Discussion of Li-Maug-Schwartz-Ziv: When shareholders disagree: trading after shareholder meetings

Moqi Groen-Xu, LSE

Oslo, May 2019

An empirical paper on disagreement

- Disagreement where it is most relevant: around shareholder meetings
- Trading volume and volatility patterns consistent with disagreement
  - High trading volume around the meeting
  - Volume high even if prices do not change
- Introduces microstructure measures of disagreement
  - Kandel-Pearson (1995)/Bollerslev et al. (2018): low volume-volatility-elasticity
  - Banerjee-Kremer (2010): Autocorrelation after periods of high volume/volatility
- Shareholders exit if they find out about their disagreement
  - Funds sell after the majority voted against them (regardless of management position)

Literature

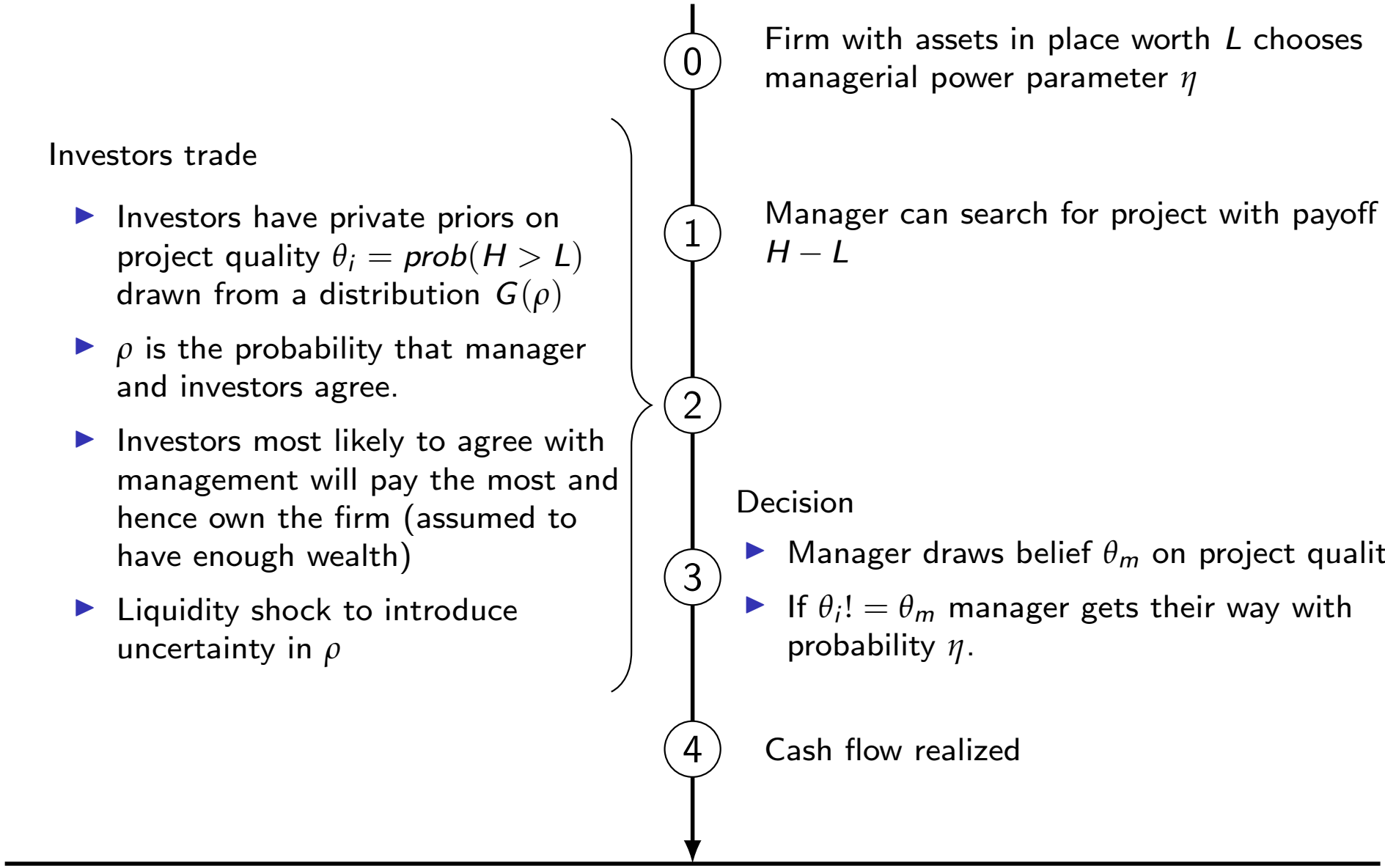
Disagreement speaks to the big questions in the Asset Pricing literature

- Are markets efficient? Why do bubbles and crashes occur?
- Intuitively correct and nests most behavioral assumptions

What about the big questions of Corporate Finance literature?

