Accepted Manuscript

The Effects of Institutional Investor Objectives on Firm Valuation and Governance

Paul Borochin, Jie Yang

PII: S0304-405X(17)30130-7
DOI: 10.1016/j.jfineco.2017.06.013
Reference: FINEC 2789

To appear in: *Journal of Financial Economics*

Received date: 22 March 2016
Revised date: 7 September 2016
Accepted date: 10 October 2016

Please cite this article as: Paul Borochin, Jie Yang, The Effects of Institutional Investor Objectives on Firm Valuation and Governance, *Journal of Financial Economics* (2017), doi: 10.1016/j.jfineco.2017.06.013

The Effects of Institutional Investor Objectives on Firm Valuation and Governance *

Paul Borochin
School of Business
University of Connecticut†

Jie Yang
Board of Governors of the
Federal Reserve System‡

This version: November, 2016

Abstract

We find that ownership by different types of institutional investors has varying implications for future firm misvaluation and governance characteristics. Dedicated institutional investors decrease future firm misvaluation, in both direction and magnitude, relative to fundamentals. In contrast, transient institutional investors have the opposite effect. Using the U.S. Securities and Exchange Commission (SEC) Regulation FD as an exogenous shock to information dissemination, we find evidence consistent with dedicated institutions having an information advantage. Similarly, dedicated investors are associated with better future governance characteristics, while transient investors are not. The valuation effects are primarily driven by institutional portfolio concentration while the governance effects are driven by portfolio turnover. These results imply a more nuanced relationship between institutional ownership and firm value and corporate governance.

Keywords: Institutional investors, investor type, dedicated, transient, misvaluation, corporate governance, blockholding, portfolio turnover, information dissemination, SEC Regulation FD

JEL classification: G30, G32, G14, G23

*We thank Bill Schwert (Editor), an anonymous referee, Reena Aggarwal, Joseph Golec, David Robinson, seminar participants at Georgetown University, University of Baltimore, University of Massachusetts Lowell, and the Office of the Comptroller of the Currency, and participants at the 2016 European Financial Management Association Meeting and 2016 Financial Management Association. The ideas in this paper are solely those of the authors and do not necessarily reflect the view of the Federal Reserve System. All remaining errors are our own.

†2100 Hillside Road, Unit 1041, Storrs, CT 06269. Phone: (860) 486-2774. Email: paul.borochin@uconn.edu.

‡Corresponding author: 20th Street and Constitution Avenue, N.W., Washington, DC 20551. Phone: (202) 736-1939. Fax: (202) 245-4213. Email: jie.yang@frb.gov.