

Dissertation Proposal

Artem Neklyudov

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Three Essays in Financial Economics:

Securitized Trading, Heterogeneous Dealers on Decentralized Over-the-Counter Markets, and Strategic Information Acquisition with Overlaps

The first essay studies the relationship between customer bid-ask spreads and dealers' interconnectedness with each other on an over-the-counter market with search friction. We develop a search model of decentralized interdealer market and show that dealers with lower search efficiency charge wider bid-ask spreads in equilibrium when customers are not engaged in active shopping for large trading gains. In the model dealers face different liquidity states and have different intrinsic (or "buy and hold") valuations for the asset. Centralized dealers have higher search efficiency than peripheral dealers and are less exposed to their liquidity risk. The model captures the core-peripheral structure of dealer networks documented by recent empirical studies of municipal bonds, asset-backed securities, and collateralized mortgage obligations.

The second essay is an empirical study of securitized trading and dealer networks (co-authored with Burton Hollifield and Chester Spatt). Traditionally, various types of securitized instruments have traded in opaque markets. During May 2011 the Financial Industry Regulatory Authority (FINRA) began to collect transaction data from broker-dealers (without any public dissemination) as an initial step towards increasing transparency and enhancing its understanding of these markets. In this paper we study the structure of the intermediary network and how that influences the nature of bid-ask spreads. We use two alternative methodologies to measure dealer's relative positions in the interdealer network. Some dealers are relatively central in the network and trade with many other dealers, while many others are more peripheral. We propose a way to disentangle dealers' local and global importance and perform empirical analysis using the constructed measures. We also study the determinants of bid-ask spreads, such as the size of the underlying trade and the path by which trade execution and intermediation occur. One focus in our paper is the contrast between registered instruments that are freely tradable and Rule 144a instruments with much more limited disclosures that can only be purchased by sophisticated investors.

The third essay is on strategic information acquisition with overlaps and emerging trading outcomes. The industry of asset management and proprietary trading produces massive amounts of research and useful information. Information production is performed by multiple competing agents that each try to benefit individually from the produced information and conceal their knowledge from the general public. Information gets partially revealed through trading by informed agents, and the degree of such revelation depends on factors that were extensively studied in the past. In this paper we fill in the gaps by generalizing the learning technologies available to agents and allowing for various scenarios of overlaps in agents' information sets. This allows us to study in more detail and enrich existing results about information revelation and informativeness of prices.