A new study by Boris Vallée and Christophe Pérignon offers evidence that local politicians in France (and probably elsewhere) used high-risk loans for political gain in the years leading up to the recent financial crisis. The strategy worked: Toxic loans helped mayors get reelected.  
   
 Open for comment; 3 Comments posted.

One consequence of the 2008 financial crisis was the virtual disappearance of traditional mergers and acquisitions activity. The years following the onset of the financial crisis have demonstrated, however, that M&A deal making is alive and well—in Chapter 11. In this study of a large sample of Chapter 11 cases, the authors examine how and why M&A has become a significant part of the process, arguing that the rise of M&A has blurred the usual distinctions between reorganization and liquidation.  
   
 Closed for comment; 0 Comments.

Mobile money—the use of electronic money transfer through cellular networks—is rapidly expanding in developing countries, especially among the "unbanked." One persistent problem for mobile money agents, however, has been managing inventory and service quality. Using data from Kenya and Uganda, two East African countries at different stages of mobile money market development, the authors introduce an operations management lens for mobile money and explore the effects of competition and service quality on demand.  
   
 Closed for comment; 0 Comments.

At the heart of the recent financial crisis were nontraditional securitizations, especially collateralized debt obligations and private-label mortgage-backed securities backed by nonprime loans. Demand for these securities helped feed the housing boom during the early and mid-2000s, while rapid declines in their prices during 2007 and 2008 generated large losses for financial intermediaries, ultimately imperiling their soundness and triggering a full-blown crisis. Little is known, however, about the underlying forces that drove investor demand for these securitizations. Using micro-data on insurers' and mutual funds' holdings of both traditional and nontraditional securitizations, this paper begins to shed light on the economic forces that drove the demand for securitizations before and during the crisis. Among the findings, variation across securitization types and investors is key to understanding the crisis. Beliefs appear to have been an important driver of mutual fund holdings of nontraditional securitizations. Results also underscore the importance of optimal liquidity management in the context of fire sales. Key concepts include: Inexperienced mutual fund managers invested significantly more in these products than experienced managers. Beliefs-shaped by past firsthand experiences-played an important role. Managers who had suffered through the market dislocations of 1998 invested substantially less in nontraditional securitizations than those who had not. For insurance companies, incentives appear to have played an important role, though the nature of the relevant incentive conflict seems to have varied across small and larger insurance firms.  
   
 Closed for comment; 0 Comments.

Professor Sandra Sucher wants to change the way business thinks about workforce reductions. "We want people to learn about the forces they unleash in the firm when they institute layoffs."  
   
 Open for comment; 18 Comments posted.

There is a widespread assumption that corporate political spending is highly profitable, earning well more than what would be expected in a competitive market. However, in the popular press and even in previous scholarship most of the returns cited as evidence for this phenomenon are based on descriptive research rather than empirical studies. What are the real economic returns of corporate political spending? Here the authors apply a more rigorous approach for a clearly delimited time period by examining the returns to corporate political spending on what became the American Jobs Creation Act ("the AJCA") of 2004. Findings differ sharply from those generated in prior studies. Specifically, for the median politically active firm in the sample 1) an increase in $1 million in lobbying expenditures is associated with about $32.35 million in taxes saved; 2) an increase in $100,000 of PAC contributions is associated with about $15.64 million in taxes saved; and 3) the additional filing of ten tax-related lobbying reports is associated with about $21.08 million in taxes saved. These results are particularly relevant in light of continued corporate attempts to generate support in the Congress for another "one-time" tax break on repatriated foreign income in line with the AJCA of 2004. Overall, the study suggests that the very high returns to political investment heralded in the press - obtained through descriptive methods - are, in fact, nearly an order of magnitude smaller when more rigorously estimated via instrumentation. Key concepts include: Prior research has shown that firms generally use three different methods of political spending in complement with one another. It is thus more meaningful to consider three return estimates jointly. In this current paper, for the median firm in the sample an increase of $1 million in lobbying contributions (over the firm's prior cycle contributions) is associated with $32.35 million in taxes saved on repatriated foreign income. An increase of $100,000 in PAC (political action committee) contributions is associated with about $15.64 million in taxes saved. The additional filing of ten tax-related lobbying reports is associated with about $21.08 million in taxes saved.  
   
