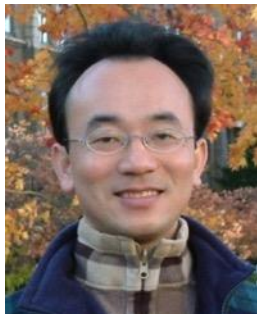# Event Studies in Finance

1132AIFQA04

MBA, IM, NTPU (M5147) (Spring 2025)

Tue 5, 6, 7 (13:10-16:00) (B3F17)

Min-Yuh Day, Ph.D,
Professor

Institute of Information Management, **National Taipei University**

https://web.ntpu.edu.tw/~myday

https://meet.google.com/
miy-fbif-max

2025-03-11

Syllabus

Week   Date   Subject/Topics

1 2025/02/18 Introduction to Artificial Intelligence in Finance and
Quantitative Analysis

2 2025/02/25 AI in FinTech: Metaverse, Web3, DeFi, NFT,
Generative AI for Financial Innovation Applications

3 2025/03/04 Investing Psychology and Behavioral Finance

4 2025/03/11 Event Studies in Finance

5 2025/03/18 Case Study on AI in Finance and Quantitative Analysis I

6 2025/03/25 Finance Theory and Data-Driven Finance

Syllabus

Week   Date   Subject/Topics

7 2025/04/01 Self-Study

8 2025/04/08 Midterm Project Report

9 2025/04/15 Financial Econometrics

10 2025/04/22 AI-First Finance

11 2025/04/29 Industry Practices of AI in Finance and
                 Quantitative Analysis

12 2025/05/06 Case Study on AI in Finance and Quantitative Analysis II

Syllabus

Week   Date   Subject/Topics

13 2025/05/13 Deep Learning in Finance;
            Reinforcement Learning in Finance;
            Generative AI in Finance

14 2025/05/20 Algorithmic Trading; Risk Management;
            Trading Bot and Event-Based Backtesting

15 2025/05/27 Final Project Report I

16 2025/06/03 Final Project Report II

Event Studies in Finance

Outline

- **Event Studies in Finance**

- **Event Studies for Financial Research**

- **Event Study Methodology**

- **Efficient Market Hypothesis (EMH)**

  - **Efficient Markets**

  - **Inefficient Markets**

Doron Kliger and Gregory Gurevich (2014),
Event Studies for Financial Research:
A Comprehensive Guide,
Palgrave Macmillan

EVENT STUDIES
FOR FINANCIAL
RESEARCH

A COMPREHENSIVE GUIDE

DORON KLIGER AND GREGORY GUREVICH
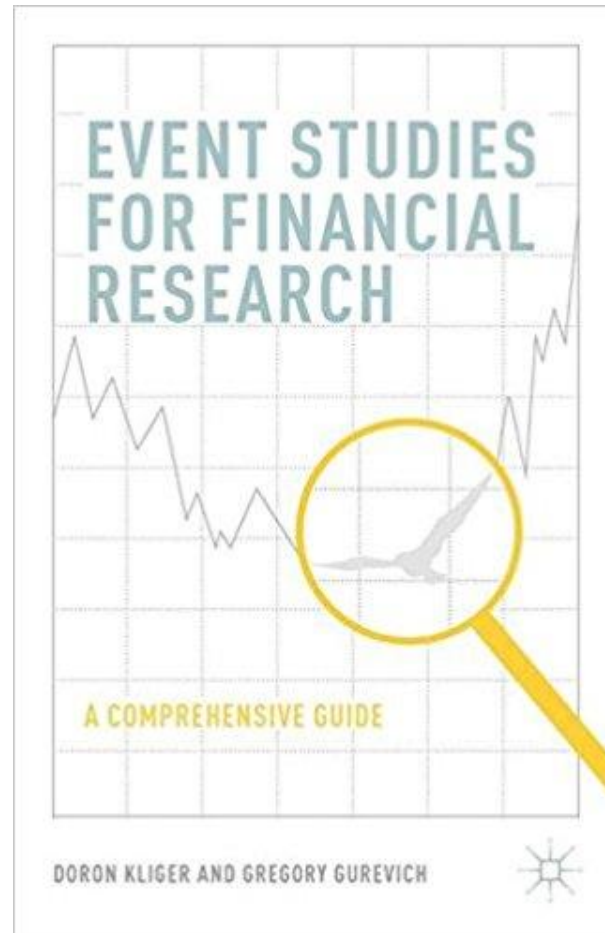
Event Studies in Finance

- **Event studies are widely used in finance research to investigate the implications of**
  - **Announcements of corporate initiatives**
    - Mergers and acquisitions, equity and debt issuance, dividends and repurchases, corporate restructuring
  - **Regulatory changes**
    - Board reform, compensation, changes in taxation, workplace safety
  - **Macroeconomic shocks on stock prices**
    - The COVID-19 pandemic, Brexit, the Paris Agreement

Event Studies in ESG and Sustainable Finance

- Atz, U., Van Holt, T., Liu, Z. Z., & Bruno, C. C. (2023). **Does sustainability generate better financial performance? review, meta-analysis, and propositions**. Journal of Sustainable Finance & Investment, 13(1), 802-825.

- Kumar, S. (2023). **Exploratory review of esg factor attribution to the portfolio return in Fama-French factor model framework**. Academy of Marketing Studies Journal, 27, 1-20.

- Leite, B. J., & Uysal, V. B. (2023). **Does ESG matter to investors? ESG scores and the stock price response to new information**. Global Finance Journal, 100851.

- Li, Z., Feng, L., Pan, Z., & Sohail, H. M. (2022). **ESG performance and stock prices: evidence from the COVID-19 outbreak in China**. Humanities and Social Sciences Communications, 9(1), 1-10.

- Wang, J., Hu, X., & Zhong, A. (2023). **Stock market reaction to mandatory ESG disclosure**. Finance Research Letters, 53, 103402.

Firm-level Event Studies

- **M&As**

- **Restructuring**

- **Equity issuance**

- **Dividends**

- **Analyst forecasts and recommendations**

- **Earnings**

Single- and Cross-county Event Studies

published in the four major finance and IB journals

Firm-level events

Event/sample	Single-country sample					Cross-country sample					Cross country (%)
	JF	JFE	RFS	JIBS	Total	JF	JFE	RFS	JIBS	Total	
Firm-level events											
M&As	35	50	13	0	98	0	1	3	15	19	16.24
Restructuring	16	18	3	0	37	0	0	0	2	2	5.13
Equity issuance	15	15	6	0	36	0	1	0	0	1	2.70
Dividends	9	11	3	0	23	0	0	0	0	0	0.00
Analyst forecasts and recommendations	9	6	3	0	18	0	0	2	0	2	10.00
Earnings	9	5	4	0	18	0	0	1	1	2	10.00
Board structure changes	7	9	3	0	19	0	0	0	0	0	0.00
Debt issuance	4	9	3	0	16	0	1	0	0	1	5.88
Investor activism and voting	2	10	5	0	17	0	0	0	0	0	0.00
Listing/delisting	10	0	0	0	10	2	3	1	1	7	41.18
Share repurchases	5	9	1	0	15	0	0	0	0	0	0.00
News	3	7	5	0	15	0	0	0	0	0	0.00
Managerial turnover	4	7	2	0	13	0	0	0	0	0	0.00
Bankruptcy and liquidation	6	3	2	0	11	0	0	0	0	0	0.00
Managerial compensation	4	6	1	0	11	0	0	0	0	0	0.00
Credit ratings	5	3	1	0	9	0	0	0	0	0	0.00
Right offerings	2	6	0	0	8	0	0	0	0	0	0.00
Bank loan	3	3	1	0	7	0	0	0	0	0	0.00
IPOs, IPO lockups, and quiet period	2	2	3	0	7	0	0	0	0	0	0.00

Single- and Cross-county Event Studies

published in the four major finance and IB journals

Country-level events

Event/sample	Single-country sample					Cross-country sample					Cross country (%)
	JF	JFE	RFS	JIBS	Total	JF	JFE	RFS	JIBS	Total	
Country-level events											
Governance reform/legislative change	8	15	6	0	29	2	1	0	0	3	9.38
Elections/Political risk events	0	8	5	0	13	1	0	1	2	4	23.53
Monetary policy	5	4	1	0	10	0	0	2	0	2	16.67
Market trading mechanism changes	3	6	1	0	10	1	0	0	0	1	9.09
Government intervention	2	0	1	0	3	3	0	1	0	4	57.14
Macroeconomic and gov. announcement	0	4	2	0	6	0	0	0	0	0	0.00
News	0	1	0	0	1	1	1	0	0	2	66.67
Exchange rates and parity deviation	0	0	0	0	0	0	1	0	2	3	100.00
Natural disasters	0	3	0	0	3	0	0	0	0	0	0.00
Stock market liberalization	0	0	0	0	0	2	0	0	0	2	100.00
Sovereign debt rating changes	0	0	0	0	0	0	2	0	0	2	100.00
Tax enforcement	0	1	0	0	1	0	0	0	1	1	50.00

Single- and Cross-county Event Studies
published in the four major finance and IB journals

Peer-level events

Event/sample	Single-country sample					Cross-country sample					Cross country (%)
	JF	JFE	RFS	JIBS	Total	JF	JFE	RFS	JIBS	Total	
Peer-level events											
Distress in bank–borrower relationship	3	1	0	0	4	0	0	0	0	0	0.00
Bankruptcy	0	3	0	0	3	0	0	0	0		0.00
M&As	0	3	0	0	3	0	0	0	0		0.00
Security issuance	2	0	1	0	3	0	0	0	0		0.00
Regulatory enforcement	0	2	0	0	2	0	0	0	0		0.00
Product market entry	1	1	0	0	2	0	0	0	0		0.00
Earnings	0	0	2	0	2	0	0	0	0		0.00
Proxy contests	0	2	0	0	2	0	0	0	0		0.00
Others	0	14	3	0	17	0	0	0	0	0	0.00

Event Studies for Financial Research

state-of-the-art
event study software

event studies

Short- and Long-Term Event Studies

Cumulative Abnormal Returns
Buy-and-hod Abnormal Returns
Farma-French Calander Time Portfolios

