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FMG and Deutsche Bank Conference

The structure of regulation: Lessons from the crisis of 2007

3 March 2008



Panel Discussion: **Paul Tucker** (Bank of England), **Charles Goodhart** (FMG/LSE), **Sir Howard Davies** (LSE), **Josef Ackermann** (Deutsche Bank) and **David Webb** (FMG/LSE)

Deutsche Bank



On 3 March 2008, the FMG and Deutsche Bank hosted a special one day conference to discuss the recent financial crisis of 2007, and the lessons for regulation. Organised by **Hugo Banziger** (Deutsche Bank), **Jon Danielsson** (FMG/LSE), **Charles Goodhart** (FMG/LSE) and **David Webb** (FMG/LSE), the conference brought together academics, practitioners and specialists in the area of financial regulation.

Gillian Tett (Financial Times) opened the first session, 'Current Crisis and Historical Perspectives' by drawing upon psychology to analyse

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Corporate Governance at LSE

The London Financial
Regulation Seminar

Forthcoming FMG Public Lecture **Financial Market Stability**

Axel A Weber, President, Deutsche Bundesbank

6 June 2008, 6pm

Old Theatre, LSE

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The structure of regulation: Lessons from the crisis of 2007

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the recent crisis in terms of 'five stages of grief'. The first stage, Shock, occurred from late 2006 onwards, as the subprime losses emerged. At times overlapping with this was the second stage, Denial. In this context, she highlighted instances such as the Federal Reserve's suggestion in Spring 2007 that losses might amount only to \$50 bn. Denial, of course, gave way to Anger, anger at the US mortgage industry, the rating agencies, policymakers and banks.

In addition, she highlighted the media culpability for having failed to report on the structural problems, having 'ignored the elephant in the room' for the past seven or eight years. After focusing on the fourth stage, Depression, she discussed the possibility that talk of reform could herald the final stage, Resolution; however, she remained doubtful that true resolution had arrived.

Charles Goodhart (FMG/LSE) then discussed a few issues revealed by the recent crisis. He discussed the pre-existing deposit insurance regime, highlighting that its inclusion of co-insurance limited its ability to prevent politically embarrassing bank runs. Of course, he added, a full insurance regime would involve moral hazard; such issues emphasised the need to have 'prompt correction action' to deal with insolvent banks. He continued to discuss how shareholders might be treated in such a case, emphasising that any measure would involve some expropriation of their rights. Turning to the issue of money market operations, he highlighted the problem of stigma associated with accessing the discount window, however, he observed that making such a procedure opaque would be inconsistent with attempts to encourage transparency in the private sector. In addition, he discussed problems associated with banks' incentives to hold liquid assets; ideally, banks should hold liquid assets in good times so they can be run down in bad times. Risk sensitive CARs, according to him, also exacerbated the problem by amplifying the procyclicality of the financial system.

Session two 'Practitioner Perspectives on the Current Crisis', began with **Mark Wood** (Paternoster) who discussed the



Hugo Banziger (Deutsche Bank)

work of his company. As a regulated insurance company, Paternoster takes on companies' obligations with respect to their pension schemes. As such, it collects assets from the

pension schemes and reinvests them in capital markets. From this perspective, Mark Wood spoke about the role played by increasing life expectancy in financial markets, providing a net drain on the corporate sector. He also discussed potentially destabilising risks in financial markets, including terrorism and natural disasters such as Hurricane Katrina.

The next presentation was given by **Hugo Banziger** (Deutsche Bank) who focused on the conclusions to be drawn for financial institutions' risk management. Hugo Banziger underscored the importance of the 'originate and distribute' banking model and of maintaining dynamic balance sheets. In the case of Deutsche Bank, he drew a direct link between its requirement to frequently turn over their balance sheet, and its success in avoiding large losses during the current crisis. He further pointed to Deutsche Bank's integrated approach to risk management as another key factor behind its success during the current crisis. In particular, the tight links between the market side, treasury and the risk management division had allowed information from different markets to flow rapidly within the institution permitting Deutsche Bank to manage both liquidity and credit risk carefully in response to market developments. Hugo Banziger emphasised the ability to maintain tight structuring and origination standards during booms and the ability to provide clear information about the valuation of the securities supporting structured products. The

latter had permitted Deutsche Bank to securitise part of their mid cap portfolio during a time when markets were allegedly closed for securitisations. To conclude, he discussed how the current crisis had illustrated that there was no need for a more complex financial regulation, but for a regulatory regime which required more transparency.

The third presentation by **Daniele Nouy** (French Commission Bancaire) entitled 'Structure of regulation: Lessons from 2007' outlined some supervisory perspectives on the current credit crisis, and stressed the need to restore market participants' confidence in the banking sector which in turn would lead to an easing of liquidity conditions. Daniele Nouy highlighted four areas where the supervisory bodies could participate in this process. Firstly, more transparency regarding the valuation of banks balance sheets, with a more responsible approach by banks and auditors and with a greater emphasis on the publication of stress tests. Secondly, a strengthening of the capital adequacy framework. The first steps towards this strengthening had been taken with the implementation of the Basel II capital adequacy rules in January 2008, but she stressed that this framework could be improved to provide more detailed guidelines specifying exactly what constitutes a true risk transfer. Thirdly, the market turmoil revealed a need to enhance liquidity risk assessment with a particular emphasis on the need for creating incentives for banks to hold adequate liquidity buffers. Lastly, Daniele Nouy called for greater transparency regarding the methodology underlying credit ratings and the valuations of structured products.

The next presenter, **Charles Dallara** (International Institute of Finance), opened his presentation by comparing the 'originate and syndicate' model of banking with the new model of 'originate and distribute' and argued that this new business model is here to stay. He proceeded to reflect on the current



Charles Dallara (International Institute of Finance)

crisis and outlined the four main conditions which had led to it. The first was market participants' inadequate risk analysis and the lack of a risk management culture within some of the key players of the

financial system. Second was the complexity and opaqueness of structured products. Third was the importance of banks' compensation structure in creating incentives for banks to take risks, and the incentives for rating agencies to provide favourable ratings given that the people requesting the ratings are also their source of revenue. Lastly, the speaker pointed to how the benign liquidity conditions of the past five years had led to a favourable environment for the development of a bubble in credit markets. Charles Dallara continued his presentation by discussing the development of a best industry practice for risk management, the need for monitoring rating agencies and of the development of an appropriate ratings methodology for structured products. He pointed to Basel II as a big step in the right direction, but called for a greater harmonisation of financial regulation globally, and for an elimination of the regulatory inconsistencies between different jurisdictions. Finally, he discussed the potential for a principles based financial regulation and questioned whether pushing towards a more complicated financial regulation would help achieve financial stability.



