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# GOVERNMENT INVOLVEMENT IN THE CORPORATE GOVERNANCE OF BANKS

Linus Siming\*

*Abstract*—On March 18, 1976, the Swedish parliament voted on a bill that, if approved, would have substantially increased both the scale and scope of government representation on bank boards. Since parliament was hung, the outcome of the vote was decided by a lottery. I exploit this lottery to study the causal effect on shareholder value of government involvement in the corporate governance of banks. I find that the rejection of the bill resulted in positive abnormal returns that persisted in the following days. The results suggest that unsolicited government involvement in the corporate governance of banks is harmful for owners.

*JEL codes:* G14, G34, G38

*Keywords:* Corporate governance, Stakeholders, Banks, Natural experiment

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## I. Introduction

The extent to which it is possible to combine the economic interests of individual firms and society at large is contentious. As has been highlighted in the wake of the recent financial crisis, this is especially true for banks, with the politicians of major parties calling for increased government involvement in their management.<sup>1</sup> The economic consequences of government involvement are, however, poorly understood. I investigate one particular aspect of this problem by asking how the unsolicited government involvement in the governance of banks affects the value of shareholder equity.<sup>2</sup>

While it may seem intuitive that unsolicited government intervention in the corporate governance of banks is costly for the owners, it is far from obvious and surprisingly difficult to prove. On the one hand, the common agency literature argues that the involvement of stakeholders other than shareholders will increase agency costs for firms in general (Jensen, 2001; Tirole, 2001, 2002) and for banks in particular (Laeven, 2013), because the shareholders' objective to maximize equity value differs from the government's objective to maximize society's welfare. By contrast, an influential body of literature suggests that stakeholder representation can lead to policies that,

<sup>1</sup> For example, the leader of Italy's third largest political party calls for a nationalization of Italian banks (Kirchgaessner, 2015).

<sup>2</sup> Equity value is the value of shareholders' claims on the assets and cash flows of the business. For publicly traded firms this is measured as the market value of each share times the number of shares outstanding.

while seemingly deviating from shareholder value maximization, may create shareholder value. In particular, it is argued that stakeholder representation can reduce agency costs and create shareholder value by means of three mechanisms: through mutually beneficial exchanges involving stakeholder-specific information (Becht, Bolton, & Röell, 2003; Magill, Quinzii, & Rochet, 2015; Zingales, 2000), by forcing shifts to investments that are more profitable in the long run (Germain & Lyon-Caen, 2016), and by reducing excessive risk taking (Bolton, Mehran, & Shapiro, 2015).

Furthermore, it is empirically challenging to study the relation between government involvement in the governance of banks and equity value due to the endogenous relation between governance structure and equity value (Adams, Hermalin, & Weisbach, 2010; Wintoki, Linck, & Netter, 2012). If government representation on the boards of banks is mandatory, there is no meaningful variation to study and, if not, we cannot typically know what causes the results. For instance, if we find, in a cross section, that banks with government representatives have lower (higher) equity value than banks without any government representative, is this, then, because of the presence of government representatives or is it simply because worse-run (better-run) banks appoint them to their boards?

To overcome this challenge, I utilize a natural experiment. The Swedish general election in 1973 resulted in a hung parliament with the left- and right-wing blocs winning 175 seats each. As a result of the tied outcome, 152 parliamentary votes from 1973 to 1976 were decided by a lottery wherein a member of parliament was asked to draw a ticket from a ballot containing a yes and a no ticket. Such a lottery occurred on March 18, 1976, when parliament voted on proposals from a legislative bill from the ruling left-wing bloc that, if approved, would have substantially increased both the scale and scope of the government's involvement in the corporate governance of banks. In short, the bill included proposals to let representatives appointed by the government have the right to

participate in deliberations and decisions not only in the central and local boards of a bank but also in any executive body directly subordinate to a board. Such executive bodies include the management team of the chief executive officer (CEO) and credit committees. In addition, each municipality council would be required to appoint two board members to the board of every local bank office in the municipality. The government motivated the bill on the grounds that society needs to directly participate in and decide over banks' decisions on whom to provide financing and other matters of societal importance. The right-wing bloc strongly opposed these proposals, arguing that the public sector should not intervene in the decision making process of private businesses. Thus, the vote had to be decided by lottery. Since the winning lottery ticket for each contested item was no, these proposals were rejected.

I use the outcome of this lottery and the movement in bank stock prices on the Stockholm Stock Exchange (SSE) around the lottery to study the impact of stakeholder legislation on shareholder value. Employing a variety of standard event-study methods, I find that the rejection of the proposals led to an abnormal positive market return. The economic effect is sizable, with immediate abnormal returns of 0.489 to 0.655 percentage points. Depending on the length of the event windows, the cumulative abnormal returns around the lottery range from 0.684 to 1.128 percentage points.