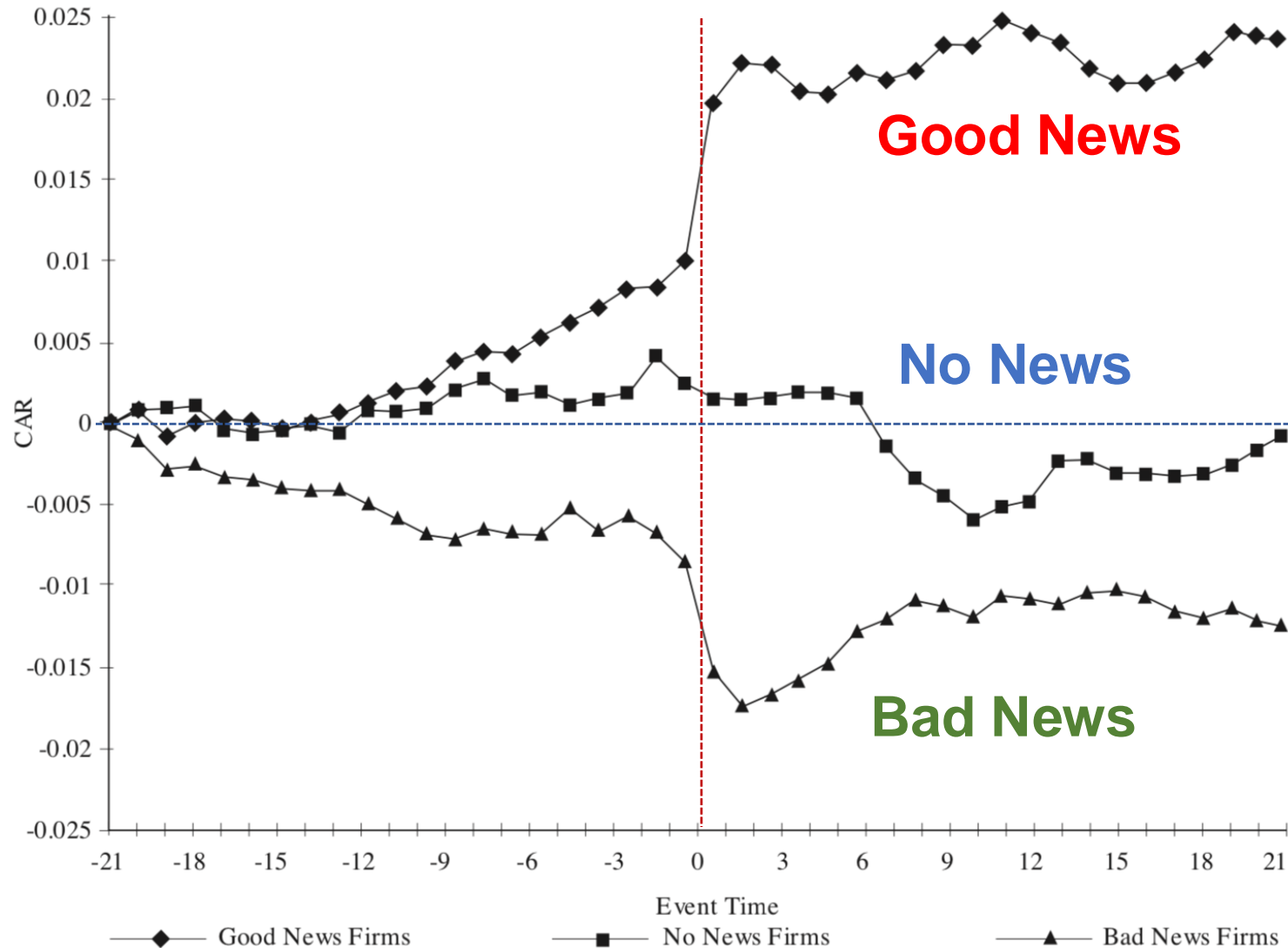## Parametric and Non-Parametric Tests

Time-Series t-Test
Cross-Sectional t-Test
Standardized Residual Test
Standardized Cross-Sectional Test
Corrado Rank Test
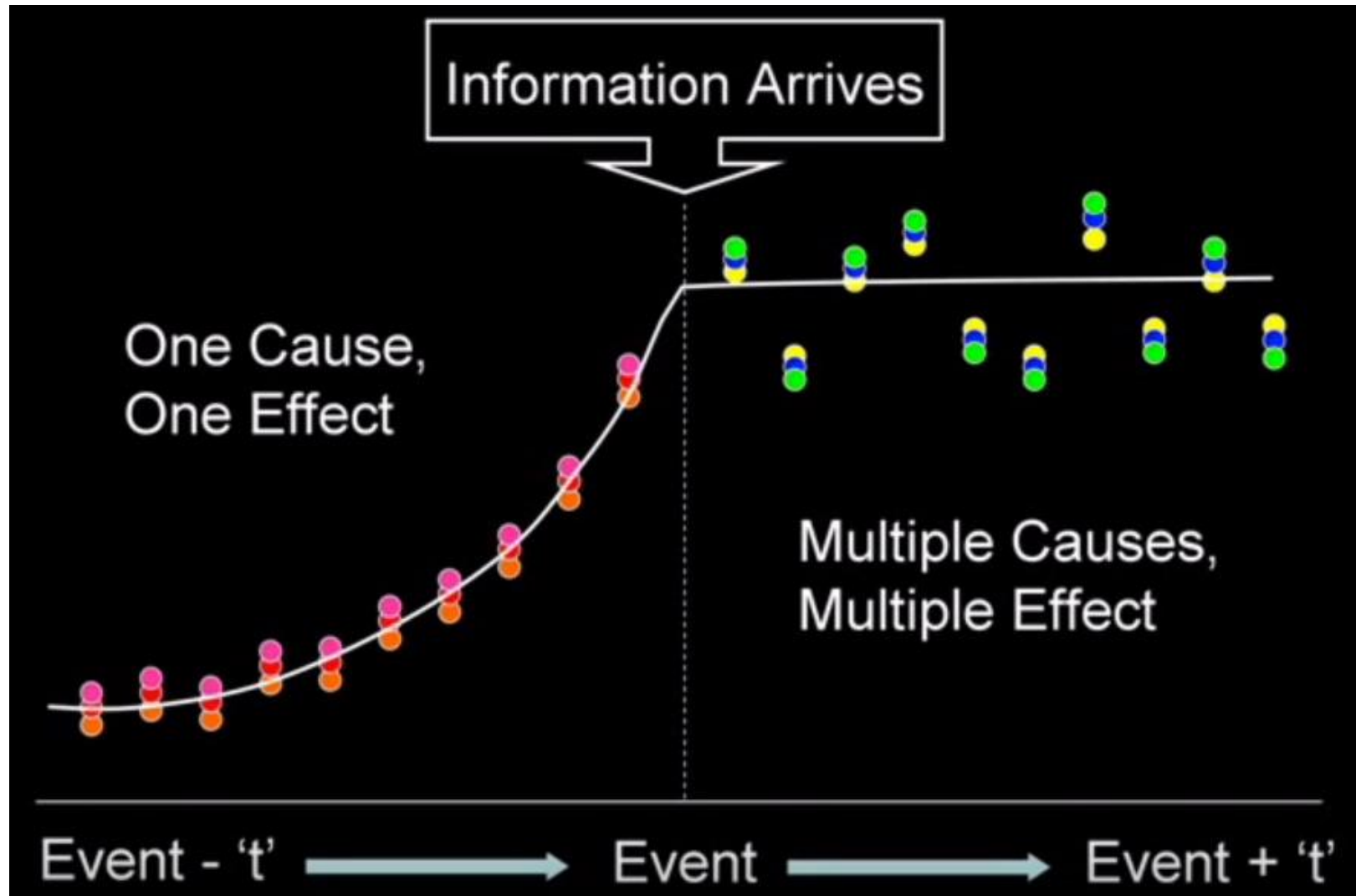Generalized Sign Test
Skewness-Adjusted t-Test

Return Models

Constant-Mean
Market Adjusted
Market Model
Factor Model
Matching Models
Stocks and Bonds

https://eventstudymetrics.com/

Event Studies in Economics and Finance

Source: MacKinlay, A. C. (1997). Event studies in economics and finance. Journal of economic literature, 35(1), 13-39.

Event Study

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Event Study
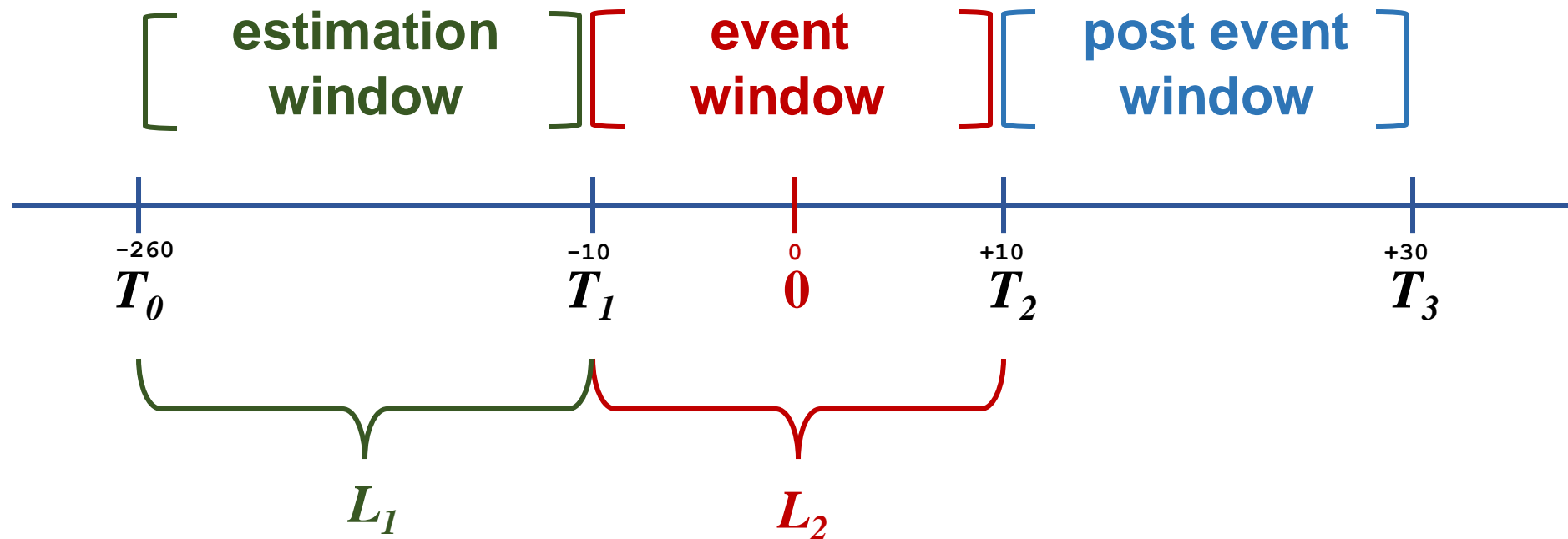# Time line for an event study

Event

Event Study Methodology
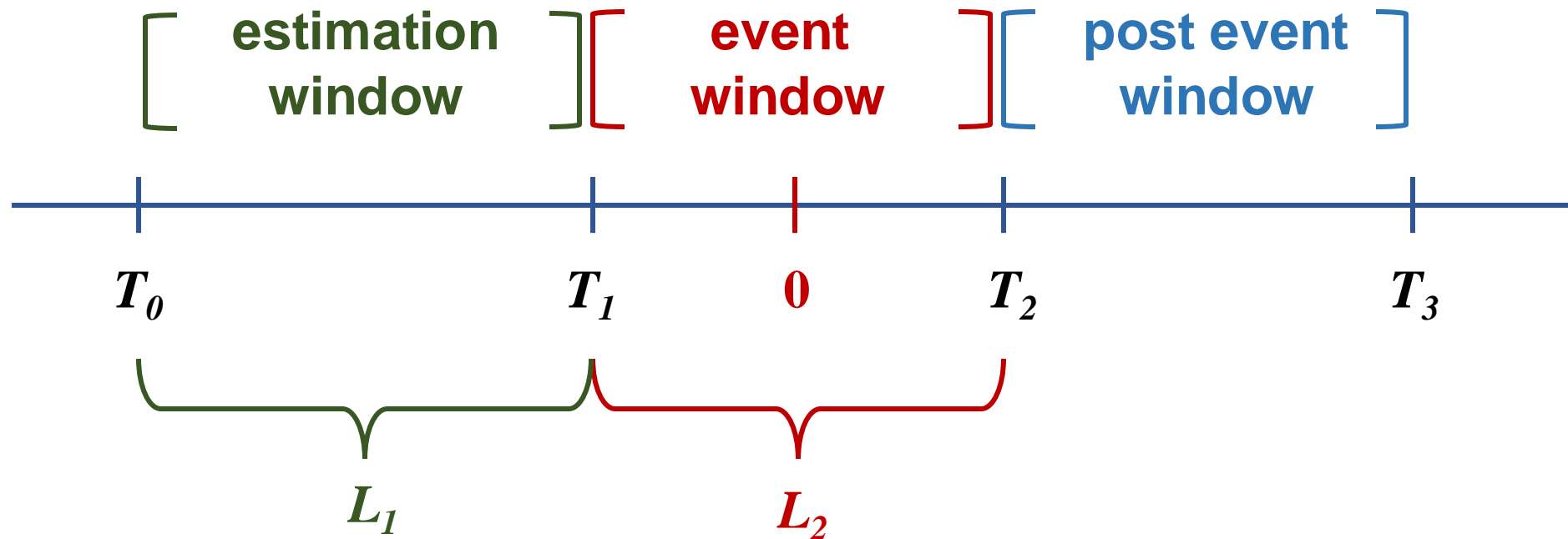
Event Study Methodology
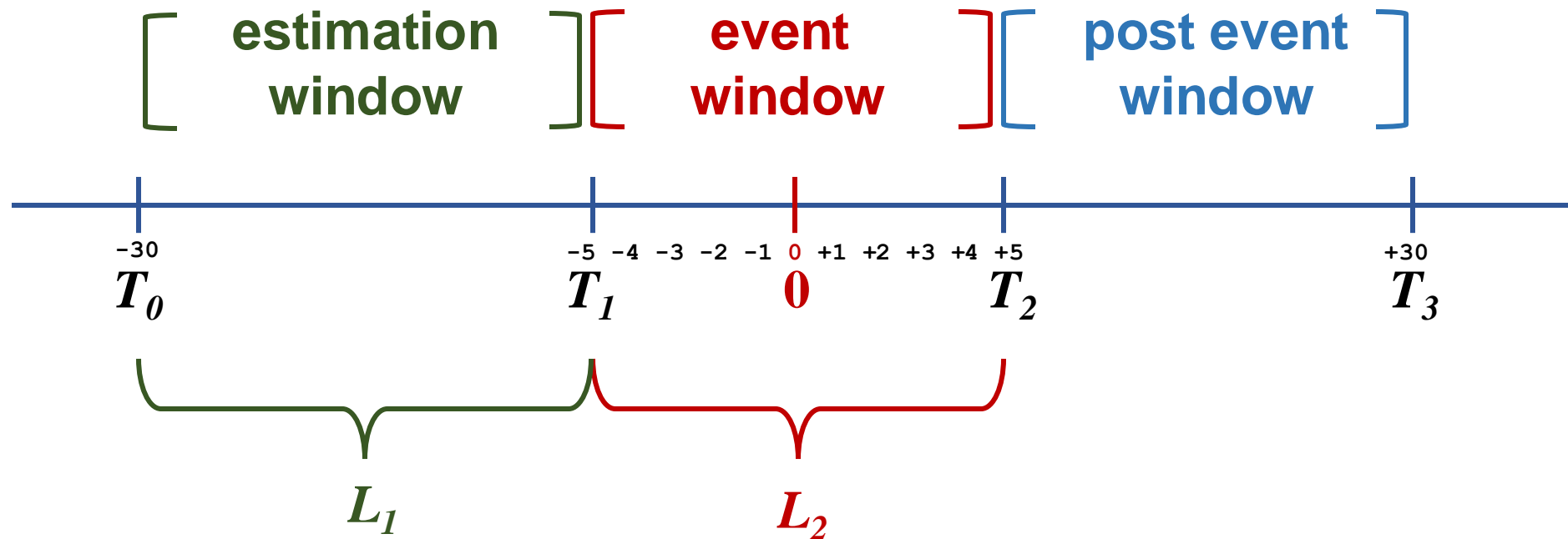
Event Study Methodology

Efficient Markets

Behavioral Economics

Behavioral Finance

Rational Behavior

Irrational Behavior

Emotion

Sentiment

Modern Financial Research

- **Theoretical Finance**

  - **study of logical relationships among assets.**

- **Empirical Finance**

  - **study of data in order to infer relationships.**

- **Behavioral Finance**

  - **integrates psychology into the investment process.**

Behavioral Finance Themes

- **Heuristic-Driven Bias**

- **Framing Dependence**

- **Inefficient Markets**

Efficient Market Hypothesis (EMH)

Efficient Market Hypothesis (EMH) (Fama, 1970)

Efficient capital markets: A review of theory and empirical work

EF Fama - The Journal of Finance, 1970

This paper reviews the theoretical and empirical iterature on the efficient markets model. After a discussion of the theory, empirical work concerned with the adjustment of security prices to three relevant information subsets is considered. First, weak form tests, in which the information set is just historical prices, are discussed. Then semi-strong form tests, in which the concern is whether prices efficiently adjust to other information that is obviously …

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Malkiel, B. G., & Fama, E. F. (1970).
Efficient capital markets: A review of theory and empirical work.
The Journal of Finance, 25(2), 383-417.

