Research Statement for Shastri S. Sandy

I study the interaction between investors and the firm. My research focuses on empirical corporate finance, behavioral finance, and corporate governance. I am interested in answering large-picture questions on the relationship between investor behavior and firms through channels such as stock price impact, value of firm assets, and decisions taken by firm’s management. The Great Recession and consequent legislation passed to better regulate the actions of and impact on investors demonstrate the importance of properly understanding the relationship between investors and firms. Are there unintended consequences of these new regulations? Do current financial regulations achieve their desired effects, and what is the impact on the firm?

My research seeks to shed light on these questions through the examination of the relationship between investors and the firm. One of my papers examines how firms change the structure of executive compensation in anticipation of having greater shareholder interests in executive compensation. Another paper investigates whether firms use their assets to influence the actions of their equity investors. I also investigate the effect of institutional ownership on the value of the firm. I analyze whether institutional investors collude in their buying decisions, and seek to circumnavigate financial regulations. The behavioral biases of investors, the manner in which they process information, and whether their over-confident tendencies adversely influence their investment decisions and what this means for firm takeovers are also investigated in my research. Another mechanism I use to investigate the interaction between investors, specifically shareholders and the firm is proxy voting. Regulation passed after the financial crisis has placed stronger emphasis on shareholder rights as a mechanism for monitoring firms. I analyze the manner in which firms’ desires to obtain shareholder approval influence their corporate decisions.

My education and past work experiences have all helped to shape my approach to research. My training at MIT has helped me be able to efficiently process large datasets such as institutional trading data. I am also able to use Perl Script to obtain data from SEC filings. My experience as a research analyst in litigation consulting made me aware of the large economic losses possible due to inefficient relationships between investors and the firm. It also exposed me to methods of using legal precedence as instruments for economic analysis. My training at the University of Chicago emphasized the importance of identification, being able to cleanly test a hypothesis and to rule out alternative hypotheses.

Below are descriptions of my research where I attempt to rigorously quantify the relationship between investors and the firm through various identification strategies.

**Working Papers (Under review at a top journal or being revised to be sent to a top journal)**

1. *Do Underwriters Place IPO Shares in the Best Hands and Does It Matter?*  
*Abstract:*  
I test the Wall Street claim that investment banks place shares of equity offerings in the hands of "dedicated" shareholders. For IPOs where investment banks have discretion over selecting the
shareholder base, I find investment banks do not satisfy long-term shareholders’ demand for shares. Investment banks do not influence the IPOs’ shareholder composition in a manner that affects long-run returns, volatility nor monitoring of management. I find a significant correlation between shareholder composition and five-year returns following SEOs, but no correlation for IPOs. Evidence suggests these results are due to investor stock selection and not investment banks placement decisions.

2. Does Shareholder Scrutiny Affect Executive Compensation? Evidence from Say-on-Pay Voting
Featured on Harvard Law School Forum on Corporate Governance and Financial Regulation, and on MarketWatch
Accepted at Mid Atlantic Regional Conference (MARC), and FMA
Co-author: Mathias Kronlund, University of Illinois at Urbana-Champaign

Abstract:
As a result of the Dodd-Frank Act of 2010, public firms must periodically hold advisory shareholder votes on executive compensation ("say on pay"). We examine how firms change the structure and level of executive pay when they face a say-on-pay vote. Our identification strategy exploits within-firm variation in the intensity of shareholder scrutiny, by comparing compensation across years when a firm is expected to face a vote, versus years when it is not. This strategy is enabled by firms that hold votes every other two or three years, resulting in a predetermined cyclical schedule for whether a particular year’s compensation will be put to a vote. We find that firms reduce salaries to CEOs but increase their stock awards, pensions, and deferred compensation in years when they face a vote. The additional pay (mainly from stock awards) outweighs the reduction in salaries, so total pay is higher in years with a vote. These results show that increased shareholder scrutiny—in the form of holding say-on-pay votes—changes how executives are compensated. However, these changes seem mainly to improve the “optics” of pay, and, contrary to the goals of the say-on-pay regulation, have resulted in higher, not lower, total pay.

3. Capital Structure as a Strategic Negotiating Tool: Evidence from Shareholders’ Class Action Lawsuits

Abstract:
I use a negative exogenous shock to shareholders’ ability to file class action lawsuits - the passage of the 1995 Private Securities Litigation Reform Act - to test the effect of the probability of being sued on a firm’s capital structure. After the passage of the Act, firms with the highest ex-ante probability of being sued have the largest decline in leverage ratio. The change in leverage is inversely related to the time until the debt matures. These results suggest that managers use their capital structure, specifically their short-term debt, strategically as a negotiating tool in shareholder initiated class action lawsuits.