Because of the key role that banks play in the modern economy and because they are more complex and have more stakeholders than most other firms (Mehran, Morrison, & Shapiro, 2012), there is a vast empirical literature on the corporate governance of banks. However, as noted by de Haan and Vlahu (2016) in their survey spanning the literature from 1980 to 2015, there is no consensus on the influence of different corporate governance mechanisms on bank performance. Furthermore, de Haan and Vlahu (2016) find that most studies do not carefully examine the

potential problems associated with reverse causality. The main contribution of this paper therefore lies in establishing a causal relationship between stakeholder representation in the form of government-appointed directors and shareholder value in banks. Unlike almost every other event study, the event that I study is truly exogenous and the estimates are therefore causal, conditional on there being no other unexpected events that influenced stock market prices and accepting the standard models that I use. Since I find positive abnormal returns associated with the rejection of the proposals to substantially increase both the scale and scope of government involvement in the governance of publicly listed banks, the results may be viewed as empirical evidence in favor of those who argue that unsolicited government board representation is harmful for owners of banks.

It is, however, important to bear in mind two limitations of the study when considering this conclusion. First, since banks differ from other firms with respect to both the business that they operate and their corporate governance, it is possible that the results could look different for other industries. Second, this paper is focused on the agency conflicts of allocating decision power to stakeholders other than owners from the viewpoint of the latter. The relevant measure is therefore equity value, not enterprise value. It is possible that the effects on enterprise value, when the interests of debt holders—including depositors—are also considered, could be different.

I conduct a range of tests to gauge the robustness of the main result. First, I investigate how the returns of the banking sector respond to important milestones in the build-up to the voting impasse. On January 15, it was announced that the bill had a 50% support level among members of parliament and, on February 11, it was announced that the remaining 50% of parliament members would vote no to the main parts of the bill, which meant that the fate of the bill would have to be decided by lottery. Thus, if shareholders see government involvement in the governance of publicly listed banks as value enhancing (destructive), then the abnormal returns should be positive

(negative) on January 15 and negative (positive) on February 11. I find that the reactions were strongly negative to the announcement on January 15 and strongly positive to the announcement on February 11. Though these results do not derive from a lottery, they provide support that shareholders see government involvement in the governance of publicly listed banks as value destructive.

Second, I study the returns of all non-banking firms listed on the SSE, since it may help us in asserting that the returns I obtain for the banking sector are truly a reaction to the lottery. The proposal was also expected to affect the broader business community. Some have argued that it would limit the free credit market and thus reduce possibilities to allocate credit efficiently. Thus, borrowers would be unable to obtain credit for profitable investments and the shareholders of such firms should welcome the rejection of the proposal as positive news. Others have argued that the government representatives could potentially be needed to force banks to develop currency forward markets. Such markets were much needed by exporting firms to hedge floating exchange rates, but banks had been hesitant to develop them because of the high costs involved. Thus, the shareholders of the companies in the biggest exporting business sectors—forest and agriculture and industrials—may not have seen the rejection of the bill as univocally positive. I find that the returns are the highest (lowest) for those sectors that stood the most (least) to lose if the proposals had passed. These results suggest that the returns that I observe across the stocks listed on the SSE on the event day are indeed a reaction to the lottery.

Third, to ensure that no other contemporaneous event could have given rise to the same reactions that I observe, I also examine potentially confounding events. The major events in international financial markets during the month of March 1976 were the problems facing the ‘snake in the tunnel,’ the European Community’s mechanism for managing fluctuations of their currencies

against the U.S. dollar (USD). Inflation and balance of payment deficits among the member countries put pressure on the currency parities. Due to the weakness of its currency, France chose to leave the mechanism on March 15. Since Choi, Elyasiani, and Kopecky (1992) find that exchange rate innovations can have an impact on the return of bank stocks, I investigate if the results are driven by exchange rate movements by augmenting the event day studies with daily exchange rates between the Swedish krona (SEK) and the main currencies at the time. I find that the abnormal returns for the banking sector following the parliamentary lottery cannot be explained away by fluctuations in the exchange rate of the SEK vis-à-vis these major currencies.

The remainder of the paper is organized as follows. I describe the institutional background in Section II. I develop empirical predictions in Section III. Section IV presents the main analysis. Results from the robustness tests are discussed in Section V. I conclude the paper in Section VI. This article is accompanied by an Online Appendix that contains translations from Swedish to English of the main sources cited in the text.

## **II. Institutional Background**

### *A. The Lottery Parliament*

In 1971, the Swedish bicameral parliament was replaced with a unicameral parliament with 350 seats.<sup>3</sup> In the general election of 1973, the two parties on the left, the Social Democrats (*Socialdemokraterna*) and the Communist Left Party (*Vänsterpartiet Kommunisterna*) jointly won

<sup>3</sup> The number of parliament members was reduced by one to 349 for the elections in 1976.



175 seats and the same number of seats was won by the three parties on the right, that is, the Moderate Party (*Moderaterna*), the Centre Party (*Centerpartiet*), and the People's Party (*Folkpartiet*). Thanks to the requirement that a majority was needed in parliament to force a resignation, the incumbent Social Democratic government, led by Prime Minister Olof Palme, retained power with the support of the Communist Left Party (Hermansson, 2010).

The views of private business were greatly polarized between the two main political groupings (von Sydow, 2005). As a consequence of these ideological differences, the 1973–1976 parliament has become known as the ‘lottery parliament,’ since 152 decisions—7% of all decisions taken—were decided by a lottery after the initial vote ended in a draw.

#### *B. Legislation Bill on Public Representation in Banks*

Since 1971, the government had the right to appoint up to three members—extended to five in 1972 for the largest banks—to the central non-executive boards of banks.<sup>4</sup> The underlying reason for the government's right to appoint board members, even though it was not a shareholder, was to “ensure that society can directly participate and decide over the banks’ decisions on whom to provide financing to, individual matters of credit, and all other matters of importance from the view point of society” (Government legislation bill 1976/76:53, p. 25).<sup>5</sup> However, the government soon

<sup>4</sup> By law, these boards had to have a total of five to 23 members.