Efficient Market Hypothesis (EMH) (Fama, 1970)

SESSION TOPIC: STOCK MARKET PRICE BEHAVIOR

SESSION CHAIRMAN: BURTON G. MALKIEL

EFFICIENT CAPITAL MARKETS: A REVIEW OF THEORY AND EMPIRICAL WORK*

EUGENE F. FAMA**

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EFFICIENT CAPITAL MARKETS: A REVIEW OF THEORY AND EMPIRICAL WORK*

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I. INTRODUCTION

THE PRIMARY ROLE of the capital market is allocation of ownership of the economy's capital stock. In general terms, the ideal is a market in which prices provide accurate signals for resource allocation: that is, a market in which firms can make production-investment decisions, and investors can choose among the securities that represent ownership of firms' activities under the assumption that security prices at any time "fully reflect" all available information. A market in which prices always "fully reflect" available information is called "efficient."

This paper reviews the theoretical and empirical literature on the efficient markets model. After a discussion of the theory, empirical work concerned with the adjustment of security prices to three relevant information subsets is considered. First, *weak form* tests, in which the information set is just historical prices, are discussed. Then *semi-strong form* tests, in which the concern is whether prices efficiently adjust to other information that is obviously publicly available (e.g., announcements of annual earnings, stock splits, etc.) are considered. Finally, *strong form* tests concerned with whether given investors or groups have monopolistic access to any information relevant for price formation are reviewed.[1] We shall conclude that, with but a few exceptions, the efficient markets model stands up well.

TABLE 1 (from [10])
First-order Serial Correlation Coefficients for One-, Four-, Nine-, and Sixteen-Day
Changes in Log_e Price

	Differencing Interval (Days)			
Stock	One	Four	Nine	Sixteen
Allied Chemical	.017	.029	−.091	−.118
Alcoa	.118*	.095	−.112	−.044
American Can	−.087*	−.124*	−.060	.031
A. T. & T.	−.039	−.010	−.009	−.003
American Tobacco	.111*	−.175*	.033	.007
Anaconda	.067*	−.068	−.125	.202
Bethlehem Steel	.013	−.122	−.148	.112
Chrysler	.012	.060	−.026	.040
Du Pont	.013	.069	−.043	−.055
Eastman Kodak	.025	−.006	−.053	−.023
General Electric	.011	.020	−.004	.000
General Foods	.061*	−.005	−.140	−.098
General Motors	−.004	−.128*	.009	−.028
Goodyear	−.123*	.001	−.037	.033
International Harvester	−.017	−.068	−.244*	.116
International Nickel	.096*	.038	.124	.041
International Paper	.046	.060	−.004	−.010
Johns Manville	.006	−.068	−.002	.002
Owens Illinois	−.021	−.006	.003	−.022
Procter & Gamble	.099*	−.006	.098	.076
Sears	.097*	−.070	−.113	.041
Standard Oil (Calif.)	.025	−.143*	−.046	.040
Standard Oil (N.J.)	.008	−.109	−.082	−.121
Swift & Co.	−.004	−.072	.118	−.197
Texaco	.094*	−.053	−.047	−.178
Union Carbide	.107*	.049	−.101	.124
United Aircraft	.014	−.190*	−.192*	−.040
U.S. Steel	.040	−.006	−.056	.236*
Westinghouse	−.027	−.097	−.137	.067
Woolworth	.028	−.033	−.112	.040

* Coefficient is twice its computed standard error.

Cumulative Average Residuals
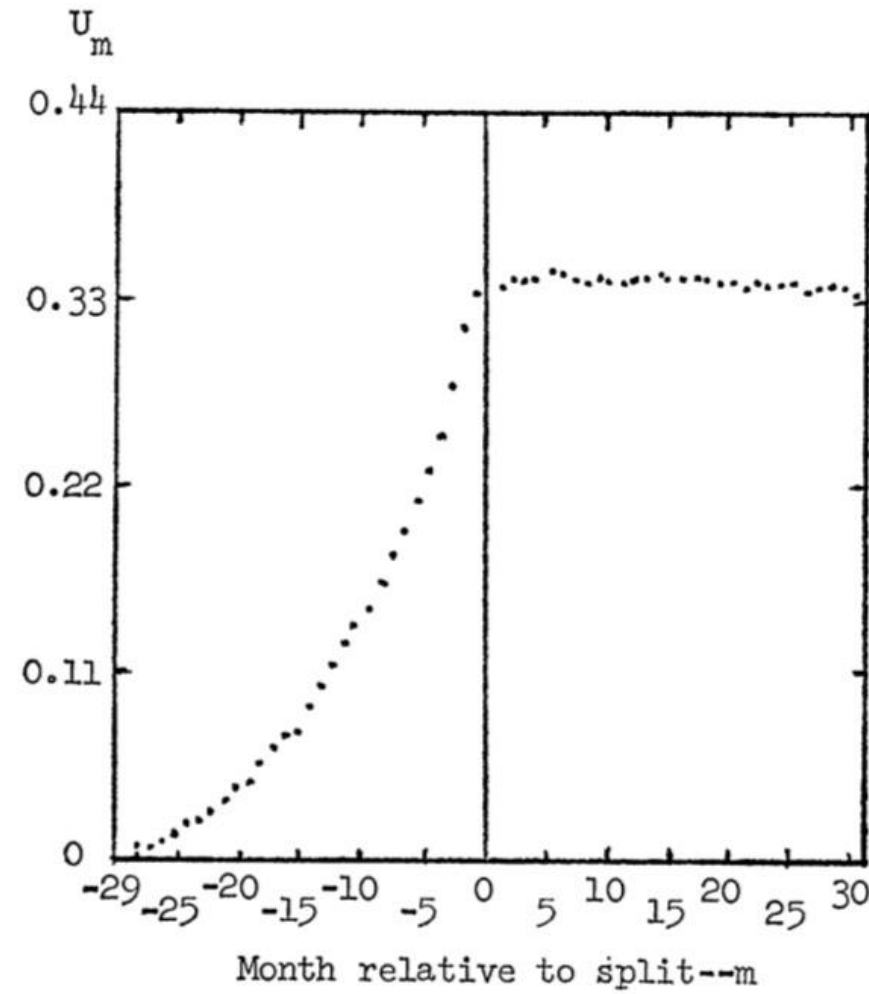
FIGURE 1a
Cumulative average residuals—all splits.

Source: Malkiel, B. G., & Fama, E. F. (1970). Efficient capital markets: A review of theory and empirical work. The Journal of Finance, 25(2), 383-417.
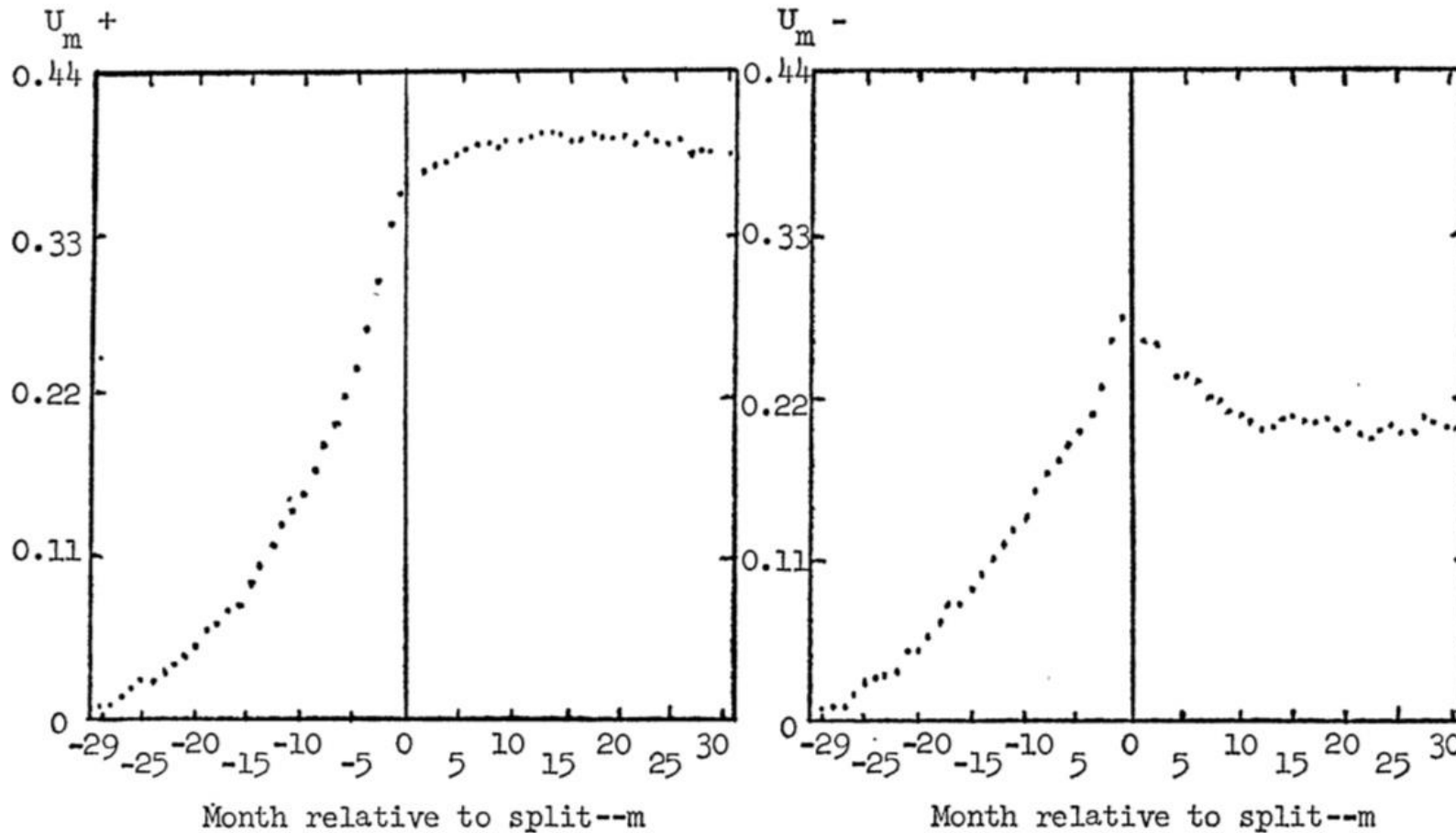
Cumulative Average Residuals

FIGURE 1b
Cumulative average residuals for dividend "increases."

FIGURE 1c
Cumulative average residuals for dividend "decreases."

Market Efficiency

The empirical work itself can be divided into three categories depending on the nature of the information subset of interest. *Strong-form* tests are concerned with whether individual investors or groups have monopolistic access to any information relevant for price formation. One would not expect such an extreme model to be an exact description of the world, and it is probably best viewed as a benchmark against which the importance of deviations from market efficiency can be judged. In the less restrictive *semi-strong-form* tests the information subset of interest includes all obviously publicly available information, while in the *weak form* tests the information subset is just historical price or return sequences.

Source: Malkiel, B. G., & Fama, E. F. (1970). Efficient capital markets: A review of theory and empirical work. The Journal of Finance, 25(2), 383-417.

Types of Efficiency Market

- **Weak Form**
  - **Security prices reflect all information found in past prices and volume.**

- **Semi-Strong Form**
  - **Security prices reflect all publicly available information.**

- **Strong Form**
  - **Security prices reflect all information—public and private.**

Can Financing Decisions Create Value?

Source: Ross et al. (2005), "Corporate Finance", 7th Edition, McGraw–Hill

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What Sort of Financing Decisions?