 Closed for comment; 0 Comments.

Georges Doriot, the Harvard Business School educator who played a pioneering role in the emergence of the postwar entrepreneurial economy, is the subject of a new exhibit and website at Harvard Business School.  
   
 Open for comment; 1 Comment posted.

A new study by Bhavya Mohan, Ryan Buell, and Leslie John has an important conclusion for retailers: Explaining what it costs to produce a product can potentially increase its sales.  
   
 Open for comment; 13 Comments posted.

This article surveys research at the intersection of international economics and corporate finance. Recent research illustrates how international trade and multinational activity are affected by the credit constraints firms face and by firms' ability to make use of internal capital markets. Differences in access to financial capital explain variation in trade participation at the country, industry, and firm level. Firms need to fund fixed and variable costs of cross-border transactions, and these transactions often tie up capital for longer periods of time than domestic transactions and involve distinct risks. Credit constraints also play a role in determining which firms choose to conduct operations in multiple countries and what kinds of activities they perform in different jurisdictions. Through their internal capital markets, multinational firms can raise funding in one location and deploy it elsewhere. Internally available financial capital gives multinationals an advantage over purely domestic firms in some circumstances. Financial considerations often shape the extent to which multinationals generate spillovers for local firms. Key concepts include: The ability to access financial capital to pay fixed and variable costs affects choices firms make regarding export entry and operations, and, as a consequence, influence aggregate trade patterns. Multinationals may use internal capital markets to pay for fixed costs, address managerial moral hazard, and exploit differences in access to capital across countries. As a result, financial frictions shape multinational decisions regarding production location, integration, and corporate governance.  
   
 Closed for comment; 0 Comments.

There is growing consensus that well-functioning financial markets play a central role in driving economic growth through their ability to spur technological innovation. In this paper for the Annual Review of Financial Economics, the authors ask how financial markets might actively shape the nature of R&D that is undertaken. They also examine how this may impact technological innovation and growth through the shaping of the ideas that are developed across firms. Drawing on a new but growing literature on the role that capital markets and financial intermediaries play in impacting firm-level innovation, the authors first elaborate on theoretical contributions regarding why financing R&D projects might be distinct from financing other types of projects and the channels through which financial intermediaries and capital markets can impact innovation. They then discuss empirical studies on financing innovation in mature firms, in particular the literature on how ownership and capital structure impact the amount and nature of innovation undertaken by firms. The paper also looks at innovation in startups and the growing literature on the effect that multi-stage financing has on innovation in young firms. Three main themes emerge: 1) A growing body of work documents a role for debt financing related to innovation. 2) A very active area of research has looked at "learning" across multi-stage financing. 3) There is strong interaction between financing choices for innovation and changing external conditions. Key concepts include: Financing constraints can be extensive in the context of firms engaged in R&D and innovation-with the ability to shape both the rate and the trajectory of innovation. Capital structure plays a central role in the outcome of innovations. Bank finance is an important source of finance, particularly for larger firms with tangible and intangible assets to pledge as collateral. Public markets may provide deep pockets but pose a set of agency costs that might be particularly harmful for firms engaged in exploration and novel innovations. There is a growing interest among academics and practitioners in the multi-stage financing of innovation, both in established firms and startups, and understanding the optimal contracts and policies that might stimulate innovation.  
   
 Closed for comment; 0 Comments.