<sup>5</sup> All the parliamentary documents mentioned (bills, protocols, motions) are available through the website of the Library of the Swedish Parliament, at <https://www.riksdagen.se/sv/riksdagsbiblioteket/>.

came to realize that a substantial amount of the credit granted by the banks was approved by bodies where government representatives were not present (Government legislation bill 1976/76:53, p. 28).<sup>6</sup> Decentralization of the banks' operating strategy and delegation of power within the banks had led to many decisions being made by bodies other than the central non-executive board. For example, it was estimated that 90% of the number of loans, which corresponds to 50% of the amount of credit given, were approved by the non-executive boards of local bank offices, executive boards, credit review committees, and other management groups (*Ekonomisk Revy*, 1975a). The government thus concluded that their representatives had not sufficiently managed to influence the decisions within banks.

Consequently, the government felt that there was a need to further strengthen society's influence over the decisions made by banks. After first securing internal support at the Social Democratic party congress in early October, on November 27, 1975, the government put forward legislation

English translations of all cited parliamentary documents as well as all cited news items and articles from *Dagens Nyheter*, *Ekonomisk Revy*, and *Veckans Affärer* are available in the Online Appendix.

<sup>6</sup> For example, on June 5, 1975, Ingvar Svanberg, a socialist member of Parliament, was outraged that the management team of the bank for which he acted as the government representative, *Skandinaviska Enskilda Banken*, had canceled all credit to the industrial laundry machine producer *Coronaverken* without consulting the board of directors. Since the management team's decision was compliant with all regulations and the established praxis, Svanberg called for an "imminent change in praxis" (*Dagens Nyheter*, 1975).

bill 1975/76:53, which proposed to extend the system of government representatives in banks in three ways.

First, public representatives should have the right to participate in the deliberations and decisions of any executive body directly subordinate to any local, regional, or central non-executive board. Such executive bodies include the CEO's management team, credit committees, management committees, and ad hoc working groups. Second, each municipality council would be required to appoint two non-executive board members to the non-executive boards of every local bank office in the municipality. In total, the Minister of Finance estimated that this proposal would lead to a more than hundredfold increase in the total number of public representatives, from 15 to 1700–1800 individuals (Huss, 1975, p. 514). Third, the bill proposed that the representative on the central non-executive board should be allowed to also participate in the meetings of the regional non-executive boards.

The Communist Left Party announced its support for all three elements of the bill on January 15, 1976 (Parliament motion 1975/76:330), thus bringing the support for the bill to 50% of all parliament members. On February 11, representatives for the three right-wing parties jointly motioned to reject the two main parts of the bill (Parliament motions 1975/76:2170, 1975/76:2171, and 1975/76:2172): the right for public representatives to participate in the meetings of executive bodies and the requirement that each municipality council appoint two non-executive board members to the non-executive boards of every local bank office in the municipality. The three opposition parties disagreed with regard to the proposal to allow the public representative on the central non-executive board to also participate in the meeting of the regional non-executive boards. While the Moderate Party and the People's Party opposed the proposal, the Centre Party was in favor of it. Thus, on February 11, it became clear that 50% of the members of parliament would

vote against the two main parts of the bill and that their fate would have to be decided through a lottery.

As predicted, the mandatory votes on the two contested proposals on March 18 each ended in a draw, with 147 votes in favor and 147 votes against (Parliament protocol 1975/76:85).<sup>7</sup> Following the protocol in the event of equal votes, the deputy speaker of the house asked a member of parliament to come forward and draw a lottery ticket from a ballot containing one yes and one no vote. Since the outcome for both draws was no, the proposals were rejected. Thus, there would be no automatic hundredfold increase in the number of public representatives and no public representative would have the right to participate in the deliberations or decisions taken by any executive body within a bank.

### **III. Theoretical Background and Testable Predictions**

The banks themselves acknowledged that the potential effects of increased public control rights could be both positive and negative with respect to future profits and thereby shareholder value. An editorial in *Ekonomisk Revy* (the journal of the Swedish Bankers' Association) summarized the potential impact of the contested proposals:

<sup>7</sup> The total number of votes cast reflects the praxis of pairing, when two members of parliament from opposing political parties may agree to abstain when one member is unable to vote. Pairing is conducted by members designated for that purpose by each party and is applied whenever one bloc has lower attendance than the other.

There are reasons to not only view the bodeful invasion of public board representatives as a complicating factor in performing ones' tasks. On the one hand lies a clear risk that the proposed participation of the government appointed representatives in the internal work will lead to bureaucratization and unwieldiness, which is in sharp contrast with the efforts made by the banks to shorten decisions paths and speed up decision processes. On the other hand, the public representatives can surely in many cases bring new and valuable knowledge to the bank. (Törnqvist, 1975, p. 429)

These perspectives capture some of the main elements of the two diametrically opposed academic views on the potential effects on profitability from allocating decision power to stakeholders other than owner: the stakeholder representation viewpoint versus the common agency viewpoint.