- **Typical financing decisions include:**
  - **How much debt and equity to sell**
  - **When (or if) to pay dividends**
  - **When to sell debt and equity**
- **Just as we can use NPV criteria to evaluate investment decisions, we can use NPV to evaluate financing decisions.**

How to Create Value through Financing

- **Fool Investors**

  - **Empirical evidence suggests that it is hard to fool investors consistently.**

- **Reduce Costs or Increase Subsidies**

  - **Certain forms of financing have tax advantages or carry other subsidies.**

- **Create a New Security**

  - **Sometimes a firm can find a previously-unsatisfied clientele and issue new securities at favorable prices.**

  - **In the long-run, this value creation is relatively small, however.**

Efficient Capital Markets

- **An efficient capital market is one in which stock prices fully reflect available information.**

- **The EMH has implications for investors and firms.**
  - **Since information is reflected in security prices quickly, knowing information when it is released does an investor no good.**
  - **Firms should expect to receive the fair value for securities that they sell. Firms cannot profit from fooling investors in an efficient market.**

Reaction of Stock Price to New Information in Efficient and Inefficient Markets
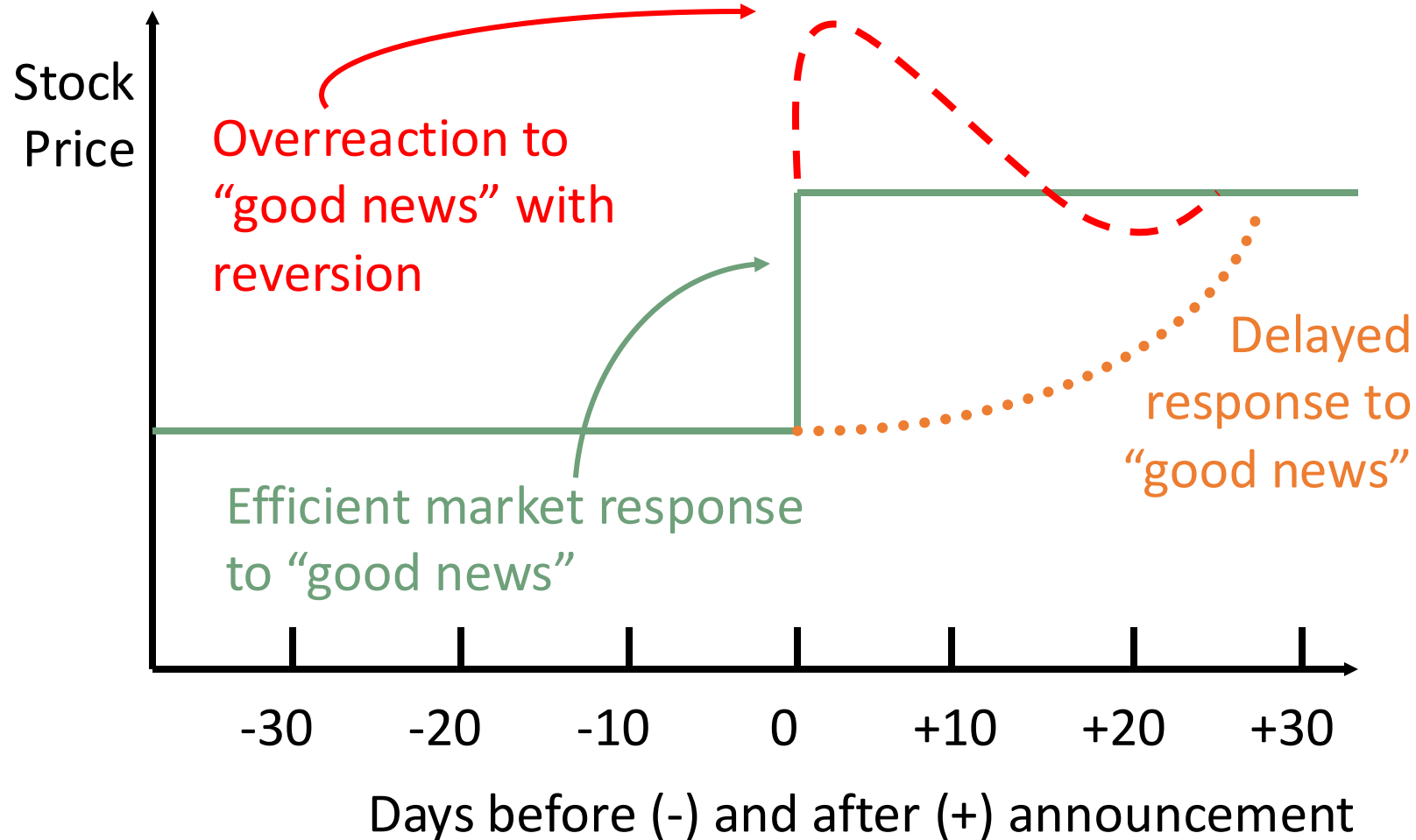
Stock Price

Overreaction to "good news" with reversion

Efficient market response to "good news"

Delayed response to "good news"

-30   -20   -10   0   +10   +20   +30

Days before (-) and after (+) announcement

Reaction of Stock Price to New Information in Efficient and Inefficient Markets

Stock Price

Efficient market response to "bad news"

Delayed response to "bad news"

Overreaction to "bad news" with reversion

-30   -20   -10   0   +10   +20   +30

Days before (-) and after (+) announcement
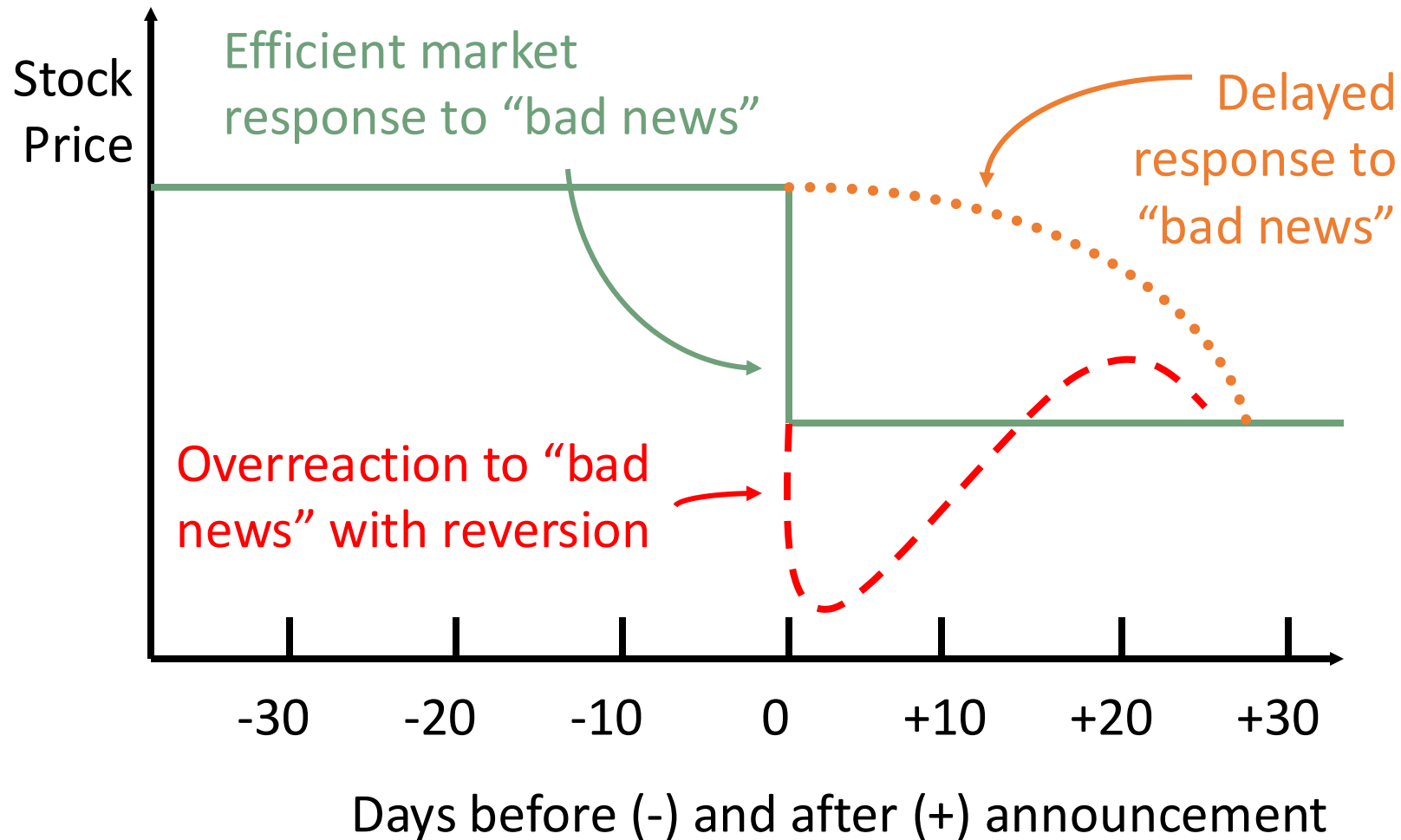
Versions of EMH/Info-Efficiency

- **Weak-form** efficiency:
  - **Prices reflect all information contained in past prices**

- **Semi-strong-form** efficiency:
  - **Prices reflect all publicly available information**

- **Strong-form** efficiency:
  - **Prices reflect all relevant information, include private (insider) information**

all public & private info

all public info

past market info

Source: Markus K. Brunnermeier (2015), "Lecture 10: Market Efficiency", Finance 501: Asset Pricing, Princeton University

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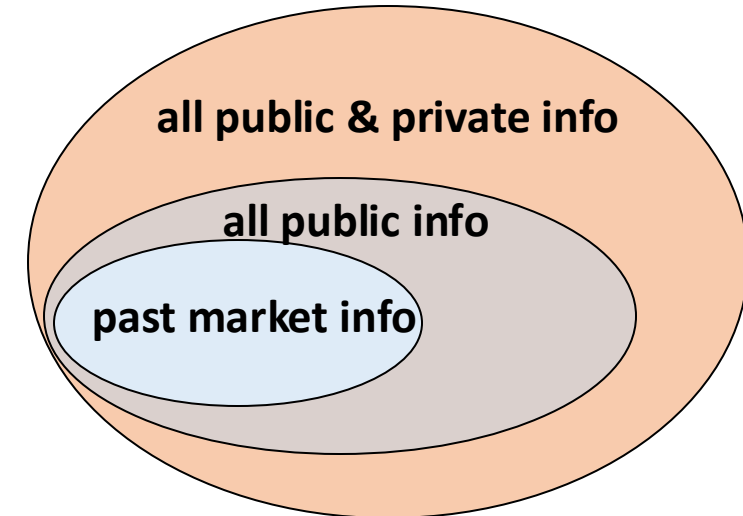
Relationship among
Three Different Information Sets

All information
relevant to a stock

Information set
of publicly available
information

Information
set of
past prices
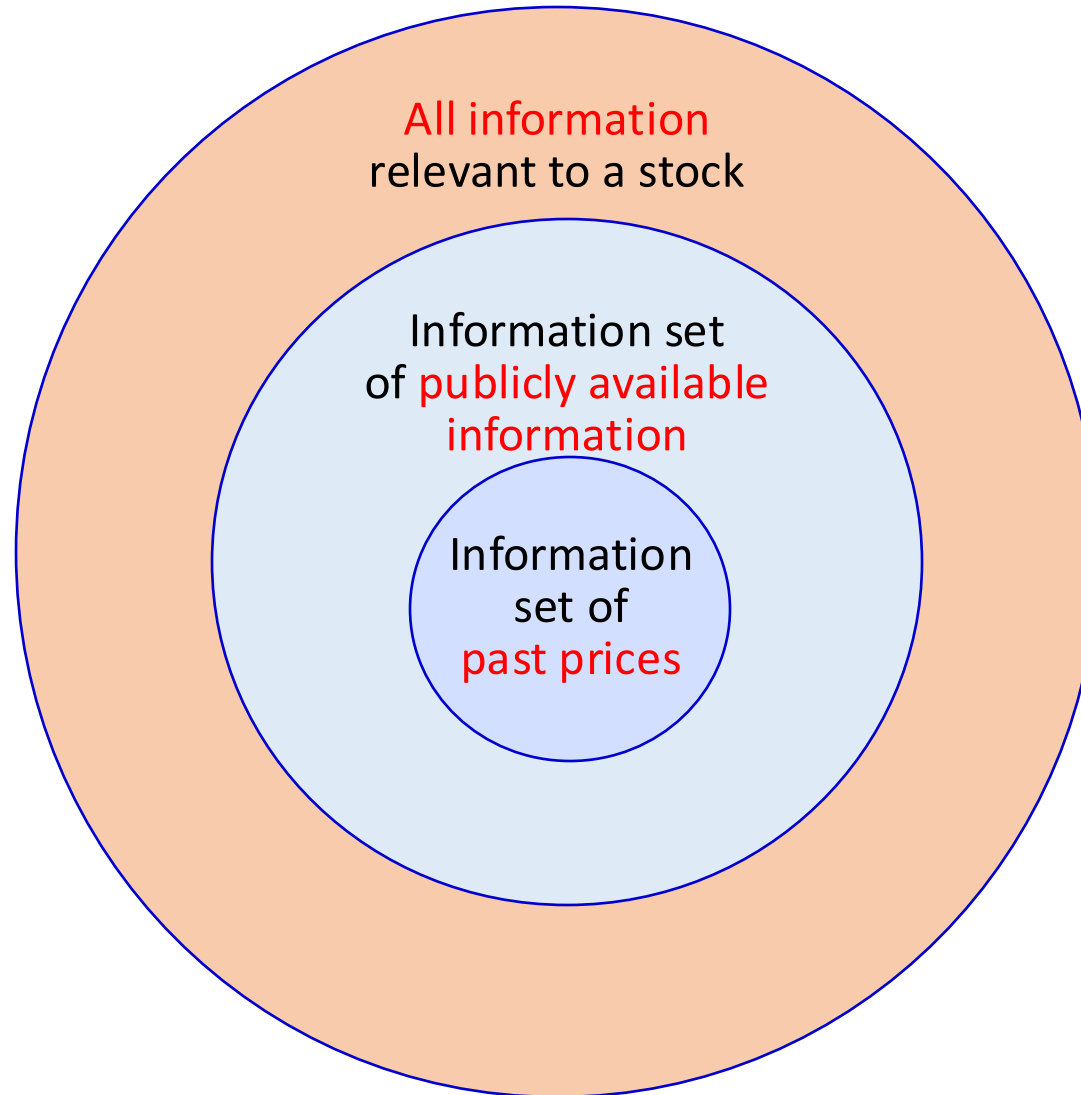
Efficient Market

- **An efficient market incorporates information in security prices.**

- **There are three forms of the EMH:**

  - **Weak-Form EMH**

    Security prices reflect past price data.