Philipp Hildebrand (Swiss National Bank)

The conference's second session was closed by a lunch presentation from **Philipp Hildebrand** (Swiss National Bank) who presented a central bank's perspective. The speaker pointed to

the benign credit and liquidity conditions of the past five years as the main cause of the excessive risk taking which had led to the crisis. Philipp Hildebrand expressed the view that matters would get worse before the end of the crisis and expressed particular concerns about a self reinforcing feedback mechanism between the financial sector and the real economy. On the main causes of the crisis, he discussed how the worlds' largest banks had paid insufficient attention to extreme risk and how this, combined with a lack of transparency and high leverage ratios, had left banks highly vulnerable to fluctuations in the sub-prime market. He also discussed an issue raised by a number of speakers, namely the importance of financial intermediaries compensation structures

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in creating risk taking incentives, and pointed to the high watermark structure employed by hedge funds as a potentially better mechanism for providing risk taking incentives. In addressing the regulatory response to the crisis, Philipp Hildebrand expressed doubts that complicating financial regulation further would lead to a more sound financial system. The speaker called for higher capital requirements and an upper limit on leverage for financial intermediaries. He re-iterated Charles Dallara's concerns about local financial regulation in a global financial market and of the opaqueness of structured products.

The third session of the Conference began with a panel discussion on 'The response of the regulatory system to the Crisis'. The panel was chaired by **Charles Goodhart** (FMG/LSE) and included the following speakers: **Jon Danielsson** (FMG/LSE), **Bill White** (Bank for International Settlements), **Peter Praet** (National Bank of Belgium) and **Michael Krimminger** (US Federal Deposit Insurance Corporation).

In the first presentation **Jon Danielsson** discussed the widespread use of complex statistical models for internal risk management, for regulation of financial institutions, and for financial stability assessment. An over-reliance on these models was identified as one of the causes of the crisis, in particular in relation to the ratings on structured investment vehicles (SIV), which were generated by highly sophisticated statistical models. These models failed to account for the default correlation in mortgages, by assuming that mortgage defaults were relatively independent events. One of the difficulties of creating reliable models lay in capturing endogenous risk, or the risks generated and amplified within the system. Agents reacted to the measurement being used to assess individual and systemic risk, and the chosen measurement should have reflected this feedback. None of this should be taken to mean that models are not useful, and indeed they are very valuable for the analysis of frequent small events in the sphere of internal risk management, in which the reliability of the models is supported by the possibility of back-testing with abundant data. However, measuring the accuracy of these models for the purpose of large infrequent systemic events is a challenge. Recent events have exposed the unreliability of models and the importance of a good understanding of liquidity risk management and adequate internal processes.

The second speaker, **Bill White** began his presentation by characterising two schools of thought: those advocating that the source of the crisis is to be found in what is new in today's financial system, such as structured products and new market participants, versus those maintaining that the main elements of the crisis are not new and follow patterns already observed in

previous similar periods of distress. He stressed the importance of the latter, expressing concern that framing regulatory reform with a focus that ignores certain recurring themes of crises may be a mistake. One such element that fuelled this and other crises was the presence of a speculative bubble across many asset classes. The audience questioned whether he was advocating a role for central banks of bursting asset price bubbles. Bill White specified that he supported that role only when these bubbles are across a wide spectrum of asset classes and are accompanied by rapid credit growth and are having significant effects on investment and consumption. A new macro-financial stability framework is needed that focuses on systemic developments and that stresses the importance of cooperation between central banks and regulators.

The third speaker, **Peter Praet** observed that investor confidence had been compromised because the banks that were understood to be conducting their business according to the industry best practice were at the heart of the subprime crisis. The role of the market should not be underestimated, and there is evidence that markets are self-disciplining following the ongoing credit crisis. Regulation should bear this disciplining role in mind, and be careful not to add unnecessarily to the control imposed by markets. He also highlighted that regulators should be cautious about introducing a leverage ratio, something which has been discussed intensively by the Basel Committee. The main weakness of the Basel II agreements is liquidity management and regulators have neglected this aspect in favour of solvency.

In the final presentation of the session **Michael Krimminger** took a step back from the current crisis and focused instead on the key issues in bank insolvency systems. Historically the focus of the regulator has been on keeping the institution afloat, instead of keeping the functions of that institution active and

operational. What is needed is a comprehensive system promoting sound banking practices, effective supervision and credible resolution. The resolution process should be clear, based on established limits



Michael Krimminger (US Federal Deposit Insurance Corporation)



Josef Ackermann (Deutsche Bank)

regarding the use of public money, and with limited deposit insurance coverage, but prompt payment.

The final session of the conference, chaired by **David Webb** (FMG/LSE) featured a panel discussion on the

given the complexity of financial markets and institutions there is no alternative to principles-based regulation. Fourth, increased transparency was required to restore confidence in the financial system. Finally, the current crisis had exposed the limitations of regulation via capital requirements and highlighted the importance of liquidity considerations.

The third presentation was given by **Paul Tucker** (Bank of England) who focused on a number of institutional features raised by the current crisis. The first referred to fact that, just as in the monetary policy arena, regimes and the resulting incentive structures, matter for financial stability. It is in this context that the UK authority proposals for deposit protection and bank crisis resolution should be understood. Second, central bank liquidity provision to banks was subject to a potential time inconsistency problem which needed to be addressed. Third, there was a need for regulators and central banks to better explain how financial stability and monetary policy operations were interrelated.

In the final presentation, **Howard Davies** (LSE), focused on compensation schemes, incentives for risk-taking and on the future of the 'originate and distribute' financial business model. He suggested that in the medium-term there would be a revival of this model with the hope that it could be accompanied by improvements in risk management, enhanced capabilities of audit and risk committees, greater ability and credibility of international and national authorities in providing warnings of potential future crises, etc. Howard Davies argued that there is no single regulatory cure-all, but rather a long agenda of detailed work to address the regulatory deficiencies exposed in recent months.

The conference then concluded with questions from the audience.

'Conclusions for financial markets'. The opening presentation by **Charles Goodhart** (FMG/LSE) provided a summary of the main points raised during the previous sessions. The first was the importance of transparency and disclosure (although it was noted that fair value accounting in a crisis was made more difficult when there was no market price for assets). The second main point was the over-reliance of regulators in models and stress testing. The ongoing crisis was also viewed as supporting the case for principles rather than rules-based regulation. Finally, the linkages between compensation structures and risk-taking were raised.

Josef Ackermann (Deutsche Bank) began his presentation by highlighting the difficulties of revising existing compensation policies and outlined five propositions on the impact of the crisis. First, there should be a move towards a global policy framework for ensuring financial stability. Second, despite the ongoing crisis, the business model of the distribution of risks via securitisation and credit risk transfer would continue. Third,

The conference was organised with the support of **Deutsche Bank AG**.

The conference brief and presentations are available on the FMG website <http://fmg.lse.ac.uk>

The conference is now available to **watch online on the FMG website**.