#### *A. Stakeholder Representation Viewpoint*

On the one side are advocates of stakeholder representation, who argue that policies that seemingly deviate from shareholder value maximization may actually lead to shareholders being better off. For example, the government argued that the proposed legislation could spur more lending to building homes. This, in turn, would be good for banks in the long run, since more houses would lead to an improved society, which in turn would lead to better business conditions for the banks in terms of more future financing opportunities (Huss, 1975, p. 509). Theoretical support for these types of arguments is given by Germain and Lyon-Caen (2016), who show that stakeholder representation (i.e., employees in their case) can shift investments from short-term to

long-term investments and that such a switch can create shareholder value in large, mature firms, where shareholders have a relatively long time horizon.

Furthermore, one bank CEO highlighted that government representatives can be a valuable asset thanks to their different experiences and personal connections: “Banks need on their boards knowledgeable advisors from different parts of society. The public representatives there fill a gap; they can be of great benefit and help an increased mutual understanding of economic and socio-economic problems” (Huss, 1975, comments by Lars-Erik Thunholm, p. 513). More generally, government representatives have unique information on the political processes and may know how to best interact with policy makers and regulators and thereby how to translate government policy into business implications. Possibly, they could help banks stay well informed of any pending legislation so that the banks can develop compliance strategies well in advance. This notion that stakeholder representation can lower agency costs through the mutual exchange of stakeholder-specific information between shareholders and other stakeholders forms the basis of the works of Zingales (2000), Becht, Bolton, and Röell (2003), and Magill, Quinzii, and Rochet (2015). These studies show, in different settings, that better cooperation between stakeholders can lead to better firm performance and thereby higher shareholder value.

Politicians and practitioners agreed that there were no serious risks facing the Swedish banking system at the time (Huss, 1975, comments by Ingvar Svanberg, p. 514, and Sten Walberg, pp. 517–518). Nevertheless, government representatives can potentially reduce both excessively high levels of risk and the consequences of excessively high risk taking through two mechanisms. First, they may signal an implicit guarantee that the government will provide financial assistance in the form of a bail-out, if needed. Second, they may help in achieving an optimal level of risk taking from the viewpoint of shareholders. Bolton, Mehran, and Shapiro (2015) show that shareholders may

not have the incentive to reduce excessively high risk taking, even if it is in their own interest, due to commitment problems. It is possible that the forced participation of other stakeholders on bank boards, such as public representatives, can alleviate this commitment problem.

### *B. Common Agency Viewpoint*

By contrast, a significant body of literature argues that stakeholder representation increases agency costs and thereby lowers shareholder value. A situation where multiple stakeholders as board members act as principals to one common agent, the CEO, gives rise to the common agency problem (Bernheim & Whinston, 1986). In particular, concerns were raised that the empowered government representatives could lead to a replacement of business criteria by political viewpoints when evaluating projects. One bank CEO explained how his bank is often asked to finance projects that are not economically viable: “It is better not to build a factory in a village if it has to shut down two or three years later and then stand as a monument of business failure and thereby also a failure for society” (Huss, 1975, comment by Erik Ehn, p. 512). Thus, there was a fear that the proposal would lead to the financing of economically non-viable projects that could crowd out financing for economically viable projects. Jensen (2001) and Tirole (2001) both argue that the key problem with stakeholder representation lies in establishing the costs and benefits of the different stakeholders represented: the shareholders’ objective is to maximize equity value and the public representative’s objective is to maximize society’s welfare. With particular reference to banks, Laeven (2013) argues that, when the state acquires control rights in banks, power is placed in the hands of bureaucrats who almost certainly do not have the same interests as other shareholders or the general public. Instead, the goals of bureaucrats are likely dictated by their political interests, including catering to special interest groups, which will harm profitability. One bank CEO referred

to the Gospel of Luke in the New Testament when arguing that it would be difficult for him as a CEO to serve two principals “No servant can serve two masters: for either he will hate the one, and love the other; or else he will hold to the one, and despise the other” (Huss, 1975, comment by Erik Ehn, p. 509). This age-old situation has been formally analyzed by Tirole (2002), who finds that CEOs who answer to many principals may develop capabilities as a compromise maker rather than as a shaper of the firm with a clear objective. Subsequently, the firm’s objectives become unfocused.

In addition, there were worries that the sheer number of public representatives would slow down the decision making process and make it inefficient (Törnqvist, 1975; Olson, 1975; *Veckans Affärer*, 1975a, 1975b). Decisions could be stalled if the 1700–1800 politicians are not able to show up at executive meetings on short notice (*Ekonomisk Revy*, 1975b). The financial literacy of these thousands of representatives was also a matter of concern. Hau and Thum (2009) find that almost all politically appointed board members on bank boards in Germany lack financial experience. Though I cannot know which politicians would have been appointed as public representatives had the proposal passed, there was fear that they would indeed lack professional knowledge about the functioning of a bank. The participation of such individuals in decision making could lead to decreased efficiency in daily work (Huss, 1975, comment by Lars Erik Thunholm, p. 513).

### C. *Testable Predictions*

All in all, the two opposing strands of literature can be summarized in the following two hypotheses.



*Stakeholder hypothesis:* Increased government involvement will decrease agency costs, which will lead to increased profits and thereby have a positive impact on shareholder value.

*Common agency hypothesis:* Increased government involvement will increase agency costs, which will lead to decreased profits and thereby have a negative impact on shareholder value.