  - **Semistrong-Form EMH**

    Security prices reflect publicly available information.

  - **Strong-Form EMH**

    Security prices reflect all information.

- **There is abundant evidence for the first two forms of the EMH.**

Why Technical Analysis Fails

Investor behavior tends to eliminate any profit opportunity associated with stock price patterns.
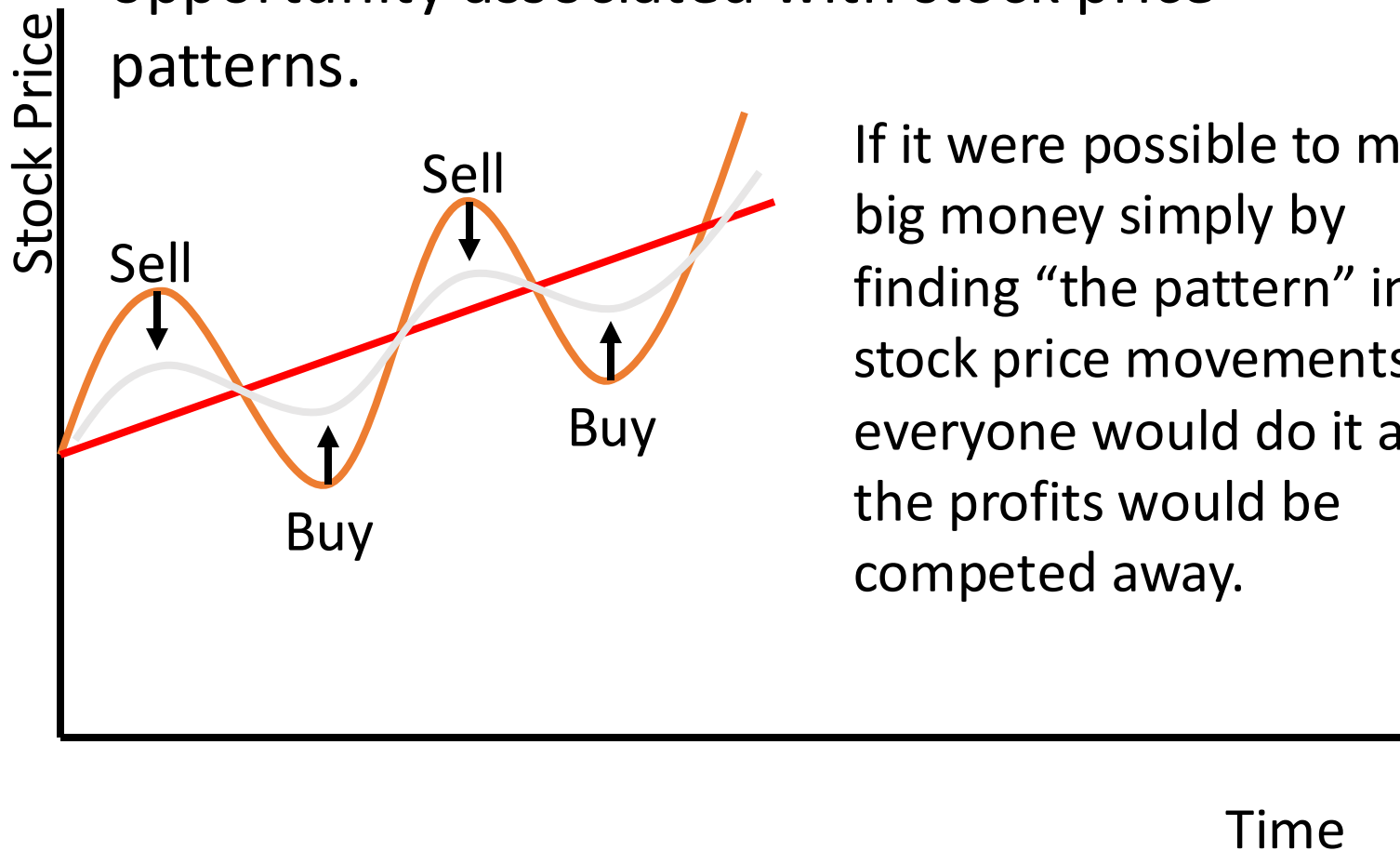
If it were possible to make big money simply by finding "the pattern" in the stock price movements, everyone would do it and the profits would be competed away.

Stock Price

Sell

Sell

Buy

Buy

Time

Evidence on Market Efficiency

- **Return Predictability Studies**

- **Event Studies**

- **Performance Studies**

Event Studies

- **Objective**
  - **Examine if new (company specific) information is incorporated into the stock price in one single price jump upon public release?**

Event Studies Methodology

1. **Define as day "zero" the day the information is released**

2. **Calculate the daily returns R_{it} the 30 days around day "zero":**
    t = -30, -29,…-1, 0, 1,…, 29, 30

3. **Calculate the daily returns R_{mt} for the same days on the market (or a comparison group of firms of similar industry and risk)**

4. **Define Abnormal Returns (AR) as the difference** $AR_{it} = R_{it} - R_{mt}$

5. **Calculate Average Abnormal Returns (AAR) over all N events in the sample for all 60 reference days**

    $$AAR_t = \frac{1}{N} \sum_{i=1}^{N} AR_{it}$$

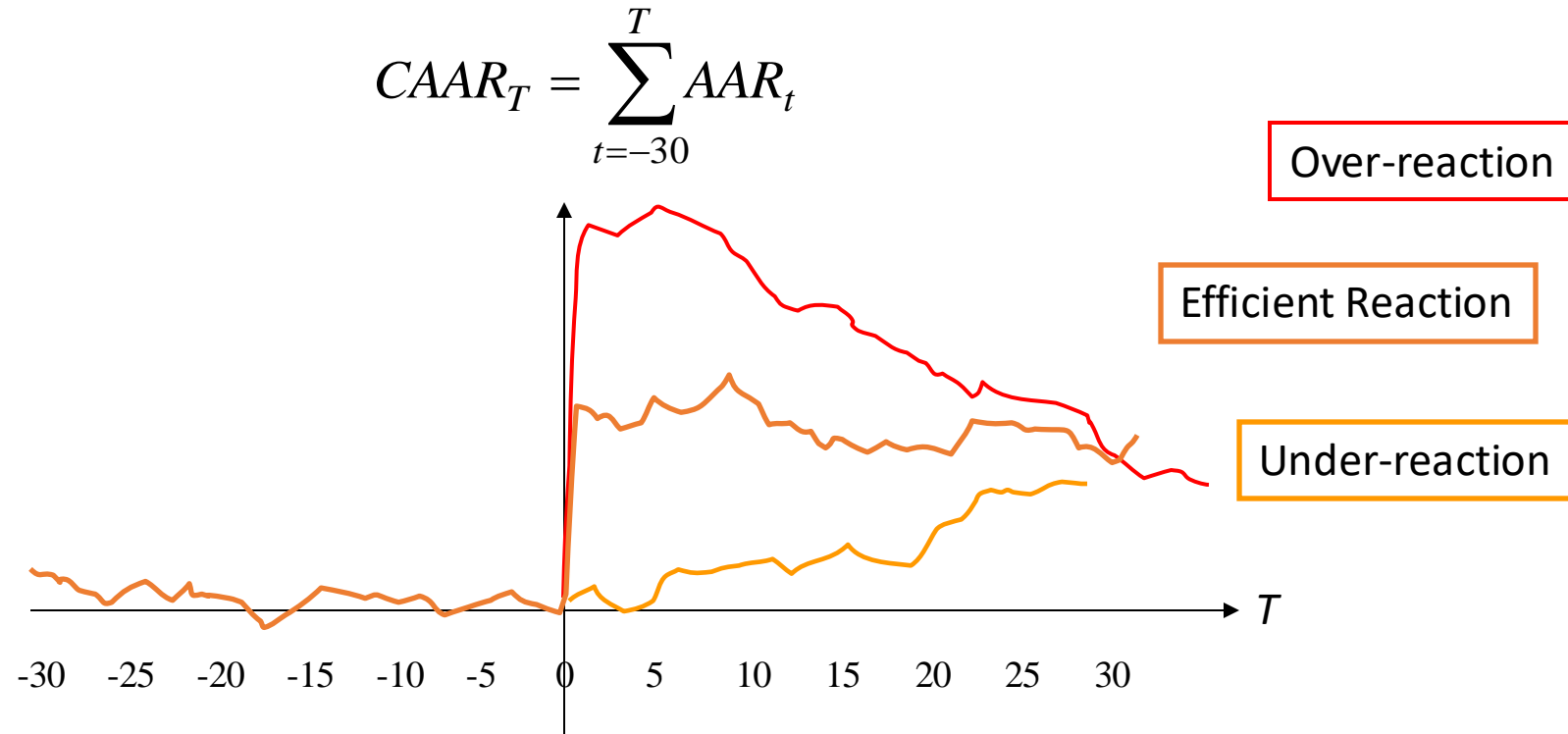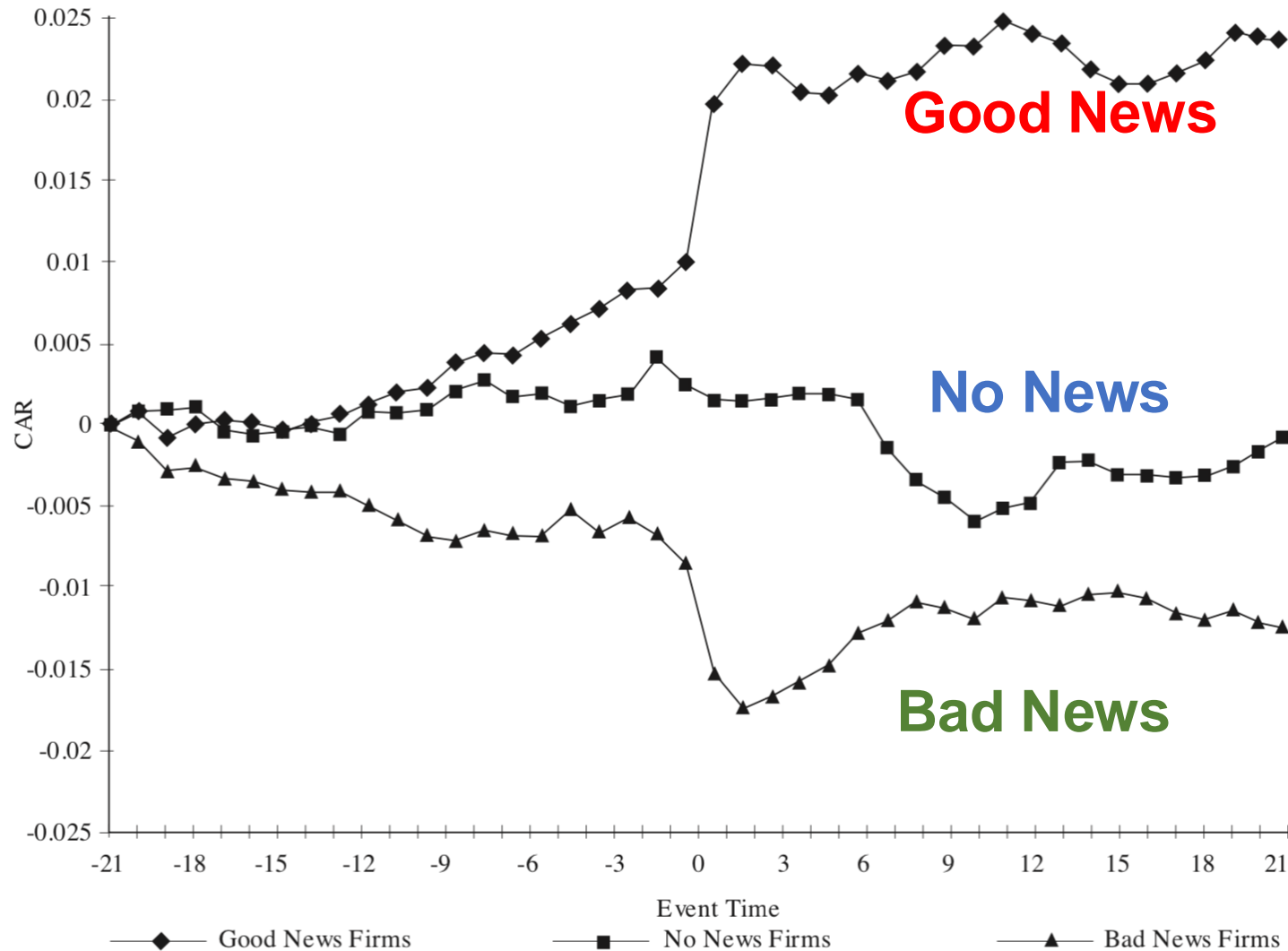6. **Cumulate the returns on the first T days to CAAR**

    $$CAAR_T = \sum_{t=-30}^{T} AAR_t$$

Event Studies Methodology

Step 1.
Define as day "zero" the day the information is released

Source: Markus K. Brunnermeier (2015), "Lecture 10: Market Efficiency", Finance 501: Asset Pricing, Princeton University

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Event Studies Methodology

Step 2.
Calculate the daily returns R_{it} the 30 days around day "zero":
t = -30, -29,...-1, 0, 1,..., 29, 30

Source: Markus K. Brunnermeier (2015), "Lecture 10: Market Efficiency", Finance 501: Asset Pricing, Princeton University

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Event Studies Methodology

Step 3.