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Axel A Weber, President, Deutsche Bundesbank

Financial Market Stability



Axel A Weber (Deutsche Bundesbank)

On 6 June FMG will host a lecture by **Axel A Weber**, President of Deutsche Bundesbank who, in the light of current tensions in financial markets, will look at financial market stability from a central bank's perspective. **Charles Goodhart** (Programme Director, Regulation and Financial Stability, FMG/LSE) will be chairing the event.

Professor Weber has been President of Deutsche Bundesbank since April 2004 and a member of the Governing Council of the European Central Bank. He is also a governor of the International Monetary

Fund and a member of the Board of Directors of the Bank for International Settlements.

From 1976 to 1982 Professor Weber studied economics at the University of Constance. He worked as a research assistant for monetary economics from 1982 to 1992, and the University of Siegen awarded him a doctorate (Dr rer pol) in 1987.

Professor Weber taught at the Rheinische Friedrich Wilhelms University Bonn as Professor of Economic Theory (1993-98). Between 1998 and 2001 he held the chair of Applied Monetary Economics at the Johann Wolfgang Goethe University Frankfurt am Main and was, in addition, Director of the Center for Financial Studies (CFS) in Frankfurt am Main (1998-2002). From 2001 until 2004 Professor Weber taught international economics at the University of Cologne.

In 2002 Professor Weber was appointed to the German Council of Economic Experts, a task he had to give up upon becoming President of Deutsche Bundesbank.

Professor Weber is married and has two children.

The lecture is organised as part of the '**London Financial Regulation Seminar**' and the '**Corporate Governance at LSE**' programmes.

Attendance to this event requires registration and a ticket.

To register email s.b.mohabeer@lse.ac.uk or call **020 7955 6301/7002**.

More information is available on the FMG website <http://fmg.lse.ac.uk>

Corporate Governance at LSE

Capital Market Summit

11 January 2008



THE MILLSTEIN CENTER
FOR CORPORATE GOVERNANCE AND PERFORMANCE

A high profile Corporate Governance event took place at the London School of Economics and Political Science on 11 January 2008 as part of Corporate Governance at LSE, a Financial Markets Group research programme, and in conjunction with the Millstein Center for Corporate Governance and Performance at the Yale School of Management. This event consisted of a meeting of experts and business and investment leaders, and formed part of the Millstein Centre's Capital Markets Research Project entitled 'Regulators and New Forces in the Capital Markets: Lead, Follow or Get Out of the Way?'.



Sir Howard Davies (LSE)

The purpose of the meeting was to discuss the impact of recent changes in world capital markets on boards of directors, regulators and policy makers. The main focus was on powerful investment entities such as sovereign wealth funds, hedge funds and private equity funds, whose motivations and methods might be different from those of conventional institutional investors. A

recent report by the McKinsey Global Institute, 'The New Power Brokers: How Oil, Asia, Hedge Funds and Private Equity Are Shaping Global Markets' served as background for the discussion. The meeting began with a brief comment on this report, highlighting the main conclusions, followed by a discussion chaired by **Sir Howard Davies**, the Director of LSE. This discussion was structured in three parts. The first part focused on the impact of shareholder activism on existing corporate governance mechanisms and on company strategy, and highlighted possible conflicts of interest between the new investors and established institutional investors. It also examined the differences in corporate governance practices among private equity firms. The purpose of the second part of the discussion was to clarify the role of regulators and supervisors in an increasingly global financial market. Finally, the last part focused on the increasing importance

of foreign investors and the role of new investors in the area of corporate social responsibility.

The opening remarks were made by **Sir Geoffrey Owen** (Department of Management, LSE), who welcomed the participants on behalf of the London School of Economics and Political Science and the Financial Markets Group.

Ira Millstein (Millstein Center, Yale School of Management) presented the Millstein Center for Corporate Governance, which was created two years ago as a research centre with the purpose of studying the role of the corporation in society. Under this broad umbrella, the centre has engaged in a number of research projects and has organised conferences on themes such as the role of independent chairs, the role of mutual funds and the importance of rating agencies. More recently, the center has shifted its focus to the impact of changes in the capital markets.

Stephen Davis (Millstein Center, Yale School of Management), the Capital Markets programme director of the Millstein Center, opened his comments by quoting Nicolas Sarkozy: 'In the face of the increasing power of speculative funds, which are extremely aggressive, and of sovereign wealth funds which do not obey economic logic, there's no reason for France not to react'. On the other hand, he mentioned how these same funds have been used as rescue devices by the corporate boards of some financial institutions in the US, when those institutions ran into difficulties as a result of the sub-prime crisis. These major changes in capital markets were the key focus of The Millstein Center's project.

After these introductory remarks, the participants briefly introduced themselves. This introduction was then followed by a summary of the McKinsey Global Institute Report: 'The New Power Brokers: How Oil, Asia, Hedge Funds and Private Equity Are Shaping Global Markets', by **Conor Kehoe** (McKinsey & Company). He started by presenting the questions this report aims to answer: who are the new power brokers in the global market, how big are they, what impact are they having and what fears are they generating? These new players are primarily the petro dollar funds and Asian central banks which together control about seven trillion dollars, and hedge funds and private equity funds, representing about two trillion dollars. Although these players are not new in the market, their significance



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is increasing, especially when compared with traditional institutional players like the insurance industry, pension funds and mutual funds which control about 20 trillion dollars each. These new players are growing quickly, at about 20 per cent a year, while traditional funds grow at around 8 per cent. Even considering a scenario of increasing oil costs and reduced trade between China and US, McKinsey estimates these players will be worth 20 trillion dollars in the next four or five years. The impact of these new players, especially sovereign funds and petrodollars funds, has been to reduce US long term interest rates by about 75 basis points, and also to redirect more money to developing and emerging markets. Another effect has been to increase the availability of long term high risk/reward investments. Equally, the presence of these players has increased activism, particularly in the case of private equity and hedge funds which have been quite active in terms of corporate governance; this trend is likely to continue. Another impact is the redefinition of boundaries, in particular between private equity and public markets. In 2006, for instance, there were more private transactions in the NYSE than new IPO's. The other relevant boundary is between that which is government-related and that which is commercial; this boundary is becoming blurred. The major concern that arises from these issues is the fact that sovereign funds might have motives other than economic interest, although McKinsey believes that today this is not the case. Other concerns relate to the possibility of asset price bubbles due to extra liquidity, or debt disasters. However, private equity is still quite small and therefore unlikely to be big enough to generate a debt crisis. A final concern is the fact that hedge funds might exacerbate financial market instability. Again, McKinsey is optimistic on this, since hedge fund strategies that are gaining momentum are increasingly driven by corporate events and not by market co-movements.

This summary was followed by a discussion chaired by Sir Howard Davies. Ira Millstein suggested that both a macro and a micro approach to this issue should be taken; in particular, attention should be focused on the impact at the board room level in terms of actions, attitudes and relations with other participants in the process. Based on his own experience, he also argued it was important to analyse the ultimate impact of these changes on corporate performance.