The resulting testable predictions of the stakeholder (common agency) hypothesis is that the rejection of the proposed legislation to expand the scale and powers of state representatives should have a negative (positive) impact on the equity value of banks.

#### **IV. Equity Value Effects**

##### *A. Data and Choice of Estimation Models*

To measure if government representation on bank boards has a positive or negative effect for shareholders, I use three event study models: a constant-mean-return model, and two versions of the market model, which are all explained in detail by Campbell, Lo, and MacKinlay (1997). Since there is no database of returns on the SSE during the 1970s, all stock market data was hand-collected. Daily data on the five sector indexes and the main index, the Affärsvärldens General Index (*Affärsvärldens generalindex*, hereafter AFGX), was photographed and manually extracted from microfilmed copies of the Swedish daily broadsheet *Svenska Dagbladet* (*SvD*), held at the

University Library in Lund and the British Library in London.<sup>8</sup> In the main analysis, I use only data for the banking sector and the main index. In subsequent robustness tests, I analyze the returns of the other four sectors. To ensure that the information was entered correctly and that there were no typos in the original newspapers, a number of quality controls were conducted, which are detailed in Appendix 1. All indexes are value-weighted and all the returns are computed using differences in the natural logarithm of the daily closing quotes of each index.

The lottery took place around 3 PM on Thursday, March 18, which was 30 minutes after the end of the day's trading on the SSE. I thus use the following trading day, Friday, March 19, as the event day. Because the proposed legislation affects all listed banks simultaneously, I conveniently account for the resulting contemporaneous cross-correlation of different banks by estimating abnormal returns (*AR*) using the return of the entire banking sector rather than estimating the model firm by firm in a seemingly unrelated regression system. That is to say, the residuals are not correlated across securities since I only have one return (the return of the banking sector) and I therefore do not need to use corrections for cross-sectional independence in the statistical tests.

Event study methods do generally not include the event period itself in the estimation period to prevent the event from influencing the normal parameter estimates. These methods need at least

<sup>8</sup> The banking sector is composed of 9 banks. The forest and agriculture sector consists of 10 firms. The industrial sector consists of 23 firms. The shipping, trade, and investment sector consists of 28 firms. The manufacturing sector consists of 35 firms. In terms of market capitalization, the banking sector constitutes about 10% of the SSE market capitalization.

two observations in the event window to enable calculation of a daily standard error. Since I am investigating the returns of one sector stemming from one event there is however only one observation on the event day. Thus, to be able to estimate  $AR$  on the event day I use in Section B a constant-mean-return model and a market model where the event day itself is included in the estimation period. These two models are however not appropriate for the study of abnormal returns before and after the event day because the estimators for the parameters of the normal return on the days around the event could be influenced by the event-day return. In such a situation both the normal returns and the abnormal returns would capture the event impact. Instead, to study if the outcome of the lottery was anticipated in the market before the event day, and to see if any event day effects persist in the days following the event, I will in Section C use a market model where the normal return measures are obtained in a pre-event estimation period.

### *B. Equity Value Effects on the Event Day*

The first approach simply computes the mean-adjusted return, estimated as the parameter  $AR$  in the following time-series regression in event time, where day 0 is the event day, March 19, 1976:

$$R_t = \alpha + ARd_t + e_t, \quad t = -252, \dots, 0, \quad (1)$$

where  $R_t$  is the daily value-weighted return for the banking sector and  $d_t$  is a dummy variable that takes a value of one on the event day, and zero otherwise. The model is estimated for a window from 252 trading days prior to the event day. My second estimation approach uses the following model, where I allow for the returns to depend on the return on the market portfolio:

$$R_t = \alpha + ARd_t + \beta I_t + e_t, \quad t = -252, \dots, 0, \quad (2)$$

with  $R_t$  and  $d_t$  as in regression (1) and  $I_t$  as the daily return of the AFGX, the Swedish value-weighted market index, measured through the natural logarithm. The difference between regressions (1) and (2) lies in that the former assumes that the mean return of the banking sector is constant through time, while the latter assumes a stable linear relation between the market return and the banking sector return. Regression (2) represents a potential improvement over regression (1) because it removes the portion of the return that is related to the variation in the market's return, which can lead to an increased ability to correctly detect the effects of the event one is investigating (Campbell, Lo, & MacKinley, 1997). In both regressions, I employ White heteroscedasticity-consistent standard errors to guard against potential serial correlation in the time series.

The results from these two models are presented in Table 1. Column (1) (column (2)) displays the results of regression (1) (regression (2)). Both models yield positive *AR* values that are statistically significant at the 1% level. The return is 0.655 percentage points for the constant-mean-return model and 0.489 percentage points for the market model.

To convert the event day abnormal returns into monetary gains one can use the banking sector's market capitalization on the eve of the event day. Hence, to see the total shareholder wealth created I multiply the event day returns with the SEK 3.2 billion market capitalization of the banking sector on March 18. The increase in shareholder wealth is SEK 20.4 million with the coefficients of the constant-mean-return model and SEK 15.6 million with the coefficients of the market model. These monetary gains represent the direct impact of the lottery outcome on shareholder wealth. In Section D I will use the abnormal returns and their cumulative analogs to assess the total implied value of the government's proposal.