Calculate the daily returns R_{mt} for the same days on the market (or a comparison group of firms of similar industry and risk)

Source: Markus K. Brunnermeier (2015), "Lecture 10: Market Efficiency", Finance 501: Asset Pricing, Princeton University

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Event Studies Methodology

Step 4.
Define
Abnormal Returns (AR)
as the difference

$$AR_{it} = R_{it} - R_{mt}$$

Event Studies Methodology

Step 5.
Calculate
Average Abnormal Returns (AAR)
over all N events in the sample for all 60 reference days

$$AAR_t = \frac{1}{N} \sum_{i=1}^{N} AR_{it}$$

Event Studies Methodology

Step 6.
Cumulate the returns on the first T days to
Cumulative Average Abnormal Returns (CAAR)

$$CAAR_T = \sum_{t=-30}^{T} AAR_t$$

Event Studies Methodology

1. **Define as day "zero" the day the information is released**

2. **Calculate the daily returns R_{it} the 30 days around day "zero":**
   t = -30, -29,...-1, 0, 1,..., 29, 30

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6. **Cumulate the returns on the first T days to CAAR** $CAAR_T = \sum_{t=-30}^{T} AAR_t$

Market Efficiency in Event Studies

$$CAAR_T = \sum_{t=-30}^{T} AAR_t$$

Over-reaction

Efficient Reaction

Under-reaction

Source: Markus K. Brunnermeier (2015), "Lecture 10: Market Efficiency", Finance 501: Asset Pricing, Princeton University

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Event Study:
Earning Announcement

Cumulative abnormal returns around earning announcements

(MacKinlay 1997)

Source: Markus K. Brunnermeier (2015), "Lecture 10: Market Efficiency", Finance 501: Asset Pricing, Princeton University

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Event Study: Stock Splits
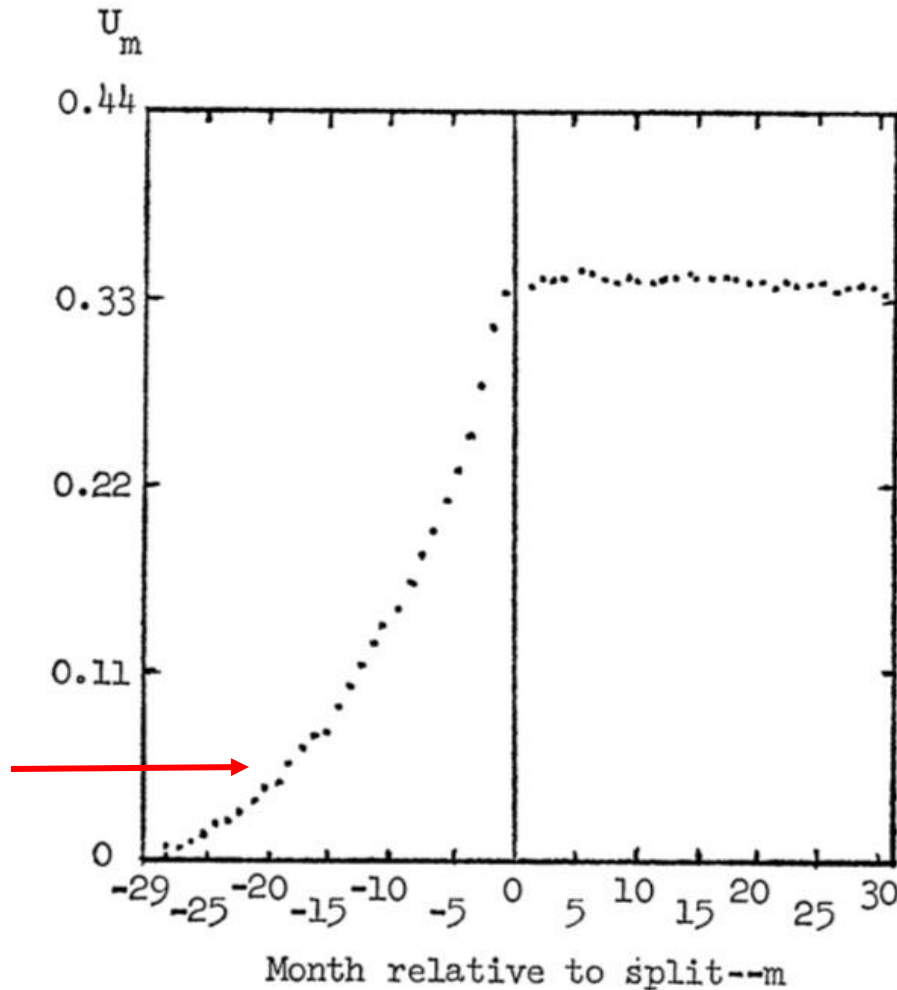
FIGURE 1a
Cumulative average residuals—all splits.

Event Study on Stock Splits by Fama-French-Fischer-Jensen-Roll (1969)

Split is a signal of good profit

Pre-announcement drift can be due to selection bias (only good firms split) or insider trading.
→ inconclusive

No post-announcement drift
→ for weak form

Event Study: Take-over
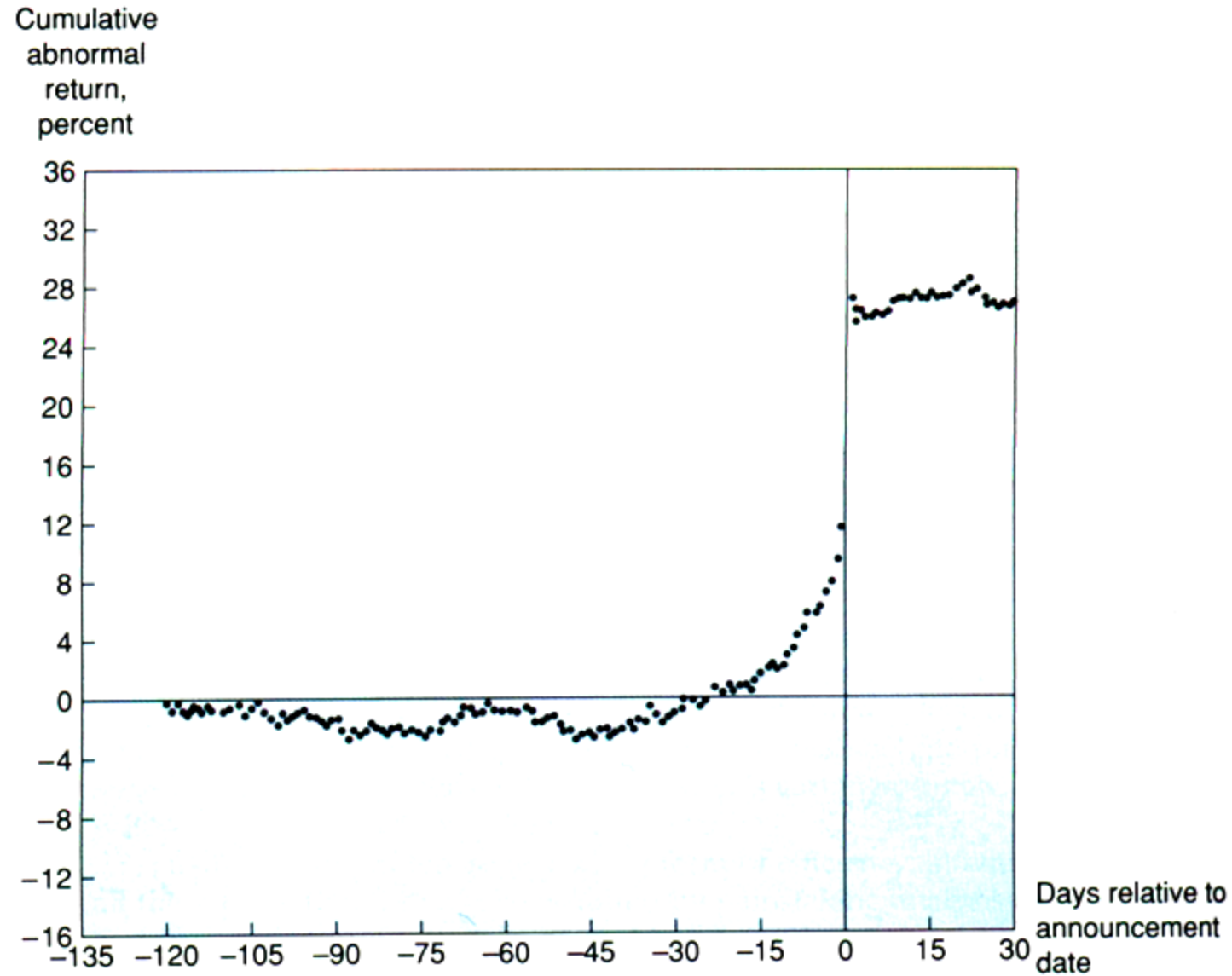
Event Study: Death of CEO

Stock Price and CEO Death
Source: Johnson et al.
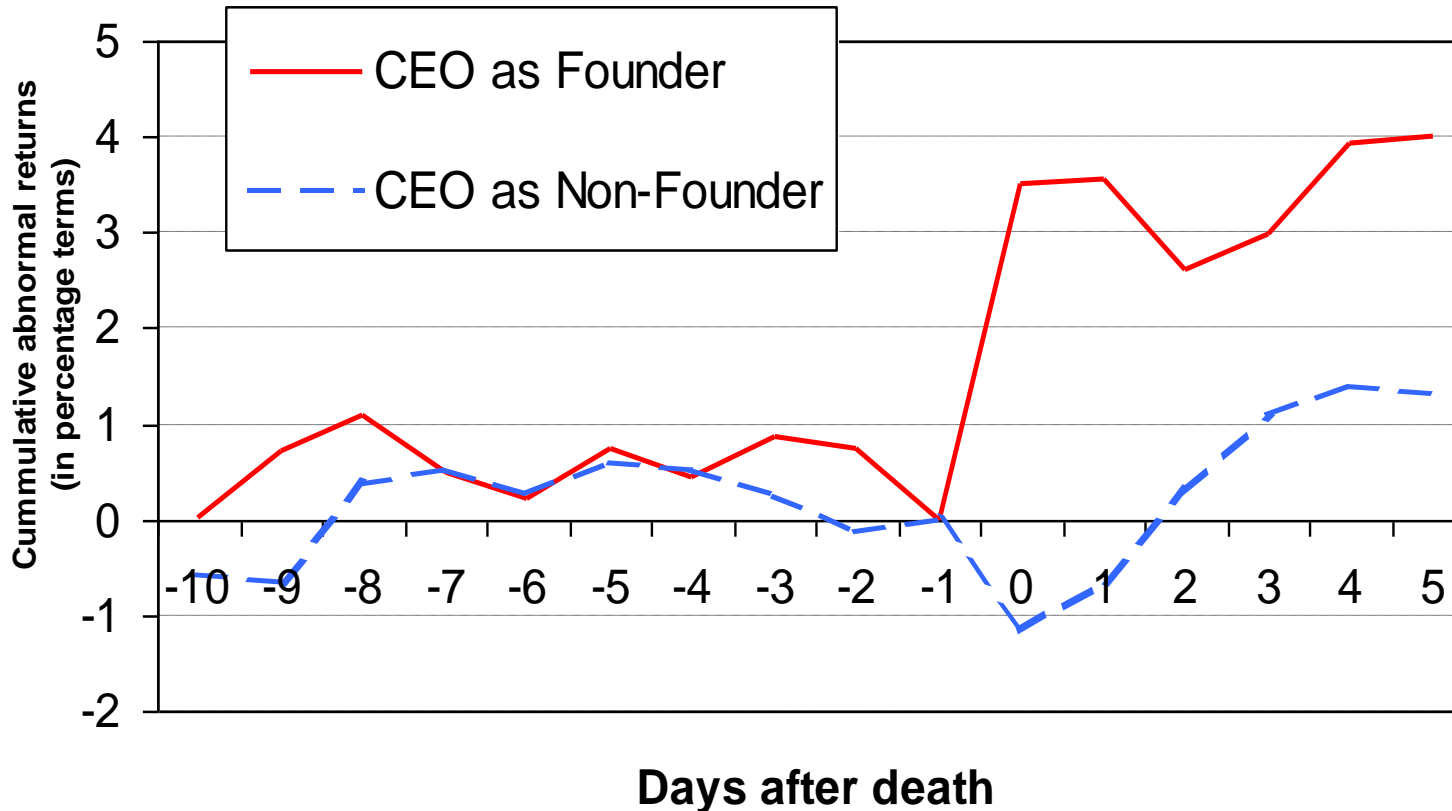
Evidence I: Predictabilities Studies