Conor Kehoe was asked about McKinsey's perspective on the dynamic effects of activism, namely by sovereign funds. He said he expects sovereign funds increasingly to exhibit this kind of behaviour. In this context, **Liz Murrall** (Investment Management Association) showed some concern about the true motivation of such activism; she referred to the political interests of countries engaged in activism, especially low transparency countries, and about the role of ethics and social responsibility in those practices. Again, Connor Kehoe pointed out that the evidence so far suggests the motivation is purely economic. The cases of Norway, Sweden, China and Russia were referred as examples for different motivations.

Antoine Faure-Grimaud (FMG/LSE) briefly described the research work that has been done at the Financial Markets Group on the topic of Corporate Governance. Focusing on the UK case, one of the projects consisted in studying the UK's, 'comply-or-explain' system. According to UK rules, firms either comply

with a set of principles or if they do not, they need to provide an explanation for why the firm has decided not to comply. The main finding from this project was that, in general, this procedure works. In particular, the number of firms that comply has increased considerably over time, although there is a significant number of firms that do not provide an explanation if they do not comply. During the period of 1998 to 2003, approximately 20 per cent of the firms who did not comply also did not provide an explanation. Another finding is that explanations are frequently poor. Antoine Faure-Grimaud classified the UK system as an interesting benchmark, because of its flexibility. It is his feeling that this flexible approach works, although in some cases it works too well, in the sense that some firms, though willing to explain why they do not comply, at the same time provide weak and vague explanations. He also shared some of the concerns presented earlier, about the new role of sovereign funds in the corporate governance practices, and about the practical impacts of these changes in the way these rules are implemented.



Paul Myners

Paul Myners described the relationship between institutional investors, companies and directors in the UK as encompassing varying degrees of tensions but rarely comfortable. Directors are often disappointed with institutional investors' understanding of company strategy and value creation that is usually reflected in their compensation structure. He was concerned that

the person who owns the shares is not the person who makes decisions concerning corporate governance. He also suggested that companies may fail to explain why they are not complying, simply because they do not want to make their reasons public. Finally, he highlighted the significant differences between the governance mechanisms in the UK as compared with the US, despite the similarity between the two economies.

Antonio Borges (Goldman Sachs International) provided some insights on these differences in corporate governance between the US and the UK. He stated that the UK model is far superior to the US because of its institutional approach. He also pointed out that, in the US, capital markets operate much more vigorously, being much more active and acting as a disciplinary mechanism for CEOs. He then made some clarifications on the role of the new players in the market. The recent good market conditions have made possible a lot of financial innovation. As a result, conditions enabled the development of new funds. In the case of private equity funds, they can now better deal with risk. Firms can now more easily be taken out of the market, either in a friendly way, in a private equity deal, or in a more hostile way. He believes that this new model is well accepted in the US, but

there are a lot of concerns in Europe. On top of this, there is the role of sovereign wealth funds that might be politically motivated.

David Pitt-Watson (Hermes Equity Ownership Services) argued that sovereign wealth funds are not a new problem in the UK, and he gave the example of golden shares and EADS. It was very important for these funds to be clear about their rules and objectives. Again, he gave the example of Norwegian funds which are considered to be great investors despite existing political motivations and emphasised the role of OECD in promoting the clarification of the goals of these new funds. He showed some concerns regarding hedge funds, saying that there are only a small proportion of those funds engaging in serious shareholder activism despite all of the noise they create in newspapers and other press. He pointed to the separation between the ownership role and the economic role in companies, arguing that this might cause some confusion in the market. He gave the example that a shareholder with a three per cent position in a company has to declare it, although a hedge fund with a short position of the same amount in the same company does not. He finished by saying that a lot of work needs to be done to clarify this situation and that particular attention should be paid to the role of information systems, especially the role of rating systems and accounting standards. He demanded more transparency, accountability and responsibility, in both small and large companies, so that different market players and board members do not get confused, and he questioned the function of shareholders' activism in this process.

Paul Davies (Department of Law, LSE) commented on the two previous remarks and started by pointing out some additional differences between the US and UK corporate laws, relating to tender offers or take-overs. He pointed out that in the UK, a firm neutrality rule is imposed on the board of targeted companies, whereas in the US the poison pills can put the management of the target company in a better position in the negotiation. With regard to sovereign wealth funds, he said that the UK has a unique system where there is no particular worry about shareholders motivations and that it is difficult in those institutions to say where the line lies between financial and political motivations.

Regarding the role of private equity funds, **Norman Pearlstine** (The Carlyle Group) suggested that some discussion was needed on the split between management and directors, and corporate governance mechanisms. He pointed out that hostile takeovers are less likely to occur in a context of private equity. He also added that some managers welcome these private equity funds because they believe this will make their life easier while managing the firm.

Sir Christopher Hogg (Financial Reporting Council) focused on the relation between corporate governance and firm performance; looking at the McKinsey report from two angles. Firstly, he argued that powerful shareholders might have conflicting motivations (political and economic). Secondly he said there was a concern among the boards of companies about ownership stability and its impact on long term strategies. He pointed

out that the power of private equity lay in its ability to have a long term perspective, as compared with the shorter term of other investors.

John Plender (Financial Times Group) commented on the role of private equity and sovereign wealth funds as *recycling* investors, arguing that equity is far better than debt as a recycling mechanism because of the threats of excessive debt. Based on the expectation that more and more companies are going to be taken over by private equity and sovereign wealth funds, he asked what would be the impact of this on disclosure regimes and requirements. He then pointed out that the focus of the discussion should eventually change to more traditional institutions, such as commercial banks and investment banks, and to the impact of capital market changes on the corporate governance of these institutions.

With respect to the changes in disclosure, Sir Howard Davies asked if there were any gains from different investors adopting different regimes, especially in relation to private equity. **John Plender** answered this question by saying that it is quite difficult to separate different investors and create a different regime for each one, but that private equity and sovereign wealth funds should be treated as a singular category.

Mats Iaksson (OECD) started his remarks by briefly characterising the new capital market players. He discussed concerns over possible political motivations of sovereign wealth funds, arguing this was a problem not only in Asian economies and other emerging markets, but also in Europe. With respect to private equity deals, he emphasised the relationship between investors and insiders, saying that a friendly take-over process is essential to its success. He also highlighted that, in many insider deals, the interests of other shareholders need to be accounted for, and that this should be reflected in the design of regulation. With respect to hedge funds, he believes that only a small fraction has engaged in significant shareholder activism. He then went on to discuss the implications of these issues for policy makers in Europe. To conclude, he talked about company boards, and the increased exposure and pressure they face from the scrutiny of new capital market players.

Liz Murrall (Investment Management Association) provided a practical example of a company to illustrate the potential conflicts between short term and long term goals of different types of investors.