### C. *Equity Value Effects around the Event Day*

The daily  $AR$  values can be aggregated to cumulative abnormal returns ( $CAR$ ) to ascertain the effects over longer periods. I start by estimating normal (i.e., expected) returns by means of a one-factor market model for the banking sector:

$$R_t = \alpha + \beta I_t + e_t, \quad t = -252, \dots, -15, \quad (3)$$

where  $R_t$ , as before, is the daily value-weighted return of the banking sector on day  $t$  and  $I_t$  is the daily return of AFGX. One benefit of model (3) compared to models (1) and (2) is that it enables us to use a pre-event estimation period for the normal model parameters. I estimate the model for a window from March 15, 1975 (252 trading days prior to the event day) to February 27 (15 trading days prior to the event day). Day 0 is the event day, March 19, 1976. I obtain daily abnormal returns,  $AR_t$ , as the difference  $e_t$  between the raw return and the return estimated from the market model.

$$AR_t = R_t - (\hat{\alpha} + \hat{\beta}I_t). \quad (4)$$

I derive the  $CAR$  values for the banking sector following the event date by aggregating  $AR_t$  values over several different symmetric and asymmetric event windows from two to 13 trading days around the event date. Two days is the minimum period for which I can obtain a standard error for the  $CAR$  value.

Table 2 presents the  $CAR$  values in the trading days prior to the event day. The asymmetric event windows start between two and six days before the event day and end one day before the event day:

$$CAR(-n, -1) = \sum_{t=-n}^{-1} AR_t. \quad (5)$$

I note that the *CARs* are all small and insignificant, which is evidence that the market is neither anticipating a positive nor a negative outcome of the parliamentary lottery draw. Table 3 presents the *CAR* values in the days following the lottery. The asymmetric event windows start on the event day and end between one and six trading days later:

$$CAR(0, n) = \sum_{t=0}^n AR_t. \quad (6)$$

I note that the positive abnormal returns persist throughout the days following the event day. The *CAR* gradually increases up to the third day after the event with an estimate of 1.128 percentage points. For the windows beyond March 24, the *CAR* decreases to an insignificant 0.790 percentage points on March 29. In Table 4 I report the results for a range of symmetric windows around the event day:

$$CAR(-n, n) = \sum_{t=-n}^n AR_t. \quad (7)$$

The *CAR* values range from 0.740 to 1.121 percentage points, depending on the window length. All the estimates are significant with the exception for windows (-4, +4) and (-6, +6).

Cumulative returns around the lottery are displayed in Figure 1. The plot is obtained by simply aggregating the daily  $AR_t$  values from March 11 to March 29, day by day. I note a clear pattern of an increase in *CAR* on the event day that persists throughout the following days. I draw two conclusions from Tables 2 to 4 and Figure 1. The first is that the market does not anticipate either of the possible lottery outcomes. The second is that the positive abnormal returns stemming from the lottery persists in the days following the event day.

All in all, the results from all three models individually suggest that shareholders reacted favorably to the rejection of the proposals to substantially increase both the scale and scope of

government involvement in the governance of publicly listed banks. Importantly, this is observed whether one controls for market returns or not and holds with both longer event windows of regressions (1) and (2) as well as with the shorter event windows of regression (3). I conclude that the stakeholder hypothesis is rejected in favor of the common agency hypothesis.

#### *D. Implied Value Effects*

Given that the stock market had priced in the 50% chance of rejection of the bill, the observed estimates thus represent the value differential of moving from a 50% probability of an event happening to the event happening with certainty. The implied value effects of the proposed legislation differ depending on which investment horizon one considers. On the event day, abnormal returns with regression (1) and regression (2) are 0.655 and 0.489, respectively. Thus, the total impact of rejection of the law on the event day amounts to twice the abnormal return, or 1.31 and 0.978 percentage points, respectively. In terms of *CAR* values, the lowest estimate, 0.684 percentage points, is obtained with the two-day asymmetric event window from March 19 to March 22. The highest estimate, 1.128 percentage points, is obtained with the asymmetric four-day window ranging from the event day, March 19, to March 24. Thus, the implied valuation effect for periods longer than one day ranges between 1.368 and 2.256 percentage points.

To interpret whether this range of abnormal returns is large or small, I relate them to the findings of two influential studies on the market impact of important policy and banking events. First, Bernanke and Kutner (2005) study how U.S. stock markets react to policy decisions taken by the Federal Reserve. They find that, on average, a hypothetical unanticipated 25 basis point cut in the federal funds rate target is associated with a 1% immediate daily increase in the Center for Research in Security Prices value-weighted index. This impact of a monetary policy surprise seems to stem

from either its effects on expected future excess returns or its effects on expected future dividends. Second, Swary (1986) investigate how a portfolio of large banks reacted to the announcement in 1984 that Continental Illinois National Bank (which ultimately became the largest ever U.S. bank failure) was in financial distress. The event study found significant negative abnormal returns of approximately three percentage points in the week following the news of Continental's problems. These negative returns could be explained by investors' belief that depositors would lose confidence in major banks and thereby put downward pressure on banks' earnings. Thus, the size of the implied market impact, in terms of its absolute value, of the proposal to increase both the scale and scope of government representation on the boards of banks lies somewhere between the impact of an 0.25 percentage point unexpected change in interest rates and the impact of the failure of a major commercial bank.