Small- and medium-sized enterprises and entrepreneurs around the world frequently face "institutional voids" of credit: In many places there are systematic constraints to obtaining credit stemming from underdeveloped capital and intermediary markets, regulatory systems, contract-enforcing mechanisms, and so on. In many countries, microfinance institutions (MFIs) help overcome such gaps by providing small- and low-interest loans to low-income individuals for them to establish small businesses. However, even though a great deal is known about the effects of MFIs in facilitating the development of SMEs and small entrepreneurs, we still need to understand how variation in institutional contexts shapes the way in which MFIs are effective in bridging these gaps. In this paper, the authors examine the effect of globalization on MFI operations across developing and emerging economies, looking specifically at more than 2,000 MFIs from 119 emerging and developing countries around the world over the period 2002-2012. Overall, findings shed light on both the bright side and the dark side of globalization from the perspectives of how social organizations (MFIs) can serve the global poor. Key concepts include: This paper contributes to understanding the dynamics of institutional voids in emerging economies. Globalization processes can both ameliorate and exacerbate challenges of institutional voids in emerging and developing economies. A key outcome to understand MFI operation and effectiveness is the interest rates they charge their customers.  
   
 Closed for comment; 0 Comments.

Steady and reliable earnings bring many advantages to the firms that deliver them. Share prices rise, capital costs decline, and bonuses become both bigger and more likely. Such firms grow faster and attract more talented people to manage that growth. Despite these benefits, however, scholars and practitioners have long been critical of the short-term focus that often characterizes western managers. In this paper the authors develop and describe a model suggesting that the solution to this seeming paradox lies in the fact that earnings management, above a given threshold, is relatively harmless, but below this threshold it can be disastrous. The results have important implications for understanding managerial incentives and the internal processes that create sustained advantage. Key concepts include: The model in this paper reconciles the tension in management scholarship between those who have shown that a focus on "managing earnings" is associated with better performance in the capital markets and those who have suggested it may be dangerously short sighted. Balancing attention to both short and long term investments may be a critical source of competitive advantage. A key source of above average performance might be the differential ability of firms to create relational contracts that incorporate subjective evaluations of capability.  
   
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The process of value creation starts with the choice of a promising company, extends through the structure of the investment and into the deal management process, and ends as the venture capitalist positions the company for an exit to a situation where it can continue to grow. In all regions, value creation plays an important role in every venture capital investment. Given the relative youth of the industry in Latin America and the Caribbean (LAC), the issue of value addition is particularly critical. In this paper the authors draw on scholarship, industry statistics, and interviews with six LAC fund managers. They also place the material in the context of their combined 56 years of experience studying the VC industry in order to describe the challenges facing fund managers in value creation. The paper concludes with nine best practices that should be especially helpful in LAC as these economies develop. Key concepts include: There are nine best practices for creating value in portfolio companies. Some of them apply to the internal operations of the VC firm while others address methods through which the fund managers interact with the portfolio companies. An unwillingness to risk failure restrains LAC's innovative and entrepreneurial culture. Entrepreneurs in the LAC region are less familiar with best practices in business, such as reaching beyond family and friends for investors in their companies, and most are new to the expectations of active, equity-owning investors. Situations vary greatly between countries. What works in one LAC country may not succeed in another, forcing fund managers to be particularly flexible and creative to add value in their portfolio companies.  
   
 Closed for comment; 0 Comments.

As life expectancy expands, seniors face a new threat: outliving their retirement savings. Robert Pozen says new Treasury rules will encourage purchase of "longevity annuities" that provide income into the 80s and 90s.  
   
 Closed for comment; 0 Comments.

Apple wants to convert your iPhone into a digital wallet with Apple Pay. Professors Benjamin Edelman and Willy Shih assess its chances for success and wonder if consumers have a compelling reason to make the switch.  
   
 Closed for comment; 12 Comments posted.