According to **Ira Millstein** there were great changes in the relationship between the board and stock markets. In the early days, the board did not face pressures from capital markets or shareholders. People inside the board room would talk about corporate investment, dividends and conglomerates. Not until recently did the board start to be concerned about capital markets. Now, concerns are primarily focused on capital markets and potential takeovers. In this context, poison pills are not seen as so bad anymore because they can help to give companies time to breathe and take stock. Also, the companies' goal to increase shareholders' value was very clear in the past, while today shareholder have such different views and interests that this is no longer possible.

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Paul Boyle (Financial Reporting Council) attempted to summarise the consensus so far and emphasised that the main goal should be to improve corporate performance. He also pointed out that this involved constraints and gave some examples such as the treatment of employees, product and consumer safety and the systemic implications of corporate behaviour on other market participants. He defined some constraints to be imposed on the behaviour of companies and shareholders. He concluded by saying that there is a complex set of dynamics that we need to understand, and that the role played by private equity funds and private companies will help define new rules and policies on these matters.

Paul Woolley (FMG/LSE) said that although the remarks made so far were centred on the micro-effects, there were very important macro effects. The overall economic impact of financial institutions and capital markets has exploded in recent years. Forty years ago the financial sector accounted for about 10 per cent of corporate profits; now that figure is more like 35 per cent to 40 per cent. It has been an engine that has grown very fast and might overtake the real economy in the near future. However, at the end of the day it should be the real economy that plays the major role and not intermediary services.

Returning to the topic of the micro level, **Conor Kehoe** described some conclusions from the study of private equity firms: in many cases, these firms out-perform the market. They found a good correlation between deal performance (or value creation) and the level of engagement of the private equity partner (ie, engagement and time spent with the management team prior to the acquisition). They believe that the success of private equity relies on the time, motivation and resources that the private equity partner puts on those deals. When asked about the lessons public companies can learn from private equity, he said that the differences between the two types of companies lie mainly in the attitudes of non-executive directors.

Adding further to Conor Kehoe's comments, **Antonio Borges** said that we need different corporate governance models for different types of companies. He pointed out that private equity firms have a similar model to some companies in continental Europe which have a big block of shareholders that are very engaged with the board. As a result these companies often achieve superior performance. However this is not a universal model and it might not apply to all industries. In industries that grow fast, companies are much better with a diversified ownership structure. Finally he suggested the need for internal mechanisms of corporate governance as a substitute for the external ones.

David Pitt-Watson, while commenting on the differences between the US and Europe, said that those differences largely stemmed from corporate law, especially from regulations affecting the relations between management team and shareholders. For instance, take-over processes in the US and the UK are dissimilar.

Sir Geoffrey Owen asked if there was any evidence that the weaknesses of the US system, relying on powerful boards, had damaged American industrial performance. He raised some doubts on the superiority of the UK system; he said he was not aware of any evidence that companies in the UK perform better than companies in the US because of a better system of corporate governance.

Liz Murrall said that some comparative research was done in order to advise some emerging markets on which corporate governance system to adopt, but she said it was quite difficult to provide evidence for a causal link between the corporate governance model and corporate performance.

David Pitt Watson suggested that a good methodology to test this link should look at systems where the governance has changed or where shareholder interventions took place, although he added that this type of methodology was difficult to implement with respect to the US.

Paul Myners pointed out that, despite the lack of evidence, the UK system is clearly better than the US, because it is designed to increase shareholder value and not corporation value as in the US. To add to this point, **Antonio Borges** highlighted some research by Collin Mayer that provides evidence suggesting companies with significant block holders and stable ownership structures achieve superior performance.

Paul Boyle added to this discussion by arguing that shareholders have different motivations. There are shareholders with short term, trading motivations that are not necessarily consistent with the long term goal of increasing company value. Again he said that constraints should be imposed on such shareholders' behaviour. It is his belief that this type of conflict is more frequent in the US than in the UK.

The last topic to be discussed was the impact of the changes in capital markets on corporate social responsibility (CSR).

Norman Pearlstine pointed out that for the majority of firms this is imposed from the outside and does not emerge from inside the company. He also mentioned that some managers of companies that have become private regard as a benefit the fact that they do not need to do the CSR report anymore. However, it is generally accepted among management scholars that CSR, and the focus on stakeholders as well as shareholders, is good for the firm.

With respect to this topic, **Sir Geoffrey Owen** said it was important to focus on whether the changes in capital markets and companies' outside context make any difference in terms of CSR. **Ira Millstein** believes that CSR should be seen as a way to increase stakeholders' value and feels that the awareness being given to this topic is increasing.

Steven Davies linked this point back to corporate governance issues by asking what represents good corporate governance. Many companies define a social corporate profile and there has been some agreement that companies should care about their communities and stakeholders. However, if there is





Sir Geoffrey Owen (Department of Management, LSE)

concentrated ownership and shareholders do not share the same interests as communities or other stakeholders, what will be the impact on boards? He also said it is widely accepted that, to achieve shareholder value, companies should increase stakeholder value. However, Ira Millstein pointed out that, in some cases, increasing stakeholder value is made at the expense of shareholders value. In the case of private equity firms,

Conor Kehoe said that there is no evidence that shareholders get involved in the dimension of CSR, that instead they leave this to the managers.

Paul Davies and **Ira Millstein** both agreed that it is not clear what the definition of CSR is, and it is also not clear that increasing shareholders' value is made at a cost to other stakeholders.

Davis Pitt-Watson also agreed these are concepts that are difficult to define and that the link between CSR and value is also very difficult to establish. He gave the example of BP who started a study six years ago and gave up upon discovering that there were about 240 million beneficiaries of their dividends! Under these circumstances it is very difficult to separate CSR from shareholder value. On the other hand he pointed out that there are some changes occurring, and that CSR is something that managers should care about.

John Plender remarked that it is short-sighted on the part of managers to switch to private equity simply because they can then switch from corporate social responsibility to corporate social irresponsibility. Part of the reason why there is a political concern about private equity in the UK is because so far private equity is seen as a licence to operate under light supervision. If people start seeing private equity in this new perspective, it will not be seen as a valuable asset any more.

With regard to sovereign wealth funds, **Antonio Borges** said that one should be less concerned about areas where public interest is involved, because usually those cases are heavily regulated. In this case the actions of shareholders are limited by definition.

Before the final remarks, **Sir Howard Davies** summarised the main questions and answers in the session. With respect to the first topic, he shared some worries and concerns about the new changes in capital markets and the impact on companies. He referred to agreement that there are conflicts of interest between different types of shareholders, primarily arising from the different time-horizon of their goals. He suggested that there were lessons to learn from the private equity model and emphasised the role of non-executive directors. With respect to the second topic, he agreed on the need for a disclosure regime for mergers and acquisitions, although it is product market competition, more than shareholder ownership, that drives companies' behaviour and performance. Finally, on the topic of CSR he concluded that this is a difficult issue because of the different objectives involved.