## **V. Robustness**

I next discuss and present the results of a wide variety of robustness checks, including the use of different samples, other event dates, and additional controls.

### *A. Market Reactions on Support and Opposition Announcement Dates*

As discussed in Section II, January 15 and February 11 were key dates in establishing the belief in the market that the government's proposals would have to be decided by a lottery. On January 15, it was announced that the bill had a 50% support level and, on February 11, it was announced



that the remaining 50% of parliament members would vote no to the two main parts of the bill.<sup>9</sup> Thus, on the later date, it became clear that there would be a parliamentary deadlock that could only be solved by a lottery. If shareholders saw government involvement in the governance of publicly listed banks as value enhancing (destructive), then the returns should have been positive (negative) on January 15 and negative (positive) on February 11.

In Table 5, I examine the abnormal returns for the banking sector on these two dates. Column (1) (column (2)) reports the results from estimating regression (1) (regression (2)) where January 15 (February 11) is the event day,  $t = 0$ , in the first (second) row. The reaction is strongly negative to the announcement on January 15. The *AR* coefficients are -0.720 and -0.802 percentage points, respectively; by contrast, the reaction is strongly positive to the announcement on February 11 and the *AR* coefficients are 0.302 and 0.461 percentage points, respectively. All the coefficient estimates in Table 5 are significant at the 1% level. I conclude that the reactions of shareholders on these two dates are consistent with the hypothesis that shareholders see government involvement in the governance of publicly listed banks as value destructive.

<sup>9</sup> The motion of the Communist Party was written and submitted to parliament—that is, made public—on January 15 (Protocol 197576-50, p. 92). The three right-wing motions were written on February 9 but were not submitted to parliament until February 11 (Protocol 197576-64, p. 73).

## *B. Abnormal Returns in Other Business Sectors*

Studying the returns of the non-banking firms listed on the SSE may help us in asserting that the *AR* values I obtained for the banking sector in Section IV are truly in response to the rejection of the government's proposals. In addition to the positive or negative impact on banks, it was also debated how the bill would affect the broader business community. It was generally argued that it would limit the free credit market, where different credit institutions can arrive at market compatible decisions, and thus reduce the possibilities of allocating credit efficiently (Huss, 1975, comments by Lars-Erik Thunholm, pp. 508 and 517, and by Thomas Hagdahl, pp. 516–517). Thus, one would generally expect shareholders of firms that risked problems obtaining credit if the bill passed to welcome the lottery outcome as positive news. However, it was also argued that the government representatives could potentially force banks to develop currency forward markets (Sandberg, 1975). Such markets were much needed by exporting firms to hedge floating exchange rates, but banks had been hesitant to develop them because of the high costs involved. Thus, shareholders of the main exporting business sectors may not see rejection of the bill as univocally positive. The biggest exporting sectors of the economy at the time were the forest and agriculture sector and the industrial sector (Statistical Abstract of Sweden, 1976). Thus, if rejection of the proposed legislation implied foregone benefits for these two sectors, one should expect their *AR* values to react less positively compared to those of the other business sectors on the event day.

In Table 6, I present the event day estimates of the *AR* values from all five business sectors that were represented on the SSE at the time: banks; manufacturing; forest and agriculture; industrials; and shipping, trade, and investment. The estimates for each sector are shown in Panel A for regression (1), and in Panel B for regression (2).

I report the returns of the banking sector in column (1) of Table 6, which are the same estimates that were reported in Table 1. In columns (2), (4), (6), and (8), I report the *AR* values of the forest and agriculture, manufacturing, industrials, and shipping, trade, and investment sectors, respectively. In both panels, I note that the lowest *AR* values are for the main two exporting sectors, that is, forest and agriculture and industrials. Accordingly, the largest differentials between the returns of the banking sector and the other sectors—presented in columns (3), (5), (7), and (9)—are for the industrial sector and the forest and agriculture sector. The relatively weaker performance of these two sectors on the event day is consistent with the withdrawal of expectations that the proposed legislation would have spurred investments by banks in currency forward markets. The firms in the manufacturing and shipping, trade, and investment sectors enjoy strongly significant and positive *AR* values on the event day. This positive reaction is consistent with the withdrawal of concerns that the proposed legislation would have caused credit rationing and reduced the ability to obtain credit efficiently.

All in all, one notes from Table 6 that the returns across the non-banking sectors listed on the SSE are the highest (lowest) for those sectors that stood to lose the most (least) if the government's proposals had passed. This result lends credence to the interpretation of the returns of the banking sector in Section IV as causal reactions to the outcome of the parliamentary lottery.

