COLLOQUIUM

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Information Asymmetry and Leverage Adjustments: A Semiparametric Varying Coefficient Approach

Abstract

Information asymmetry reflects the risk and uncertainty faced by investors and is a measure of a firm's transparency. High information asymmetry could increase the cost of external financing, which in turn impede a firm's leverage (debt-asset ratio) adjustment. This paper studies the adjustment speed toward the target leverage in the presence of information asymmetry using micro-level data from China. In contrast to the previous studies, we allow heterogeneity in the adjustment speed coefficient by modeling it as a nonparametric function of information asymmetry and other firm characteristics. This refinement not only allows for more flexibility in the model, but it also facilitates further exploration into the differences and determinants of firms' financing behavior. We uniquely build the firm-level measure of information asymmetry into the traditional partial leverage adjustment framework. Based on our firm-level measure of the adjustment speed, our paper explores why the leverage adjustment speed matters by examining its association with the corporate performance indicators. We find that China's firms do have leverage targets and they slowly adjust toward these targets. We also find that the adjustment speed decreases with an increase in information asymmetry. Overall, firms which converge toward their targets faster perform better in value, profitability, investment and costs.

Tuesday, Oct 15, 2019
12:00 – 12:50 P.M.
372 Mathematics and Science Center (MSC)

(Refreshments at 11:30-12:00 PM in the kitchen area adjacent to 368 MSC)