The final remarks were made by **Ira Millstein**. He felt the meeting was very helpful in trying to understand the issues under discussion. He concluded by saying that the US should learn from the UK, specifically regarding shareholder activism. The system in the UK is more subtle, but still very powerful and efficient in promoting communication between shareholders and the management team. He concluded by going back to the macro level and by sharing some concerns regarding the evolution of capital markets, which are becoming increasingly complex and pose some risks for the real economy.



Corporate Governance at LSE

The future of AIM as a stock market for growing companies

12 March 2008

Presentation of AIM report: Sir Geoffrey Owen, Julia Black, Sridhar Arcot

Sir Geoffrey Owen (Department of Management, LSE), **Julia Black** (Department of Law, LSE) and **Sridhar Arcot** (ESSEC Business School) will give a brief presentation of their report on AIM which was commissioned by the London Stock Exchange and published in September 2007.

Before opening up the general discussion, there will be comments from practitioners including **Philip J Secrett** (Grant Thornton UK LLP), **Tom Troubridge** (PricewaterhouseCoopers), **David Pinniger** (Abingworth) and **Theresa Wallis** (Lidco Group plc).

The questions to be discussed will include:

- Can AIM enlarge its international role, attracting companies from the US, Continental Europe and emerging markets, while at the same

time continuing to serve its original constituency – small and medium-sized British companies?

- Given the size of AIM and its varied composition, are the regulatory and enforcement arrangements appropriate?
- What can be done to improve liquidity for the smaller AIM stocks?
- How important is AIM as a source of finance for high-tech firms – can it play the same sort of role in Europe as NASDAQ has done for high-tech entrepreneurial firms in the US?
- How well does AIM serve institutional and retail investors?

A summary of this event will be provided in the July issue of The FMG Quarterly Review.

The Corporate Governance at LSE initiative is led by

Professor Paul Davies, Department of Law, LSE
Professor Antoine Faure-Grimaud, Financial Markets Group, LSE
Dr Thomas Kirchmaier, MBS and Financial Markets Group, LSE
Sir Geoffrey Owen, Department of Management, LSE

Attendance at the Corporate Governance at LSE Research Debates is by invitation only.

Further information is available on the Corporate Governance at LSE website:

www.lse.ac.uk/CorporateGovernance



The Paul Woolley Centre for the Study of Capital Market Dysfunctional

First Annual Conference

12 and 13 June 2008

The First Annual Conference of the Paul Woolley Centre for the Study of Capital Market Dysfunctional will take place on 12 and 13 June 2008.

The Paul Woolley Centre was established at the London School of Economics and Political Science in September 2007. Research at the centre aims at understanding the workings of capital markets and the social efficiency of allocations these markets achieve. The research departs from the Arrow-Debreu view of frictionless markets, and emphasises the role of financial institutions (eg, investment banks, mutual, hedge, and pension funds) in influencing prices and allocations. The main themes are:

- Contracts and organisational structure: What contracts should govern the agency relationship between investors and fund managers? How do contracts influence managers' investment policies? What determines the organisational structure of the fund-management industry?
- Market frictions and asset prices: How do frictions such as asymmetric information, market-entry costs, or agency, impact the informational efficiency of prices? What are the implications for market liquidity and for phenomena such as excess volatility or contagion?

- Allocative efficiency and the macro-economy: Frictions can generate allocative inefficiencies, such as imperfect risksharing and misallocation of capital in the macroeconomy. How important are these inefficiencies and how can they be measured?

- Policy implications: Can regulatory policies mitigate market inefficiencies? For example, can changes in contracts between investors and managers, or the introduction of new assets, generate Pareto-improvements?

The Paul Woolley Centre will be holding a conference each year based on these broad themes as well as related research questions. The goal is to bring together researchers working on such questions, disseminate their research, and stimulate the development of new ideas. Papers will have discussants.

The first conference will take place on 12 and 13 June. It will start in the afternoon of Thursday 12 June, and end in the afternoon of Friday 13 June. Friday's session will be joint with the Adam Smith Asset Pricing (ASAP) Workshop, which is also meeting on Saturday 14 June.

Programme Committee: **Bruno Biais** (University of Toulouse), **Denis Gromb** (London Business School and LSE), **Christopher Polk** (LSE), **Dimitri Vayanos** (LSE), **Paul Woolley** (LSE)

For more information about the Centre please visit The Paul Woolley Centre website at www.lse.ac.uk/PaulWoolleyCentre/

Contact: Tanya Hall, Programme Administrator
The Paul Woolley Centre for the Study of Capital Market Dysfunctional
Telephone: 020 7852 3502
Email: t.hall@lse.ac.uk



Capital Markets Workshop

The Capital Markets Workshop meets regularly throughout the academic year at 5pm on Wednesdays in room R405, Lionel Robbins Building, LSE. Please visit the FMG website for updates and changes in times and locations.

The CMW schedule for the Summer Term is as follows:

Summer Term 2008

| | |
|-----------------|---|
| 30 April | Wei Xiong (Princeton University) |
| 7 May | Darrell Duffie (Stanford GSB) |
| 14 May | Urban Jermann (Wharton School, University of Pennsylvania) |
| 21 May | Efraim Benmelech (Harvard University) |
| 28 May | Bruno Biais (University of Toulouse) |
| 4 June | Lauren Cohen (Harvard Business School) |
| 11 June | Arvind Krishnamurthy (Kellogg School of Management, Northwestern University) |
| 18 June | Ricardo Caballero (Massachusetts Institute of Technology) |
| 2 July | Itay Goldstein (Wharton School, University of Pennsylvania) |

The updated schedule is available on the FMG website at <http://fmg.lse.ac.uk>. If you require further information, please call 020 7955 6301/7891 or email fmg@lse.ac.uk.

The Capital Markets Workshop is funded by:
The Department of Finance, LSE
The Suntory and Toyota International Centres for Economic and Related Disciplines (STICERD), LSE



The London Financial Regulation Seminar

Summer Term 2008

An inter-disciplinary and inter-collegiate group of experts specialising in financial regulation will be holding a regular series of seminars, and more occasional conferences, on topics relating to this field.

Unless otherwise stated, meetings take place on **Mondays in R405, 4th Floor, Lionel Robbins building** at LSE between 5.45pm to 7.15pm.

Enter the Library building through the side door on Portugal Street, and take the elevator to the 4th floor. Drinks will be served afterwards.

Monday 12 May

Gabriel Sterne and **Sujit Kapadia** (Bank of England), on 'A Framework for Quantifying Systemic Stability'.