- **Statistical variables have only low forecasting power, but**
  - But some forecasting power for P/E or B/M
  - Short-run momentum and long-run reversals
- **Calendar specific abnormal returns due to Monday effect, January effect etc.**
- **CAVEAT: Data mining: Find variables with spurious forecasting power if we search enough**

Long-Run Reversals

Figure 1 Cumulative Average Residuals for Winner and Loser Portfolios of 35 Stocks (1–36 months into the test period)
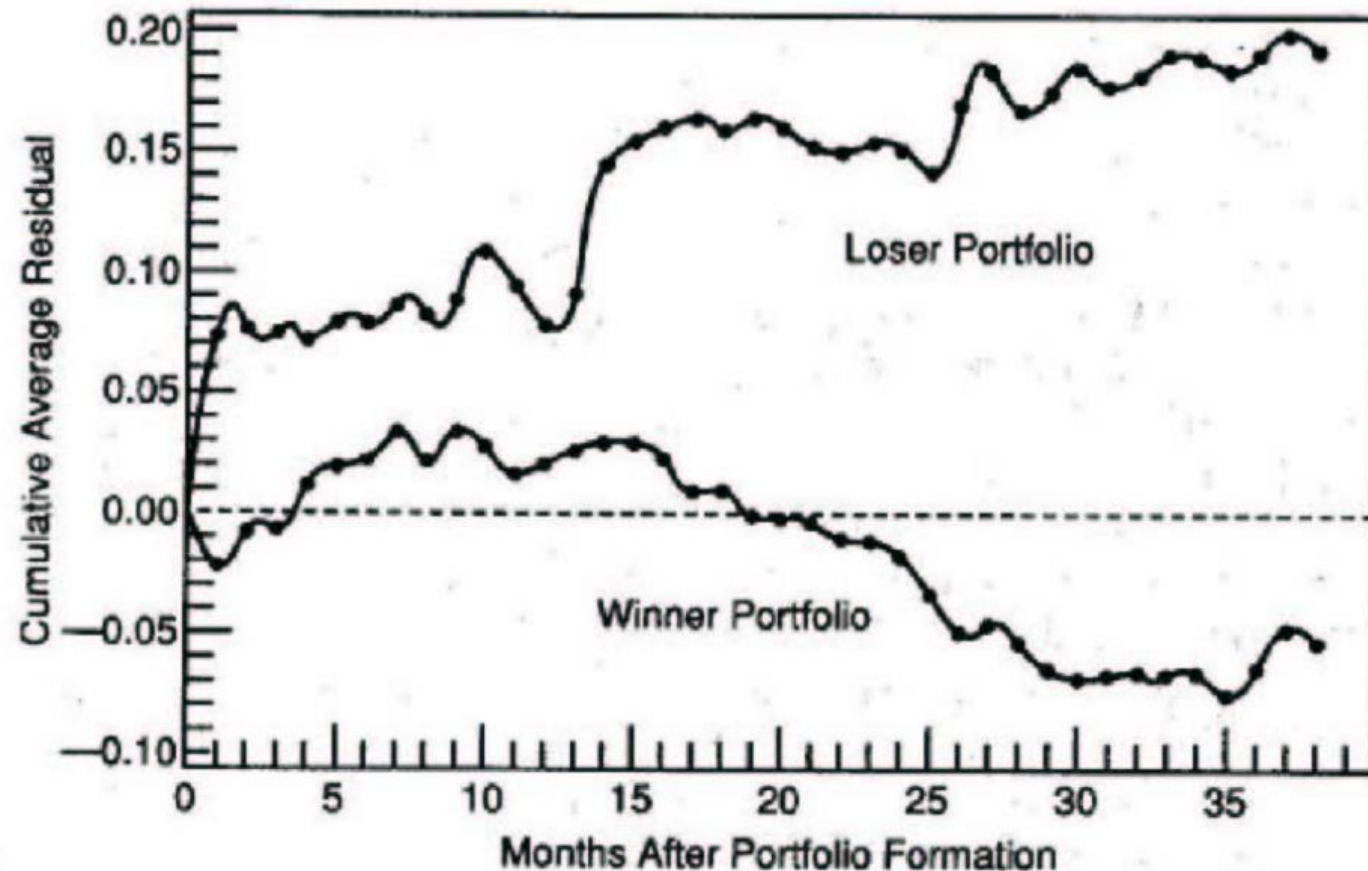
Long-run Reversals

Returns to previous 5 year's winner-loser stocks (market adjusted returns)

Source: Markus K. Brunnermeier (2015), "Lecture 10: Market Efficiency", Finance 501: Asset Pricing, Princeton University

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Short-run Momentum

Momentum
Monthly Difference Between Winner and Loser Portfolios at Announcement Dates

Monthly Difference Between Winner and Loser Portfolios *(y-axis: -1.5% to 1.0%)*

Months Following 6 Month Performance Period *(x-axis: 1 to 35)*
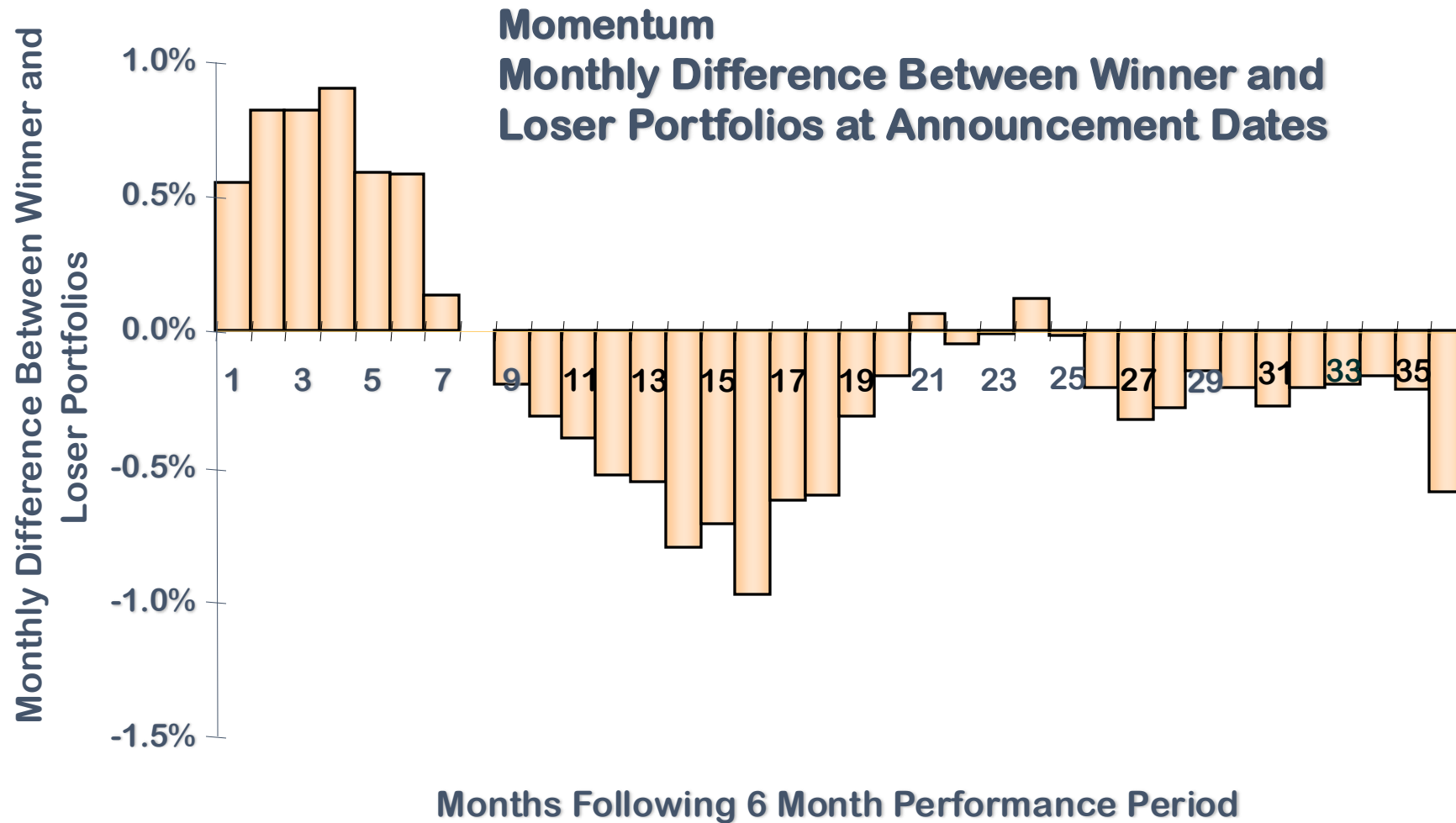
Getting Technical
Barron's March 5, 2003

STANDARD & POOR'S 500

($SPX,D) Dynamic,0:00-24:00

Corrective wedge pattern or the start of a new trading range?

Copyright © 2003 eSignal.
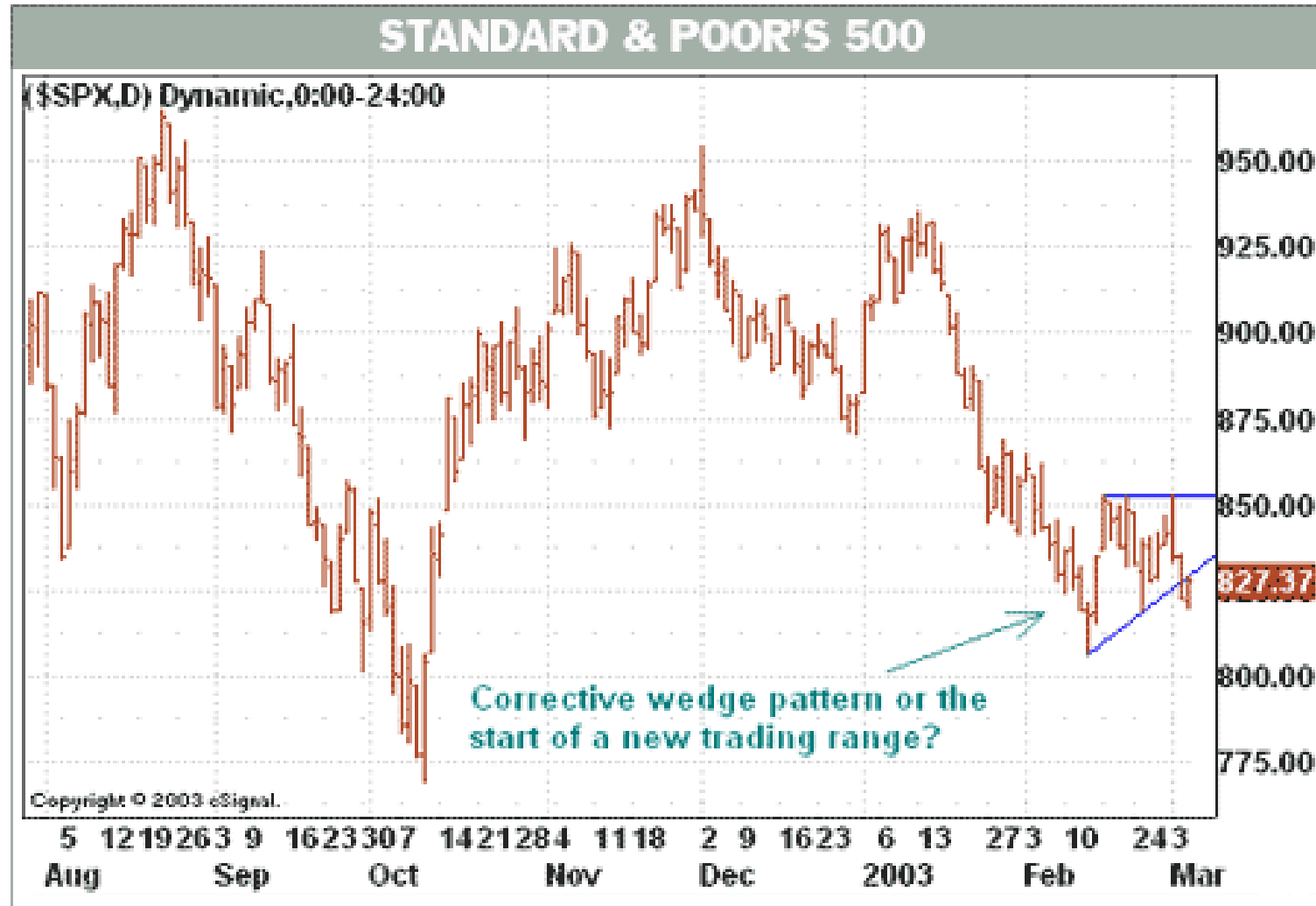
Getting Technical

Back to Buy Low, Sell High   *Barron's March 12, 2003*

Source: Ross et al. (2005), "Corporate Finance", 7th Edition, McGraw–Hill

What Pattern Do You See?