One of the most dramatic reversals in Federal Reserve policymaking has been the targeting of monetary policy towards financial stability. In 1923, for example, the Federal Reserve's Annual Report officially announced that the goal of monetary policy was the avoidance of speculative lending, which was thought to lead to inflation and crisis. By contrast, in 2002 there was broad agreement at the Fed with economist Ben Bernanke's view that monetary policy should be aimed exclusively at macroeconomic goals while financial stability should be ensured by regulatory means instead. In this paper the author explains when this reversal occurred and he sheds some light on why it did. He shows that two principles in 1923—the discouraging of speculative lending by commercial banks, and the desire to meet the credit needs of business—remained important in Federal Open Market Committee (FOMC) deliberations until the mid-1960's. After this, the FOMC spent less time discussing the composition of bank loans. Overall, as the author argues, an unwillingness to devote monetary policy to financial stability may well make financial crises more likely. This paper may thus contribute to the understanding of the ultimate sources of the financial crisis of 2007. Key concepts include: This paper explores the persistence and some of the consequences of the eventual abandonment by the FOMC of principles embedded in the Federal Reserve's Tenth Annual Report of 1923. As the Fed directs monetary policy towards financial stability, the history of how it abandoned this earlier goal contains lessons for the future. Understanding the abandonment of the Fed's 1923 principles also sheds light on the relevance of various views about what determines Fed policy.  
   
 Closed for comment; 0 Comments.

The massive surge of foreign capital to emerging markets in the aftermath of the global financial crisis of 2008-2009 has led to a renewed debate about the merits of international capital mobility. To stem the flow of capital and manage the attendant risks, several emerging markets have recently imposed taxes or controls to curb inflows of foreign capital. The case for capital controls usually rests on measures designed to mitigate the volatility of foreign capital inflows. However, controls also have an implicitly protectionist aspect aimed at maintaining persistent currency undervaluation. In this paper the authors investigate the effects of capital controls on firm-level stock returns and real investment using data from Brazil. Brazil is important because it has taken center stage as a country that has implemented extensive controls on capital flows between 2008 and 2012. Among the authors' key findings, real investment at the firm level falls significantly in the aftermath of controls. Overall, capital controls can increase market uncertainty and reduce the availability of external finance, which in turn can lower investment at the firm level. Capital controls disproportionately affect small, non-exporting firms, especially those more dependent on external finance. Key concepts include: Capital controls policy measures range from large-scale efforts to reduce the volatility of foreign capital inflows to a protectionist stance on maintaining the competitiveness of the external sector. The intended purpose of controls notwithstanding, evidence in this paper suggests that capital controls can increase market uncertainty and reduce the availability of external finance, which in turn can lower investment at the firm level. Controls affect small, non-exporting firms most, especially those more dependent on external finance.  
   
 Closed for comment; 0 Comments.

Created in the 1930s, outlet stores allowed retailers to dispose of unpopular items at fire-sale prices. Today, outlets seem outmoded and unnecessary—stores have bargain racks, after all. Donald K. Ngwe explains why outlets still exist.  
   
 Open for comment; 9 Comments posted.

In part three of her series on the state of small-business lending, Karen Mills discusses how public-private partnerships and government guarantee programs have the potential to enhance economic growth.  
   
 Closed for comment; 0 Comments.

Small businesses are core to US economic competitiveness. Not only do they employ half of the nation's private sector workforce--about 120 million people--but also since 1995 they have created approximately two‐thirds of the net new jobs in the country. Yet in recent years, small businesses have been slow to recover from the recession and credit crisis that hit them especially hard. This lag has prompted the question, "Is there a credit gap in small business lending?" In this paper the authors compile and analyze the current state of access to bank capital for small business from the best available sources. The authors explore both the cyclical impact of the recession on small business and access to credit, and several structural issues that impede the full recovery of bank credit markets for smaller loans. They argue that the online banking market is likely to continue to grow, disrupting traditional ways of lending to small businesses. This will create both opportunities and risks for policymakers and regulators. Key concepts include: Small businesses create two out of every three net new jobs, but there remains a significant jobs gap. Structural issues make it more difficult for community banks to fill market gaps in small-business lending. New entrants are innovating and using technology in ways that improve access, time needed for delivery of capital, and the overall borrower experience. The policy challenge is to ensure that these new marketplaces have sufficient oversight to prevent abuse, but not too much oversight that the innovation is dampened or delayed.  
   
 Closed for comment; 0 Comments.