Q-GROUP ANNOUNCES WINNERS OF ITS ANNUAL JACK TREYNOR PRIZES

Prizes recognize academic research papers relevant to
investment management and financial markets

New York, November, 2016

The Institute for Quantitative Research in Finance (The Q-Group) is pleased to announce the 2016 winners of its annual Jack Treynor Prizes. The Prize recognizes superior academic working papers with potential applications in the fields of investment management and financial markets. The three 2016 winners (in alphabetical order by paper title) are:

Credit-Implied Volatility

Bryan Kelly, University of Chicago
Gerardo Manzo, University of Chicago
Diogo Palhares, AQR

The pricing of corporate credit can be succinctly understood via the *credit-implied volatility* (CIV) surface. Using a method analogous to the estimation of implied volatility from options contracts, the authors compute credit-implied volatility each month from the firm-by-maturity panel of CDS spreads using the Merton model. The process transforms CDS spreads into units of asset volatility. The CIV surface facilitates direct comparison of credit spreads at different "moneyness" (firm leverage) and time to maturity. The authors use this framework to characterize the behavior of corporate credit markets. They examine moneyness (leverage); they show that of credit spreads dynamics can be parsimoniously described with three clearly interpretable factors; and they examine the cross section of CDS risk premia.

Extrapolation Bias and the Predictability of Stock Returns by Price-Scaled Variables

Stefano Cassella, Krannert School of Management, Purdue University,
Huseyin Gulen, Krannert School of Management, Purdue University

Using survey data on expectations of future stock returns, the authors estimate the degree of extrapolation bias (DOX)—the belief that what has happened recently will continue to happen—in investor expectations. Considerable time-series variation exists in the DOX; evidence shows that it can predicted to a meaningful extent. The authors show that the ability of the dividend-price ratio to predict the equity premium is contingent on the DOX. There is Predictability is when the DOX is high and weak otherwise. These results help answer a critical question: when will an overvalued asset, or even a bubble, experience a correction?

Lazy Prices

Lauren Cohen, Harvard Business School
Christopher Malloy, Harvard Business School
Quoc Nguyen, University of Illinois at Chicago

When making required regulatory financial reports, firms very often repeat the same MD&A texts that they most recently used. Changes in these texts can be quite informative. Using the complete history of regular quarterly and annual filings by U.S. corporations from 1995-2014, the authors show that changes to the language and construction of financial reports have strong implications for firms' future returns: a portfolio that shorts "changers" and buys "non-changers" earns up to 188 basis points per month (over 22% per year) in abnormal returns in the future. Changes in language referring to the executive (CEO and CFO) team, or regarding litigation, are especially informative for future returns.

Copies of these papers are available on the Q Group website at http://www.q-group.org/jack-treynor-prize-winners/.

About Jack Treynor

Jack Treynor was one of the founders of modern quantitative investment management. His pioneering work on how discount rates should depend on risk anticipated and contributed to the development of the Capital Asset Pricing Model. Jack subsequently made numerous other contributions in the areas of performance evaluation, risk management, trading analytics, and inflation dynamics. As the long-time editor of the *Financial Analysts Journal*, Jack substantially raised the quality of discourse among financial analysts. Many of his articles, including some written under the pseudonym Walter Bagehot, have become classics of investment management. Until his death in May 2016, Jack was a Q-Group Research Fellow and a long-time member of Q Group, where his contributions to the program and to the discussions at our meetings were invaluable.

About the Q-Group

The Institute for Quantitative Research in Finance, the "Q-Group" (www.q-group.org) advances the practice of global investment management by connecting investment professionals with rigorous research and ideas at the frontier of the industry. We are a membership organization with over 140 sponsor organizations that represent many of the most important investment sponsors, managers, and consultants in North America and beyond. Our membership includes banks, insurance companies, securities firms, investment consultants, investment advisors, mutual fund managers, state and private pension fund managers, foundations and university endowment funds.

Q-Group's semi-annual conferences are renowned for bringing scholars, investment practitioners, and other interested professionals together to discuss and debate current issues and new ideas at the frontier of investment management. Since our founding in 1966, our programs have explored relevant topics without bias toward any perspective other than the promotion of better investment management practices for the billions of people who depend on responsible financial management for their future security.

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