Monday 19 May

Andrew Sheng (former Chairman of the Hong Kong Securities and Futures Commission), on *title tbc*

Monday 9 June

Thorvald Grung Moe (Central Bank of Norway), on 'Triggers for PCA'

Monday 16 June

Michael Foot (Promotory Financial Services, previously senior official at FSA), on 'Regulatory Lessons from the First Year of the Crisis'

The organisers of this seminar series are:-

Professor E Philip Davis, Professor of Economics and Finance, Brunel University; **Professor Charles Goodhart**, Professor of Banking and Finance, Financial Markets Group, London School of Economics and Political Science; **Dr Thomas Huertas**, Financial Services Authority, **Professor Rosa Maria Lastra**, Professor of International Financial and Monetary Law Centre for Commercial Law Studies, Queen Mary, University of London; **Dr Alistair Milne**, Reader in Banking and Finance, Cass Business School; and **Professor Geoffrey Wood**, Professor of Economics, Faculty of Finance, City University Business School.

For more information please call 020 7955 6301. For details of any changes to the scheduled programme please see the FMG's website at <http://fmg.lse.ac.uk>

Taxation Seminar

Summer Term 2008

For the Summer term, the Taxation Seminars will, as customary, take place monthly on **Monday evenings** from **6.30pm until 8pm**. The seminars will be held in **Conference Room R505** on the **fifth floor** of the **Lionel Robbins Building** (the LSE Library building on Portugal Street, WC2).

Wine, soft drinks, and sandwiches will be available from 6pm and during the seminar. As another seminar will be held immediately beforehand on several occasions, drinks and sandwiches will sometimes be available outside the conference room.

Monday 28 April

Budget and Finance Bill: Panel discussion

Ian Roxan (Department of Law, LSE)

Jonathan Leape (Department of Economics, LSE)

Malcolm Gammie CBE QC (One Essex Court)

Monday 19 May

To be confirmed

The LSE Financial Markets Group gratefully acknowledges financial support from STICERD and the LSE Department of Law for these seminars. For updated information on the seminars, please check <http://fmg.lse.ac.uk/events/> We look forward to seeing you. Please feel free to bring interested colleagues.

Jonathan Leape, Ian Roxan, Judith Freedman, Malcolm Gammie and David Oliver

Discussion papers

DP 591

Evaluating hedge fund performance: a stochastic dominance approach

Sheng Li, Oliver Linton

We introduce a general and flexible framework for hedge fund performance evaluation and asset allocation: stochastic dominance (SD) theory. Our approach utilizes statistical tests for stochastic dominance to compare the returns of hedge funds. We form hedge fund portfolios by using SD criteria and examine the out-of-sample performance of these hedge fund portfolios. Compared to performance of portfolios of randomly selected hedge funds and mean-variance efficient hedge funds, our results show that fund selection method based on SD criteria greatly improves the performance of hedge fund portfolios.

DP 592

Competition and Opportunistic Advice of Financial Analysts: Theory and Evidence

Enrico Sette

This work investigates both theoretically and empirically how the behaviour of financial analysts is affected by competition, measured as the strength of coverage of a stock from other analysts. The interaction among analysts and investors is modelled as a dynamic cheap talk game. The theoretical model shows that analysts having a conflict of interest with investors report

information truthfully with higher probability if other, 'neutral', analysts report information on the same stock. This empirical prediction is tested on data about recommendations on IPOs. The main result is that analysts working for the lead underwriter of the IPO ('insiders') are more optimistic when there are no other analysts (not working for the lead underwriter, 'outsiders') covering the stock. The data also show that insiders do not seem to use the information contained in outsiders' recommendations. Finally, outsiders are not influenced by recommendations previously issued by insiders. These results also allow one to discriminate between competing hypotheses brought forward to explain insiders' overoptimism. The empirical evidence suggests that insider analysts' overoptimism is induced by incentives rather than by a 'psychological bias'.

DP 593 (UBS Paper 044)

How Deep is the Annuity Market Participation Puzzle?

Joachim Inkmann, Paula Lopes, Alexander Michaelides

Using UK microeconomic data, we analyze the empirical determinants of voluntary annuity market demand. We find that annuity market participation increases with financial wealth, life expectancy and education and decreases with other pension income and a possible bequest motive for surviving spouses. We then show that these empirically-motivated determinants of annuity market participation have the same, quantitatively important, effects in a life-cycle model of annuity demand, saving and portfolio choice. Moreover, reasonable preference

parameters predict annuity demand levels comparable to the data, thereby questioning the conventional wisdom that limited annuity market participation is a puzzle to be explained.

DP 594

Financing Constraints and a Firm's Decision and Ability to Innovate: Establishing Direct and Reverse Effects

Vassilis Hajivassiliou, Frédérique Savignac

The paper analyzes the existence and impact of financing constraints as a possibly serious obstacle to innovation by firms. Direct measures of financing constraints are employed using survey data collected by the Banque de France and the European Commission, which overcomes the problems with the traditional approach of trying to deduce the existence and impact of financing constraints through the significance of firm wealth variables. The econometric framework employed for this study is the simultaneous bivariate probit with mutual endogeneity. The paper discusses the important identification issue of coherency conditions in such LDV models with endogeneity and flexible temporal and contemporaneous correlations in the unobservable error terms. Conditions for coherency as discussed in the existing literature are reviewed and shown to be rather esoteric. Two novel methods for establishing coherency conditions are presented, which have intuitive interpretations. Finally, the paper presents alternative approaches for achieving coherency in models hitherto classified as incoherent through



the use of prior sign restrictions on model parameters. This allows us to obtain estimates of the interaction between financing constraints and a firm's decision and ability to innovate without forcing the econometric models to be recursive. Thus, direct as well as reverse interaction effects are obtained for the first time.

DP 595

Strategic Financial Innovation in Segmented Markets

Rohit Rahi, Jean-Pierre Zigrand

We study a model with restricted investor participation in which strategic arbitrageurs reap profits by exploiting mispricings across different market segments. We endogenize the asset structure as the outcome of a security design game played by the arbitrageurs. The equilibrium asset structure depends realistically upon considerations such as depth and gains from trade. It is neither complete nor socially optimal in general; the degree of inefficiency depends upon the heterogeneity of investors.

DP 596

Value of Information in Competitive Economies with Incomplete Markets

Piero Gottardi, Rohit Rahi

A substantial literature addresses the negative effect on welfare of the release of information in a competitive market economy. We show that the value of information in this setting is typically positive if asset markets are sufficiently incomplete. More specifically, for any competitive equilibrium of a generic economy, we can find a finer information structure such that an allocation that is resource feasible and measurable with respect to this information ex-post Pareto dominates the given equilibrium allocation.

