

CEOs 'time release of news to boost stock price for self-gain'

Companies could consider alternative vesting schedules to protect shareholders: Study



Corporate news releases draw much attention from the public, as they can significantly affect investors' decisions, and hence, stock prices. Such news releases do not occur mechanically whenever corporate events take place. Instead, they are at the discretion of the chief executive officer.

As such, the possibility arises for CEOs to strategically time news releases for personal gain. A CEO who intends to sell his stocks in a given month may be incentivised to delay news releases that might otherwise have been released earlier until that month and accelerate news releases that might otherwise have been released later to that month to temporarily boost the stock price to benefit his own trading.

After all, the typical base salary of CEOs is only about 20 per cent of their compensation packages, with the performance-based portion, consisting of restricted stock and options, accounting for the majority of such packages.

In a research collaboration between National University of Singapore Business School and the London Business School, the London School of Economics and Sungkyunkwan University, we found that CEOs of US-listed companies strategically time corporate news releases to coincide with months in which their equity vests.

First, we identified the months in which a CEO's stock or options are scheduled to vest. Next, we obtained data on corporate news releases from the Standard & Poor's Capital IQ Key Developments database and classified them as discretionary and non-discretionary.

Discretionary news refers to those news items for which the company has flexibility in deciding on the timing of their disclosure. These include new product launches, major customer wins and special dividend payouts.

Non-discretionary announcements, however, are formally time-tabled regulatory statements such as quarterly earnings reports.

The timing of the release of discretionary news is thus more susceptible to strategic management by CEOs. In our study, we covered nearly 166,000 news releases.

On average, after controlling for CEOs' unvested and vested equity and other determinants of equity sales, we found that CEOs are 23 per cent more likely to sell shares in months in which their equity vests.

After controlling for significant informational releases such as earnings announcements, board meetings and analyst coverage, firms are found to release 3.5 per cent more discretionary news in vesting months compared to non-vesting months and 7 per cent more news in the vesting month compared to the month immediately prior. In contrast, there is no difference in the amount of non-discretionary news releases between vesting and non-vesting months.

Moreover, the higher the value of the equity vesting in a given vesting month, the larger the number of news releases.

Are these news items generally

more positive in the vesting month as well?

We examined the tone of the media coverage immediately after the news releases as well as the tone of the corporate news items themselves. Our analysis suggests that both corporate news and media coverage of such news are more favourable to the firm in vesting months

than non-vesting months, suggesting that CEOs tend to release more favourable discretionary news in vesting months.

We also found that they do this to benefit their trading. We found evidence that CEOs take advantage of the observed run-up in stock prices and stock liquidity. The average interval between a discretionary dis-

closure in a vesting month and the first equity sale by a CEO is five days, while the average interval till the entire vesting amount is sold is about seven days.

What are the implications of these findings?

We found that CEOs seem to delay news releases from the month prior to the vesting month and ac-

celerate news releases that would otherwise belong to the month after the vesting month. Although this strategic behaviour is not illegal in the US, delaying news releases can potentially be detrimental to shareholders who make decisions prior to the vesting months with more limited information. Therefore, companies may consider designing an alternative vesting schedule system to better protect shareholders' interest.

It is also possible that companies led by professional managers rather than owners or founders are more likely to exhibit signs of such strategic behaviour. This could be related to professional managers being more myopic, given their generally shorter employment contracts.

As it is difficult for regulators to influence the way companies time the release of discretionary news, it may be important for boards of di-

rectors to scrutinise CEOs during periods when they have significant equity vesting.

Similarly, it may be important for investors to monitor when companies reveal discretionary news such as new contract wins and special dividends and match that information with the publicly available vesting schedules of CEOs' equity, to assess whether there is personal interest at play – and perhaps discount the news accordingly.

The findings may apply to CEOs of Asian-listed companies as well, given that the breakdown of CEO compensation packages is quite standard around the world.

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