Randomly Selected Numbers
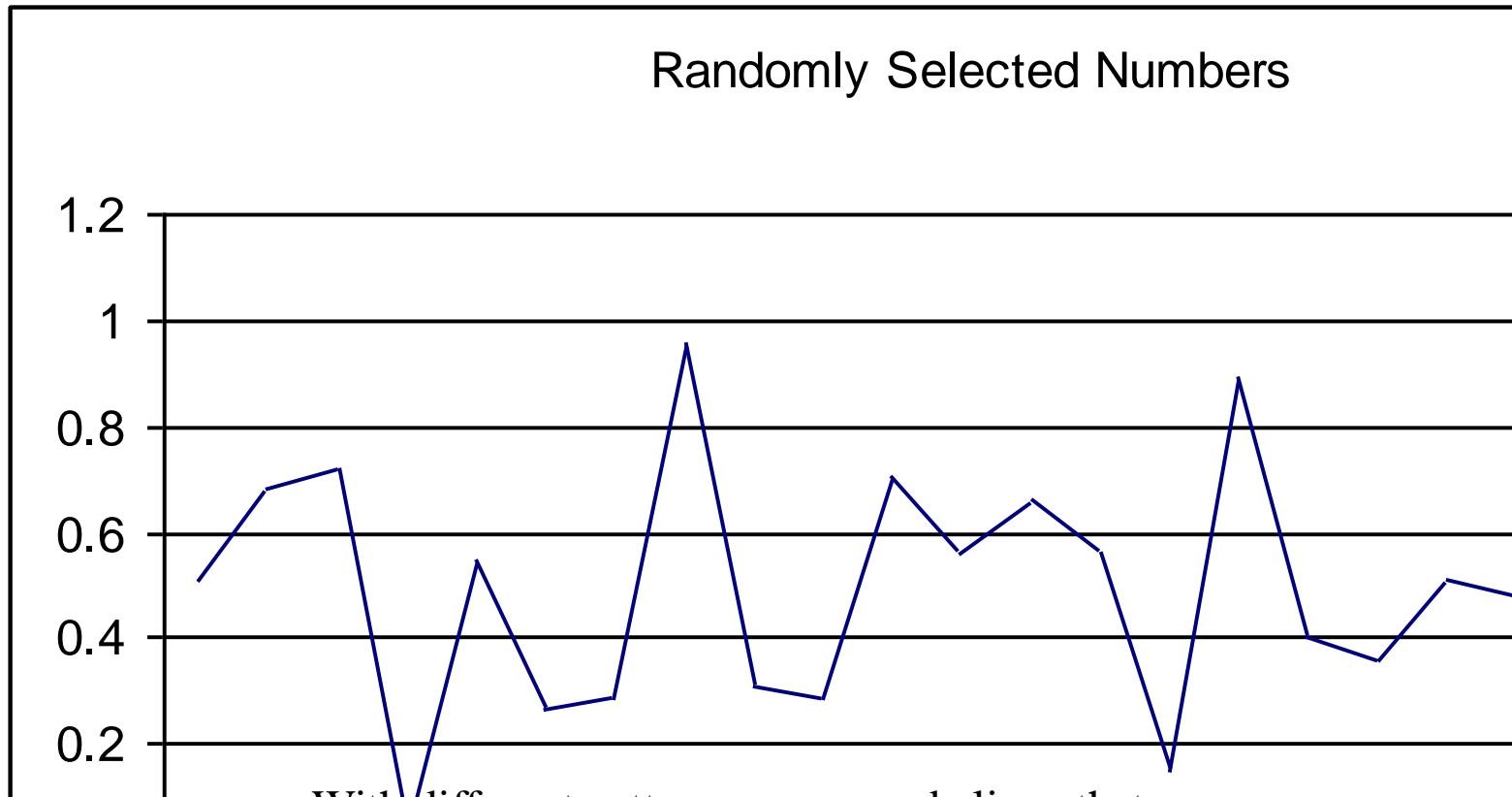
With different patterns, you may believe that you can predict the next value in the series—even though you *know* it is random.

Event Studies: Dividend Omissions

Cumulative Abnormal Returns for Companies Announcing Dividend Omissions

Cumulative abnormal returns (%)

0.146 0.108 0.032 -0.244 -0.72 -0.483 -3.619 -5.015 -5.411 -5.183 -4.898 -4.563 -4.747 -4.685 -4.49

Efficient market response to "bad news"

Days relative to announcement of dividend omission
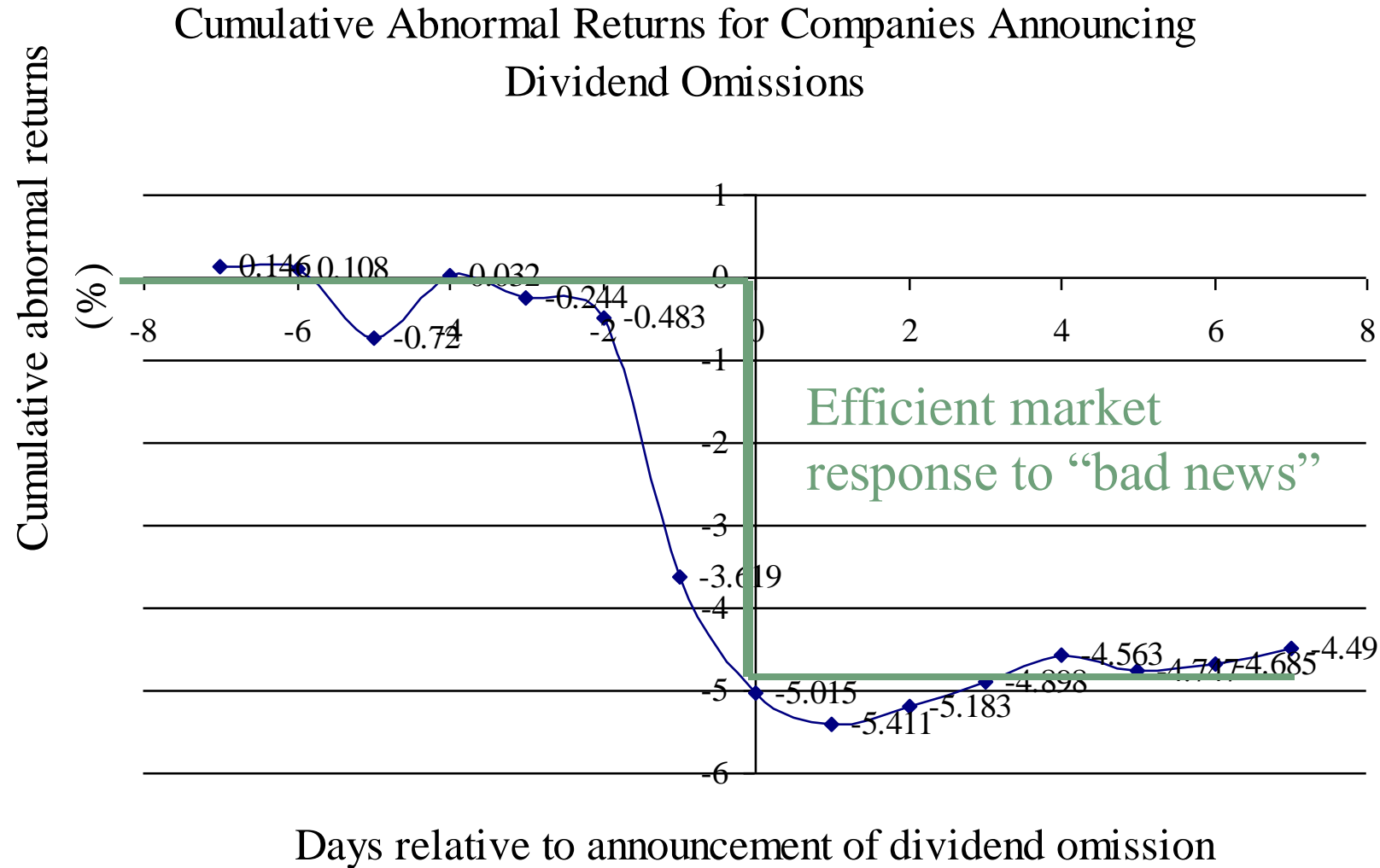
S.H. Szewczyk, G.P. Tsetsekos, and Z. Santout "Do Dividend Omissions Signal Future Earnings or Past Earnings?" *Journal of Investing* (Spring 1997)

The Record of Mutual Funds

Annual Return Performance of Different Types of U.S. Mutual Funds Relative to a Broad-Based Market Index (1963-1998)
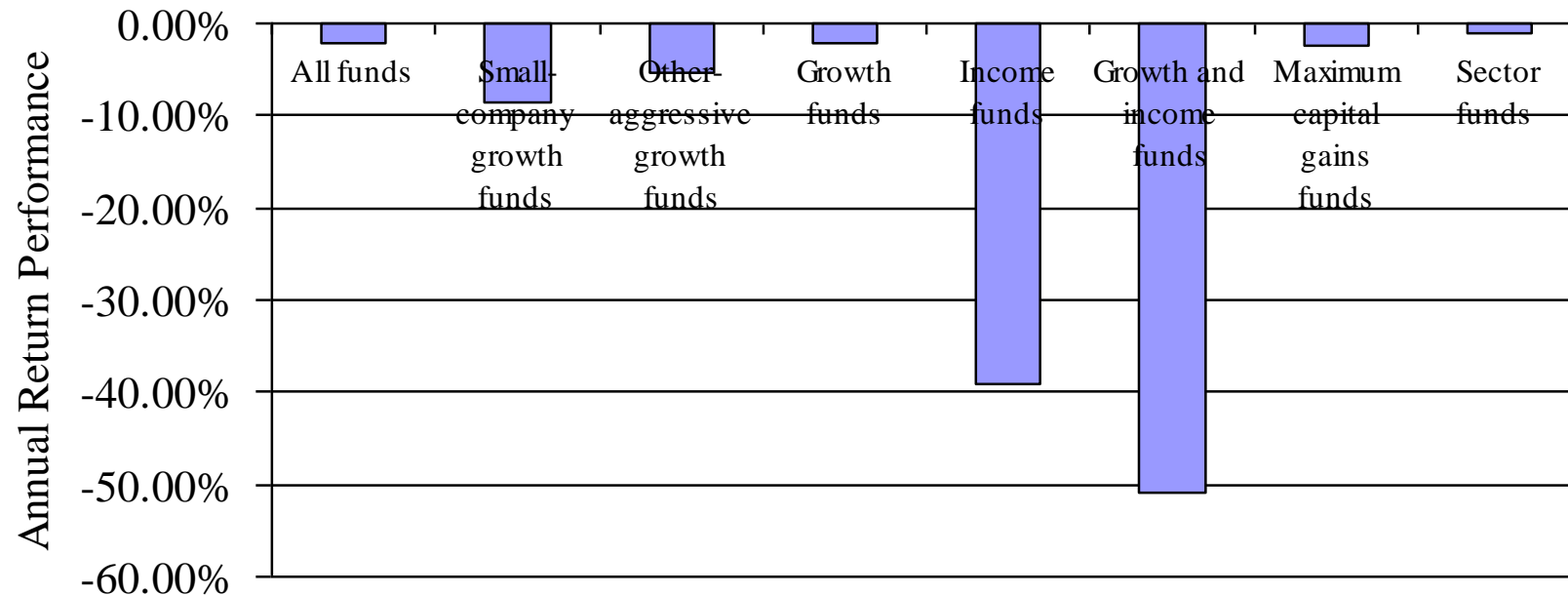
Taken from Lubos Pastor and Robert F. Stambaugh, "Evaluating and Investing in Equity Mutual Funds," unpublished paper, Graduate School of Business, University of Chicago (March 2000).

Weak Form Market Efficiency

- **Security prices reflect all information found in past prices and volume.**

- **If the weak form of market efficiency holds, then technical analysis is of no value.**

- **Often weak-form efficiency is represented as**

- $P_t = P_{t-1}$ **+ Expected return + random error t**

- **Since stock prices only respond to new information, which by definition arrives randomly, stock prices are said to follow a random walk.**

Market Efficiency

- **One group of studies of strong-form market efficiency investigates insider trading.**

- **A number of studies support the view that insider trading is abnormally profitable.**

- **Thus, strong-form efficiency does not seem to be substantiated by the evidence**

Source: Ross et al. (2005), "Corporate Finance", 7th Edition, McGraw–Hill

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Why Doesn't Everybody Believe the EMH?

- **There are optical illusions, mirages, and apparent patterns in charts of stock market returns.**

- **The truth is less interesting.**

- **There is some evidence against market efficiency:**
  - **Seasonality**
  - **Small versus Large stocks**
  - **Value versus growth stocks**

- **The tests of market efficiency are weak.**

Efficient Markets

Inefficient Markets

Behavioral Finance

Python in Google Colab (Python101)

https://colab.research.google.com/drive/1FEG6DnGvwfUbeo4zJ1zTunjMqf2RkCrT

https://tinyurl.com/aintpupython101

Summary

- **Event Studies in Finance**

- **Event Studies for Financial Research**

- **Event Study Methodology**

- **Efficient Market Hypothesis (EMH)**

  - **Efficient Markets**

  - **Inefficient Markets**

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