- What happens if managers and shareholder interests diverge?
  - More likely if shareholders disagree with each other (over and above agency or moral hazard problems)
  - Do agreeing shareholders sort themselves to align with managers?
- How can we align their incentives? How much autonomy vs monitoring?
  - Literature on control rights (Boot et al 2006, 2008; Van der Steen 2008, 2010, Dicks and Fulghieri 2015, Kakhbod et al. 2019), capital structure (Dittmar and Thakor 2007, Boot and Thakor 2011) and investment (Thakor and Whited 2011)
  - How important is shareholder voting?

Disagreement in Boot et al (2008)



$\rightarrow$ Investors with the highest priors self-select to hold shares

$\rightarrow$ Optimal managerial autonomy higher with more disagreement

Governance version of Boot et al (2008)

Project: change firm value from L to H

- Managers only want to implement if their prior for H, θ_m, is high
- Activists can force the management if managerial power η is low

Pre-voting trading

- Investors have private priors: $\theta_i^{\text{activists}} > 0.5$, $\theta_i^{\text{pacifists}} < 0.5$ (Disagreement)
- Distribution $G(p)$ unknown because of liquidity trading

Voting: allocates control rights to shareholders or managers $\eta \in 0, 1$

- Investors vote their priors
- Voting result depends on $G(p)$

Post-voting trading

- Voting outcome $\eta = 0 \rightarrow$ activists value the firm more and buy, pacifists sell
- Voting outcome $\eta = 1 \rightarrow$ activists value the firm less and sell, pacifists buy

aka exit of activists and the pack

Decision: managers get their way with probability η.

Position in the recent Governance literature

Monitoring management: blockholders (Maug 1998 etc.), exit vs. voice, activism etc.

Pre-voting trading

- Investor disagreement: Bolton et al., Dicks and Fulghieri
- Liquidity and activism: Back et al 2018

Post-voting trading: this paper

- High trading volume around meeting: investors buy in to vote / those disagreeing with voting result sell
- Volume high even without prices changes: investors disagree
- Low volume-volatility-elasticity and high autocorrelation after periods of high volume/volatility: sorting according to disagreement
- Funds sell after the majority voted against them (regardless of management position)

Voting coordination: Brav, Dasgupta and Mathews, Brav, Jiang, and Li, Kedia, Starks and Wang (2017), Cornelli and Li (2002)

Decision: managers get their way with probability η.

Link to the Corporate Governance literature

- How important is shareholder voting?
  - Role as sorting mechanism
  - Effectiveness of preference aggregation
  - Effectiveness as monitoring device
- How does liquidity affect the effectiveness of shareholder voting?
  - Buying shares to vote, value of votes, implications for post-voting price
  - Role of voice vs exit around the shareholder meeting
- What do shareholders want?
  - Which proposals do investors disagree on and what is the value implication?
  - How much does taste matter vs. information?
  - Can disclosure improve interpretation and reduce disagreement?

Empirical wish list:

- Link post-voting results to pre-voting shareholder base (positions) and voting itself
- Heterogeneity of results by type of proposals, closeness of results
- Herding, clusters, meeting-specific risk

Alternative explanations

- Different priors, different speculative positions (Karpoff 1986)
  - Document trading and positions prior to meeting?
- Private information production concentrated around shareholder meetings
  - Link trading to information content of meetings and general information asymmetry
  - Link trading to surprise of voting results
- Life-cycle related trades and temporary risk changes around shareholder meetings
  - Link trading to fund flows
- Rebalancing cascades (Chinco and Fos)
- Bayesian Learning
  - Information aggregation voting models a la Maug and Rydqvist (2009)
  - Learning about disagreement levels (Boot et al 2008)
  - Disagreement amplifies the price effects of learning (Atmaz and Basak 2018)

Thank you for giving me this paper to discuss

- Introduces investor disagreement to shareholder voting
- Corporate governance context offers more specific interpretation worth pursuing