

# **Corporate Insider Trading on the SIX Swiss Exchange**

## **Bachelor Thesis**

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## **Executive Summary**

### **Problem and Purpose**

Corporate insider trading in terms of management transactions is a current concern in capital markets around the world. Regulations on trades in somebody's firm's equity are under regular revision with the aspiration to maintain the integrity of financial markets and to diminish informational asymmetries in the most efficient way. The impact of corporate insider trades has been investigated in a diversity of literature for a specific number of capital markets, mostly with the focus on the UK and US market. In several capital markets, inter alia in the Swiss stock exchange, transactions by corporate insiders are required to be reported and publicized. This thesis' investigations are conducted in the environment of the SIX Swiss Exchange, where the duty to report corporate insider transactions was implemented in July, 2005 (SIX Exchange Regulation (2005)). The underlying assumption is that corporate insiders possess an informational advantage on the share price behavior of the firm they are related with. A consequence of the privileged access to private information is the achievement of abnormal returns when relying on confidential information. The connection between management transactions and share price behavior was the motivation of a lot of conducted research. This thesis augments this relation and sets corporate insider trading in context with earnings announcements. In the special focus of interest is the time prior to a firm's earnings announcement, when corporate insiders are expected to have an advantage in information concerning the content of the upcoming announcement. It will investigate whether managers earn significantly higher abnormal returns with transactions prior to their firm's earnings announcement than during the rest of the year. If affirmed, it will follow that the informative value of those trades is comparably larger, which might lead to favoring a blackout period, as existing in the London Stock Exchange. A trading constraint in form of blackout periods is supposed to be efficient in order to decrease informational asymmetries in financial markets. It is investigated whether

such a blackout period, which prohibits any trades by corporate insiders previous to earnings announcements, could be reasonable for Switzerland.

## **Methodology**

Investigations are conducted for a sample of 40 firms that are quoted on the SIX Swiss Exchange. The fundament of this thesis refers to the information on management transactions reported to the SIX Swiss Exchange. The thesis relies on a total of 1047 management transactions<sup>1</sup> in equity that have been executed in the time frame from August 2005 until December 2010. Information on earnings announcements are obtained from Bloomberg and the performance of the underlying stocks from Datastream. Two data sets of management transactions are considered. The first data set includes all 1047 observed transactions whereas the second data set only contains those 162 transactions that occurred either two month prior to an annual or semi-annual, or one month prior to a quarterly earnings announcement of the respective firms. The data sets of management transactions in equity are further split up in sell and buy transactions. In order to retain results that allow for the evaluation of the proposed investigations an event study is applied, which is a common methodology to determine abnormal returns in the underlying market. Most existing literature employs the standard event study approach following for instance Campbell, Lo, and Mac Kinlay (1997) or Brown and Warner (1985). Since the standard event study approach has several constraints, it is refrained from applying it and instead an alternative event study methodology in form of a regression framework using dummy variables is applied. (Binder (1998)) The regression based event study allows for some adaptations and does not rely on as many properties as the standard approach does (Lamdin (2001)). The regression framework with dummy variables is first applied on each firm individually and moreover on the whole firm's sample using a panel data set. In the course of the panel regression some further adjustments like cluster robust standard errors are implemented to improve the quality of the estimated model (Petersen (2009)).

## Results

The derived results represent patterns in abnormal returns that to some extent accord with existing literature on the Swiss capital market. As Zingg, Lang, and Wytttenbach (2007) found before, evidence is adduced that buy management transactions in general are anticipated by negative abnormal returns whereas sell transactions follow positive abnormal return behavior. In the time after a transaction has been executed buy transactions result in positive abnormal returns whereas sell transactions conclude in negative ones. This relation is given for the majority of the analyzed firms. However, it is only supported by statistical significance for the minority of firms. For the panel data sample similar patterns in abnormal returns are identified, whereupon abnormal returns are statistically significant for sell transactions by corporate insiders. Therefore it is concluded that corporate insiders earn significant abnormal returns with sell transactions in equity based on informational advantages on future stock price movements. Taking corporate insider trading previous to earnings announcements in account, no evidence for the individual regressions is found that achieved abnormal returns are significant higher in these times. For the basic panel regression no significant relation between abnormal returns and management transaction previous to earnings announcements is found either. This outcome accords with the investigation of Ammann and Kessler (2004), who neither find any pattern in higher statistically significant abnormal returns previous to earnings announcements. Only one adjustment of the model reveals a significant relation. Introducing heteroskedasticity robust standard errors in the cluster of years, gives a significant relation that sell transactions prior to earnings announcement result in higher negative abnormal returns than during the rest of the year. Therefore, when relying on the results of a panel regression with heteroskedasticity robust standard errors in the cluster of years, a blackout period for sell transactions previous to earnings announcements can be considered as effective in terms of decreasing informational asymmetries.

## **Evaluation**

The reported results identify general patterns in abnormal returns achieved through corporate insider trading. The majority of corporate insiders executes buy trades in equity in times of negative abnormal returns and conduct sell trades in times of positive abnormal returns. In the three days after the transactions are executed, significantly abnormal returns can be achieved with sell transaction, while buy transactions are characterized by positive abnormal returns, however no statistical significance. The firm's individual examinations do not show any statistical significance that trades earn higher abnormal returns due to the informational advantage on the content of upcoming earnings announcements. Hence, when relying on the individual regression a blackout period is not reasonable for the Swiss market, since managers do not seem to exploit their knowledge of confidential information. Nevertheless, panel regression results with heteroskedasticity robust standard errors provide significant evidence that sell transactions prior to earnings announcement on average result in higher negative abnormal returns in the three days after trade. Relying on average results obtained from the panel regression, a blackout period on sell management transactions previous to earnings announcement can be considered as effective for the Swiss market in order to decrease asymmetries in information.