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# **Bridging the Information Gap between Borrowers and Microfinance Lenders**

**Elizabeth W. Cooper and Nina E. Ross**

*We use a fixed effect two-stage least squares regression approach on a time series of 82 microfinance institutions (MFIs) in Africa during the period 1997-2008 to understand what drives MFI performance. MFIs with higher debt-to-equity ratios and strong profit margins tend to have stronger financial performance than institutions with low debt-to-equity and weak profit margins. Further, MFI size and expense ratio are inversely related to financial performance. Finally, we find that the older the MFI, the better the financial performance. Our study contributes to the microfinance literature by using a unique sample of non-bank financial institutions across a decade-long time series covering the entirety of the African continent. The results support the asymmetric information theory of microfinance institutions. Overall, our results indicate that it is the financial characteristics rather than MFI structure that determine performance. This may be useful for MFI investors and practitioners.*

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# **The Effect of Option Listing on Return Momentum and Reversal**

**Joel N. Morse, Hoang H. Nguyen, and Chih-Hsien (Jerry) Yu**

*Momentum studies examine short-term return continuations and long-term return reversals in various capital market environments. In this paper, we examine the informational impact of option listing on momentum strategies. We find that within a 12-month period, the profitability of momentum strategies is higher for stocks with options than those without options. Moreover, during a three-year window, stocks without listed options exhibit significant reversals in momentum return, while those that have options show no reliable evidence of reversal. When we examine the effect of risk, we document that the reversal pattern appears strongest for a subsample of stocks characterized by both small capitalization and high volatility. Our findings support the information-based proposition that option availability improves market efficiency and hence reduces investors' overreaction during the short-term momentum cycle. As a result, long-run return reversal declines. Our paper also provides new evidence supporting behavioral models related to the momentum phenomenon.*

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# **Weighing the Evidence of Dividend Initiations**

**Guohua Ma, Tianyu Zhu and Xu-Shen Zhou**

*This paper analyzes post-event stock performance based on the strength and the weight of evidence of dividend initiations. The strength refers to how extreme the evidence is; the weight refers to how credible the evidence is. Griffin and Tversky's (1992) experiments show that people are underconfident when presented with low strength and high weight information and overconfident with high strength and low weight information. This study shows that Griffin and Tversky's results extend to dividend initiation as well. Portfolios with high strength and low weight overreact to dividend announcement, while portfolios with low strength and high weight underreact. The empirical results in this paper show that the strength-weight model can explain the underreaction-overreaction puzzle and suggests that psychological biases may impact stock performance.*

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# **Impact of U.S. Twin Deficits on Bilateral Exchange Rates: Canada and China**

**David Y. Chen**

*This paper examines the U.S. twin deficits debate from a bilateral exchange rate with Canada and China and their respective international reserves angle. This one-lag dynamic linear model is based on the Euler equation expressed in a rational expectations component for aggregate consumption. Findings indicate that the variations in budget deficit had much less impact on the volatility in bilateral U.S.-China exchange rates than those for U.S.-Canada. The U.S. budget deficit variations tend to affect the variations in China's international reserves but not in Canada's. One reason is the near-fixed peg regime in the bilateral U.S.-China exchange rate during the study period of 1990 through 2008.*

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# **Bank Failures 2008: An Examination of the Impact on Stockholder Risk and Wealth**

**Omar A. Esqueda and Dave O. Jackson**

*This article investigates how recent failures of seven publicly-traded commercial banks and the banking crises of 2008 affect the wealth, the systematic and nonsystematic risk, and total risk of commercial banks. We find that the total risk of medium-sized banks is slightly more affected by the turbulence in the financial sector than larger banks. The changes in wealth are positive overall and marginally significant. Taken as a whole, the results indicate that at the end of 2008, the major consequences of the bank failure events are reflected in the level of risk and in modest changes in wealth. There is some indication that investors differentiate which bank type has more exposure, which consequently increases the risk of banks with similar characteristics as the failed banks. The best hedging strategy should therefore consider the inclusion of medium-size federally chartered banks, large banks, and money centers with a state charter only. Our results imply that regulators should more closely monitor bank holding companies based on size and charter type particularly during financial turbulence.*

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# **Bilateral Investment Treaties and Foreign Direct Investment**

**Byung S. Min, Sudesh Mujumdar and Jong C. Rhim**

*This paper investigates the relationship between bilateral investment treaties (BITs) and foreign direct investment (FDI) inflows using random coefficient panel models, and accounting for the regime shift that occurred with the 1997 Asian Financial Crisis. The estimation results reveal that BITs have a strong positive impact on FDI inflows for the pre-1997 era. However, the strength of this positive impact diminishes as more BITs are concluded, implying that each additional BIT yields a relatively smaller FDI-payoff. No statistically significant impact of BITs on FDI inflows is found for the period following the Asian Financial Crisis, implying a decline in their relative importance in attracting FDI. Further, BITs do not have a stronger impact on FDI inflows for developing countries in comparison to developed countries.*

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# **Real Interest Rate Linkages and Capital Market Integration: Evidence from the Americas**

**Bharat Bhalla, Nikiforos T. Laopodis and Anand G. Shetty**

*In this paper, we study the long-run co-movement among the real interest rates of the U.S., Canada, and a select group of Latin American countries to assess the extent of financial market integration among these countries during a period of high capital mobility. The findings of the study support a long-run relationship between the short-term U.S. real interest rate and those of Canada and the Latin American countries except Mexico.*

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