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4. **Limited Attention and Actionable Attention Shocks: Evidence from NYSE Opening and Closing Ceremonies**
Co-authors: Steve Crawford and Wesley Grey

**Abstract:**
We explore predictions from the limited attention hypothesis in the context of firms participating in NYSE’s Opening and Closing Bell ceremonies. Our unique experimental design allows us to clearly identify attention shocks and to categorize these attention shocks as actionable and non-actionable. The empirical analysis highlights a new insight: the actionability of an attention shock has a strong influence on asset pricing effects. Firms that ring the Opening Bell – investors have time during the trading day to act on the attention shock – have positive stock returns. Firms that ring the Opening Bell and are more susceptible to attention shocks – lower market capitalization firms and firms that have never participated in NYSE’s Bell ceremonies – have larger positive returns. Conversely, firms that participate in the Closing Bell ceremonies – investors have to wait till the next trading day to act – have limited returns. Our results suggest limited attention has two dimensions – quantity and time.

**Work in Progress**

1. **What are the Real Effects of Shareholder Say-on-Pay Voting**

**Brief Write-Up:**
We examine the unintended consequences of financial regulations. Firms in anticipation of having their shareholders cast a say-on-pay vote may take actions to influence their shareholders’ voting in favor of the executive compensation. There are three channels firms may take to influence a positive or “yes” say-on-pay vote. First, the firm can take actions to make shareholders happy with the firm’s performance. Second, the firm may make itself less visible to activists and proxy advising firms. If a firm is targeted by activists investors or proxy advising firms, there will be greater scrutiny on the proxy ballot items and thus less it will be likely that the say-on-pay vote will pass. Third, the firm may try to influence analysts’ opinions of the firm. We find higher returns and higher Torbin’s Q in the period leading up to the vote. We also find a lower probability of dividend decrease. These are all actions consistent with firm performance that make shareholders happy. Consistent with the theory that these characteristics are temporary, stock sales are higher during this period. There are also fewer negative 8-K filings during the period leading up to the vote. Less negative information about the firm will lead to analysts’ recommendations being more optimistic. Positive firm news make it less likely that the firm will be targeted by activists and thus less likely that there will be greater scrutiny of the proxy voting items.

2. **Frontrunning by Institutional Investors**

**Brief Write-Up:**
We study the actions of “wolf-packs”, or groups of institutional investors that have a connection with activist investors. Prior research suggests that institutional investors provide the liquidity
that facilitates the acquisition of large blocks of stock by activist investors. We find that wolf-pack investors trade differently from the rest of the institutional market. They tend to trade alongside activist investors, not against them. We also examine whether wolf-packs have the ability to earn abnormal returns on their trades. Anecdotal evidence suggests there are direct wealth transfers between wolf-pack designated institutional investors and the broader institutional markets. This wealth transfer is related to an information asymmetry situation where wolf-pack investors know about the activist’s intentions and the broader market does not. Wolf-pack trades should be abnormally profitable compared to average institutional investor trades.

3. **Initiating Mergers and Acquisitions**

**Brief Write-Up:**
The behavioral literature suggests that acquiring firms have negative announcement returns around mergers and acquisitions because these deals are driven by overconfidence. Our unique data allows us to test predictions related to the overconfidence hypothesis. Specifically, we investigate who initiates a deal, the target or the acquirer.

We identify two predictions from a behavioral market hypothesis. The first is that acquired initiated mergers will perform worse on average than target initiated mergers, under the assumption that acquirer initiated mergers are associated with relatively high overconfidence. Another prediction is that acquirer initiated mergers associated with more than one acquirer bidding will be the worst mergers in terms of post-performance because of overconfidence/optimism. In contrast, the efficient market hypothesis suggests that target initiated mergers may suffer from a lemons problem. Target initiated firms will have lower premiums to compensate the acquirer for a potential lemon problem. We find that target-initiated mergers have lower target premiums and larger acquirer announcement returns.

4. **Short-Trading by Hedge Funds**

**Brief Write-Up:**
Using a database of hedge fund trades, we examine the short selling activities of hedge funds. We find short sales comprise a small percentage of total hedge fund trades. However, we do not find short sales to be universally profitable to hedge funds. Reasons for negative returns could be due to unwinding of positions, forced sales or hedge funds not being as sophisticated as previously believed.