Report Type

 Mid Term Award Report

Full Name

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Faculty/Department

 Cambridge Endowment for Research in Finance

Project Title

 Research in Corporate Governance and Innovation

Project Start Date

 Jul 02, 2018

Project End Date

 Jul 02, 2020

Project Abstract

I study the corporate value implications of corporate governance mechanisms and product market competition. With the first paper “Shadow Pills and Long-Term Firm Value” I investigate whether the right to adopt a poison pill (where the *right* constitutes the shadow pill) is value relevant for shareholders. In the second paper “Product Market Competition and Long-Term Firm Value: Evidence from Reverse Engineering Protections” I examine the effect of decreased competition (brought about by a change in intellectual property protection) on the value of a corporation. The third paper “Directors’ Duties Laws and Long-Term Firm Value” explores the value impact of expanded director authority to consider the interests of all stakeholders of the firm.

Activities and Achievement

1. Shadow Pills and Long-Term Firm Value

This paper has been presented at academic conferences and seminars and will be submitted to the Journal of Financial Economics within the next two weeks.

This paper finds that the right to adopt a poison pill (i.e., “shadow pill”) is value increasing for shareholders. Moreover, the positive value effect is differentially higher for firms more engaged in innovative projects or with important stakeholder relationships. This finding is consistent with the bonding hypothesis of takeover defenses. These results provide the first empirical support that while the endogenous decision to adopt a poison pill is negatively correlated with value, exogenous increases in the right to adopt a poison pill (strength of the shadow pill) is beneficial to shareholders.

1. Product Market Competition and Long-Term Firm Value: Evidence from Reverse Engineering Protections

This paper has been presented at academic conferences and seminars and will be submitted to the Review of Financial Studies within the next four weeks.

This paper documents that a decrease in the intensity of competition in product markets is value enhancing for shareholders. This is especially so for firms with greater innovative ability. These findings provide the first causal evidence that (1) decreased competition leads to higher corporate value (not just an association), and (2) that the value increases are not simply attributable to standalone economics rents (from market power), but rather it is the use of rents for investments in new and existing production technologies that creates value.

1. Directors Duties Laws and Long-Term Firm Value

This paper has been presented at academic conferences and seminars and will be submitted to the Quarterly Journal of Economics within the next four weeks.

This paper shows that the enhancement of director discretion to consider the interests of all stakeholders leads to increases in corporate valuation. In addition, it is found that the increases in value are more pronounced for larger and more complex firms, firms more exposed to endogenous uncertainty and with important stakeholder relationships. These results are consistent with the bonding hypothesis of takeovers and the stakeholder orientation hypothesis. These empirical findings are important for (1) policy makers as it suggests that the shareholder-centric view of the firm might be less than optimal in certain environments and (2) opens important avenues for future research.

Dissemination

1. Shadow Pills and Long-Term Firm Value

This paper will be submitted to the Journal of Financial Economics within the next two weeks.

Conference presentations: Southwest Finance Symposium (April 2018), American Law and Economics Annual Meeting (May 2018), SFS Cavalcade North America (May 2018), 26th Finance Forum (July 2018), FMA (October 2018, scheduled).

Seminar presentations: Toulouse School of Economics (December 2017), New York University (January 2018), University of Oklahoma (February 2018).

1. Product Market Competition and Long-Term Firm Value: Evidence from Reverse Engineering Protections

Conference presentations: 2nd TILEC (University of Tilburg) conference on Competition, Standardization and Innovation, Southwestern Finance Association Annual Meeting (March 2018), 6th Annual Research Roundtable (Northwestern University) on Standard Setting Organizations and Patents (May 2018), 26th Finance Forum (July 2018), FMA (October 2018, scheduled).

Seminar presentations: University of Oklahoma (January 2018).

1. Directors Duties Laws and Long-Term Firm Value

Conference presentations: American Finance Association Annual Meeting (January 2019, scheduled).

Seminar presentations: University of Pennsylvania (February 2018).

Outputs

1. Shadow Pills and Long-Term Firm Value

Abstract: This paper analyzes the value impact of the right to adopt a poison pill – or “shadow pill” – on long-term firm value, exploiting the quasi-natural experiment provided by the staggered adoption of poison pill laws that validated the use of the pill in 35 U.S. states over the period 1986 to 2009. We document that the availability of a shadow pill results in an economically and statistically significant increase in firm value, especially for firms more engaged in innovation or with stronger stakeholder relationships. Our findings are robust to matching and portfolio analysis, and support the bonding hypothesis of takeover defenses.

Web link: <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3074658>

1. Product Market Competition and Long-Term Firm Value: Evidence from Reverse Engineering Protections

Abstract: I analyze the value impact of product market competition (PMC) on long-term firm value. Using exogenous state adoption of anti-plug-mold statutes, and their subsequent invalidation, I causally show that decreased PMC generates economically and statistically significant long-term firm value, especially for firms with greater innovative ability. My findings are robust to different specifications, including matching and portfolio analysis, and provide support for the view that a reduction in PMC leads to higher firm value by increasing investments in new and existing production technologies.

Web link: <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3074622>

1. Directors Duties Laws and Long-Term Firm Value

Abstract: This paper analyzes the long-term value impact of enhanced director discretion to consider the interests of all stakeholders by exploiting the quasi-natural experiment provided by the staggered adoption of directors’ duties laws (also known as corporate constituency statutes) in 35 U.S. states over the period 1984 to 2006. We document that the enactment of these laws results in an economically and statistically significant increase in firm value. The increase in firm value is stronger for larger and more complex firms, firms more exposed to endogenous uncertainty and with stronger stakeholder relationships. Our results support the bonding hypothesis that enhanced director discretion to protect stakeholder interests promotes long-term firm value by reducing a firm’s contracting costs. They also support the view that enhanced director discretion help internalize the externalities that firms create in incomplete markets, leading to more efficient production to the benefit of all stakeholders, including shareholders.

Web link: coming soon (within the next four weeks).

Major Difficulties and Any Other Issues

 None.

Web Links

1. Shadow Pills and Long-Term Firm Value

Web link: <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3074658> Pro

1. Product Market Competition and Long-Term Firm Value: Evidence from Reverse Engineering Protections

Web link: <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3074622>

1. Directors’ Duties Laws and Long-Term Firm Value

Web link: Coming soon (within the next four weeks).

Additional Information

Declaration

This award has not yet produced any relevant outputs, but details of any future publications will be submitted to the CERF database as soon as they become available.

1. Shadow Pills and Long-Term Firm Value

This is joint work with Martijn Cremers, Lubomir Litov and Simone Sepe.

1. Product Market Competition and Long-Term Firm Value: Evidence from Reverse Engineering Protections

This is a sole-authored project.

1. Directors’ Duties Laws and Long-Term Firm Value

This is joint work with Martijn Cremers and Simone Sepe.

Signature - Main Award Holder

Scott Guernsey