Special papers

SP 173

Analysis of Financial Stability

Charles Goodhart, Dimitrios Tsomocos

No abstract available

Forthcoming Discussion and Special Papers

Discussion Papers

DP 597

'Parametric properties of semi-nonparametric distributions, with applications to option valuation'

Angel Leon, Javier Mencia, Enrique Sentana

DP 598

'Executive Compensation and Competition in the Banking and Financial Sectors'

Vicente Cuñat, Maria Guadalupe

DP 599

'Efficient Estimation of a Semiparametric Characteristic-Based Factor Model of Security Returns'

Gregory Connor, Matthias Hagmann, Oliver Linton

DP 600

'Efficient Dynamic Coordination with Individual Learning'

Amil Dasgupta, Jakub Steiner, Colin Stewart

DP 601

'Inflation Dynamics in the US – A Nonlinear Perspective'

Bob Nobay, Ivan Paya, David A Peel

DP 602

'Inequality, Stock Market Participation, and the Equity Premium'

Jack Favilukis

Special Papers

SP 174

'Does high money growth put the inflation target at further risk?'

Tim Congdon

Visitors to the FMG

January – March 2008

Federico Bandi (Chicago GSB)

Richard Baron (Institute of Directors)

Itzhak (Zahi) Ben-David (Chicago GSB)

Annabel Bismuth (OECD)

Antonio Borges (Goldman Sachs International)

Tracey Bowler (Tax Law Review Committee)

Paul Boyle (Financial Reporting Council)

Sir Adrian Cadbury

Anusha Chari (University of Michigan)

David Clayton (PricewaterhouseCoopers)

Stephen Davis (Millstein Centre, Yale School of Management)

Masako Ueda (University of Wisconsin-Madison)

Simon Gervais (Duke University)

Sir Christopher Hogg (Financial Reporting Council)

Thomas Huertas (Financial Services Authority)

Mats Isaksson (OECD)

Conor Kehoe (McKinsey & Company)

Ralph Koijen (NYU Stern School of Business)

Leonard Kostovetsky (Princeton University)

Samuli Knapfer (Helsinki School of Economics)

Mike Krimminger (Federal Deposit Insurance Corporation)

Lars-Alexander Kuehn (University of British Columbia)

Xiaoji Lin (University of Minnesota)

John Manning (PricewaterhouseCoopers)

Ian Martin (Harvard University)

Rosemary Martin (Reuters)

Ira Millstein (Millstein Center, Yale School of Management)

Philippe Mueller (Columbia Business School, New York)

Liz Murrall (Investment Management Association)

Paul Myners

Stefan Nagel (Stanford University)

Filippos Papakonstantinou (Princeton University)

Norman Pearlstine (The Carlyle Group)

Francisco Peñaranda (Universitat Pompeu Fabra)

David Pitt-Watson (Hermes Equity Ownership Services)

John Plender (Financial Times Group)

Jose Gonzalo Rangel (NYU Stern School of Business)

Francesco Sangiorgi (Collegio Carlo Alberto)

Marianne Schulze-Ghattas (IMF)

Mark Seasholes (INSEAD)

Joanne Segars (National Association of Pension Funds)

Anne Simpson (International Corporate Governance Network)

Gary Smith (The American Academy in Berlin)

James Thompson (Queen's University Canada)

Masako Ueda (University of Wisconsin-Madison)

Mungo Wilson (Hong Kong University)

Konstantinos Zachariadis (Northwestern University)





Regional Comparative Advantage and Knowledge-Based Entrepreneurship

RICAfE2 Third Conference

Call for Papers

9 and 10 October 2008

University of Amsterdam Business School, Finance Group

The RICAfE2 Third Conference will be held on 9 and 10 October 2008 at the University of Amsterdam Business School. The organisers invite submissions for empirical and theoretical papers on the financing of knowledge-based entrepreneurial firms, on the influence of venture capital on firms' ability to translate technological advances into successful products, and on the contribution of knowledge-based entrepreneurship to regional dynamics. The topics we are planning to discuss include, but are not limited to:

- The choice between alternative sources of financing for innovative firms and their impact on strategic decisions in entrepreneurial firms;
- The determinants of knowledge-based entrepreneurship;
- Venture capital and its contribution to the knowledge-based economy and regional development;
- Economics of intellectual property rights and its implications for knowledge-based entrepreneurship;
- The role and design of financial contracts and of the choice of organisational form in fostering knowledge-based entrepreneurship;
- Effects of regulation on venture capital investment and entrepreneurial dynamics;
- The impact of corporate governance mechanisms on the performance of entrepreneurial firms.

The conference proceedings will not be published, as we aim to attract papers on their way to publication in high quality journals.

Expenses: Travel (economy class round-trip) and accommodation expenses will be covered for presenters and discussants.

Program Committee: **Stefan Arping** (University of Amsterdam), **Amar Bhidé** (Columbia University), **Bruno Biais** (University of Toulouse), **Patrick Bolton** (Columbia University), **Mariassunta Gianetti** (Stockholm University), **Thomas Hellmann** (University of British Columbia), **Gustavo Manso** (MIT), **William Megginson** (University of Oklahoma), **Eric Nowak** (University of Lugano), **Armin Schwienbacher** (University of Amsterdam; Catholic University of Louvain; Committee Chair), **Alessandro Sembenelli** (University of Torino) and **Christoph Zott** (INSEAD).

Deadline for submission of papers: 27 June 2008

Submissions are accepted online only via the RICAfE2 website:
www.lse.ac.uk/ricaf2

The authors of selected papers will be informed by the end of July.
For more information please contact Armin Schwienbacher,
a.schwienbacher@uva.nl

The Regional Comparative Advantage and Knowledge-Based Entrepreneurship (RICAfE2) Research network includes the London School of Economics (FMG), the Department of Economics and Finance of Turin University, the Center for Financial Studies (Frankfurt), HEC School of Management (Paris), University of Amsterdam, University of Tilburg, Baltic International Centre for Economic Policy Studies, University of Lugano, Indian School of Business, Technion (Israel), and the Belgrade Laboratory for Quantitative Finance. RICAfE2 is funded by the European Commission, DG-Research, under the 'Citizens and governance in a knowledge-based society' (FP6) programme, grant CIT5-CT-2006-028942.



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Financial Markets Group

The Financial Markets Group Research Centre at LSE is one of the leading centres in Europe for academic research into financial markets. [more about FMG](#)

Events this week @ FMG

Thursday, 6th March 2008 - 13.00-15.00
PhD Seminar | CANCELLED | Vincent Fardeau
location: R407, Financial Markets Group

Thursday, 6th March 2008 - 5pm
EXTRA Capital markets Workshop | Understanding Portfolio Efficiency with Conditioning Information | Francisco Penaranda (Universitat Pompeu Fabra)

In the news

[In the Press 2: The Structure of Regulation: Lessons from the Crisis of 2007 conference](#) 5 Mar 2008

Latest Stories:

[The Structure of Regulation: Lessons from the Crisis of 2007 conference - watch online soon](#) 4 Mar 2008

[The Structure of Regulation: Lessons from the Crisis of 2007 conference - watch online soon.Th](#)

New research on: Home Ownership, Housing Collateral and Aggregate Fluctuations. - The Financial Markets Group has been awarded a research grant

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FMG Review

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Designed by: LSE Design Unit
www.lse.ac.uk/designunit