is Prof. Ester Faia, who joined Goethe University in 2008, and Prof. Nicola Fuchs-Schündeln, who is also new to the House of Finance and previously taught at Harvard University. Meanwhile, Prof. Roman Inderst is rated fourth in terms of lifetime research output. Prof. Stefan Gerlach joins him in this ranking, achieving position 22. These good results underline that the research being conducted at Goethe University and the House of Finance is consistently of an excellent quality.



The EFLN Seminar Group

HOUSE OF FINANCE RESEARCHERS WIN AWARDS AND SCHOLARSHIPS

Yeon-Jue Emilie Yoo, linked to the Endowed Chair of Money, Currency and Central Bank Law, has won a EuroHypo scholarship for her research project "Multiline Financial Supervision in the United States of America".

E-FINANCE LAB SPRING CONFERENCE – "THE NEW FINANCIAL MARKETS INFRASTRUCTURE – TRADING AND CLEARING"

The 2010 E-Finance Lab Spring Conference on "The New Financial Markets Infrastructure – Trading and Clearing" was held on February 23. The topics discussed included the competition for execution venues in Europe, algorithmic trading, and current initiatives for increasing the integrity and transparency of OTC derivatives markets. There were 380 international participants from exchanges, clearing houses, regulators, banks, consultancies and research institutes, who gave some very positive feedback underlining the important role played by EFL conferences in generating a fruitful interaction between research and industry.

EUROPEAN FINANCIAL LAW NETWORK PH. D. CONFERENCE

The European Financial Law Network (EFLN) held its annual PhD conference from April 22-23, 2010. This conference was organized by Prof. Brigitte Haar, director of the doctoral program in Law and Economics of Money and Finance, and Prof. Theodor Baums, holder of the

Jan Ischdonat, a research assistant at the Department of Corporate and Financial Law, has won the first writing contest held by the Stiftung der Hessischen Rechtsanwaltschaft (the Hessian Bar Foundation) with his essay on

FILM INDUSTRY MEETS LAW AND FINANCE



Prof. Dr. Andreas Cahn, Dr. Dieter Wedel, Dr. Rüdiger Theiselmann

On the eve of the 2010 Corporate Finance Summit, Dr. Dieter Wedel held a lecture at a reception for guests from the financial sector, industry, law firms and academia. This successful German director and screenwriter spoke about his personal experiences and insights on business ethics. About 200 executives met for the conference, the second of its type, proper on May 6, which was hosted by Commerzbank AG and the Institute for Law and Finance (ILF).

PROF. STEFAN GERLACH NEW MANAGING DIRECTOR OF THE INSTITUTE FOR MONETARY AND FINANCIAL STABILITY



Prof. Stefan Gerlach

Prof. Stefan Gerlach succeeds Prof. Helmut Siekmann who had played a fundamental role in establishing the institute, as Managing Director of the Institute for Monetary and Financial Stability (IMFS). Prior to joining Goethe University, Prof. Gerlach worked for the Bank for International Settlements and headed the Research Department of the Hong Kong Monetary Authority. He is a member of the Monetary Experts Panel of the European Parliament's Committee on Economic and Monetary Affairs.

nary research required, given the global dimension of European financial markets. It also aims to support and nurture their research by providing an opportunity to interact with both internationally respected scholars and fellow doctoral students from other universities.

and Robert Gregory, together with Oliver Marschollek, were presented the best paper award at the 4th Pre-ICIS International Research Workshop on IT Project Management held in Phoenix, Arizona.

"Die deutsche Juristenausbildung unter dem Einfluss des Bologna-Prozesses – Eine kritische Analyse der aktuellen Reformmodelle".

E-Finance Lab researchers Prof. Roman Beck

QUARTERLY EVENT CALENDAR

JULY		AUGUST		SEPTEMBER	
Thursday, 1 st 5.15pm	MathFinance Colloquium Speaker: Prof. Dr. Ulrich Horst	Monday, 16 th Friday, 20 th 8am – 6pm	CFS and LEMF Summer School: “Law and Economics of Contracts” Speaker: Prof. Scott Baker, Washington University in St. Louis, USA, Prof. Douglas Cumming, Schulich School of Business, York University, Canada	Friday, 3 rd – Saturday, 4 th 9am – 6pm	CFS Conference: “Dynamics, Economic Growth, and International Trade, DEGIT – XV” Keynote Speakers: Samuel S. Kortum, University of Chicago, Olivier de La Grandville, University of Geneva
Monday, 5 th 5pm	EFL Jour-Fixe: “Collaboration Structures in Financial Markets – A Social Network Analysis of IPO Syndicates” Speaker: Prof. Dr. Oliver Hinz	Wednesday, 25 th – Saturday, 28 th	37th Annual Meeting of the European Finance Association Program Chair: Jan P. Krahnen <i>For more information please visit:</i> http://www.efa2010.org/home.html	Monday, 6 th 5pm	EFL Jour-Fixe: IP Telefonie im Bankenumfeld, Korbinian Humm Deutsche Bank
Wednesday, 7 th 12pm – 1pm	Brown Bag Seminar Finance Speaker: Grigori Vilkov	Monday, 30 th – September, Friday, 10 th 8am – 4pm	ILF Summer Course: “Bank- und Kapitalmarktrecht” attendance by application only	Wednesday, 8 th 5.30pm – 7pm	CFS Colloquium: “Wertpapierhandel im Umbruch: Chancen für Börsen und Ihre Kunden” Speaker: Dr. Reto Francioni, Deutsche Börse AG
Friday, 9 th 8.45am – 5.05pm	CFS Research Conference: “ECB and Ist Watchers” attendance on request only			Wednesday, 22 nd 5.30pm – 7pm	CFS Colloquium: “New Architecture for Financial Regulation” Speaker: Prof. Charles Goodhardt, London School of Economics and Political Science
Wednesday, 14 th 12pm – 1pm	Brown Bag Seminar Finance Speaker: Ahmed Barakat			Thursday, 23 rd – Friday, 24 th 9am – 6pm	CFS Research Conference: “Household Finance” Athens, Greece Management: Michael Haliassos, Goethe University Frankfurt (and others)
Friday, 16 th	ILF End of Academic Year Dinner attendance only on request				



Address:

House of Finance
Goethe University Frankfurt
Grüneburgplatz 1
D-60323 Frankfurt am Main
Contact Person:
Prof. Dr. Wolfgang König

Tel. +49 (0)69 798 34000
Fax +49 (0)69 33910
E-Mail: info@hof.uni-frankfurt.de
Internet: www.hof.uni-frankfurt.de