### *C. Potentially Confounding Events*

The event study approach is designed to capture the impact of the lottery on the stock returns of the banking sector. If other events occurred at roughly the same time, there would have been the question of what was the true cause of the observed changes in the equity values of the banks. Accordingly, it is important to investigate the announcements around the event day to see if there

were any confounding events. I detail the main financial market-related events that occurred in the month of March 1976 in Appendix 2. I note that much of the news centered on volatility in the currency markets resulting from problems facing the ‘snake in the tunnel,’ which was a mechanism for managing the fluctuations of the currencies of the European Community (the snake) inside narrow limits against the USD (the tunnel). Inflation and balance of payment deficits among the member countries put pressure on the currency parities. Due to the weakness of its currency, France chose to leave the mechanism on March 15. Choi, Elyasiani, and Kopecky (1992) document that exchange rate innovations can have an impact on the returns of bank stocks. To investigate if the  $AR$  values I obtain for the banking sector are driven by exchange rate movements, I augment regression (1) and regression (2) with daily exchange rate returns between the SEK and the four main currencies at the time: the German Deutsche Mark (DM), the French franc (FF), the pound sterling (GBP), and the USD. All the exchange rate returns are computed using differences in the natural logarithm of the daily closing quotes:<sup>10</sup>

$$R_t = \alpha + ARd_t + \lambda X_t + e_t, \quad t = -252, \dots, 0, \quad (8)$$

$$R_t = \alpha + ARd_t + \beta I_t + \lambda X_t + e_t, \quad t = -252, \dots, 0, \quad (9)$$

where  $R_t$  and  $I_t$  are as defined previously and  $X_t$  is a vector of the four daily currency exchange rates returns. The results for model (8) (model (9)) are presented in columns (1) to (5) (columns (6) to (10)) in Table 7. I note that the coefficients for the DM are statistically significant at the 10% level

<sup>10</sup> Daily exchange rates are calculated using the data provided by the Board of Governors of the Federal Reserve System (available at <https://www.federalreserve.gov/releases/h10/hist/>).

in column (1) and at the 5% level in column (6). When all the exchange rates are included at the same time (columns (5) and (10)), both the DM and FF exchange rates are statistically significant. Throughout the various augmented specifications, the coefficient estimates for the event day remain strongly significant. The coefficient estimates range from 0.536 to 0.655 percentage points for regression (8) and from 0.383 to 0.487 percentage points for regression (9). I conclude that the event day *AR* for the banking sector cannot be explained away by fluctuations in the exchange rate of the Swedish SEK vis-à-vis the major currencies.

## **VI. Conclusion**

I examine if representation of one group of stakeholders, the government, in executive and non-executive bank boards is beneficial or harmful for the bank's equity value. While, on the one hand, the common agency literature argues that the involvement of stakeholders other than shareholders will increase agency costs and harm the value of the latter group, the stakeholder representation literature, on the other hand, argues that stakeholder representation can reduce agency costs and create shareholder value. Typically, it is very difficult to distinguish in equilibrium if a particular type of board member affects shareholder value. I overcome this problem with the help of a natural experiment where the Swedish parliament rejected, by means of a lottery, a government proposal to grant vast powers to unsolicited public representatives on the boards of publicly listed banks.

I find that the rejection of the proposals led to a sizable increase in the banks' equity market value. This finding is supported by a range of additional tests. The results may therefore be viewed as empirical support for those who argue that government representation in banks is harmful for owners.

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## Appendix 1. Data Management

The primary source of information that I use is the weekly stock market summaries that *SvD* published throughout the period. These summaries were typically published on weekends and they contain daily closing quotes for the studied sector's indexes for the preceding five weekdays, as well as the last trading day of the previous week. While the weekly summaries appear to have been published regularly during the study period, they were not always published on the same day of the week and did not always appear in the same location in the newspaper. Consequently, it was not always possible to locate them and occasionally one had to consult the daily stock market summaries, which were normally published in *SvD* on the day following any trading day. In total, it was possible to extract data from weekly summaries for 90.2% of the sample. Data for the remaining trading days were extracted from the daily summaries.

Likewise, in the few instances when it was impossible to decipher information in the weekly summaries, due to problems with the microfiche or photographs, the daily summaries were instead consulted. In a few instances, obvious errors were corrected, such as interchanged rows or numbers, without further consultation. As a general rule, if there were weekly summaries for two consecutive weeks, the second of these was used as source for those days that overlapped between the summaries. Repeated and careful controls of the final transcribed data against the photographs suggest that transcription errors were exceedingly rare. In addition, and to ascertain that the final data was reliable, two types of quality controls were also conducted on the data reported in *SvD*. First, a random sample of 50 trading days was drawn for which daily stock market summaries were obtained from the broadsheet *Dagens Nyheter (DN)*. Second, I used the fact that, in the weekly summaries in *SvD*, the last trading day reported in one week's summary is also the first day reported in the following week's summary. This, in turn, implies that, for each of the six indexes, there are

two observations for 120 of the days for which there is data from weekly summaries. Together, these two sets of information will give a strong indication of the quality of the data.

The *SvD* data for the control days were transcribed from weekly summaries for 46 out of the 50 days, that is, 92%, and from daily summaries for the remaining four days. In total, given the six indexes, there were 300 observations for these days and the data reported in *SvD* and *DN* differed in four instances, or 1.3% of instances. Of these, two instances can, without further information, be attributed to errors in *DN* rather than *SvD*, leaving me with two discrepancies out of 300 observations, or 0.7%, which cannot be attributed to either source. In both of these instances, the differences between the numbers reported in *SvD* and *DN* were less than one per thousand of the recorded quotes of the indexes in the final data.

Finally, the control using the 120 days with two observations in *SvD* yielded similar results. In total, there were eight discrepancies out of 720 observations, or 1.1%. Two of these instances occurred on the same day and were due to two rows having been accidentally interchanged in *SvD* one week, an obvious error that had already been corrected at the transcription phase. This leaves me with six discrepancies that would not have been otherwise identified in the absence of the availability of double observations, that is, 0.8%. Of these, all involved differences in one of the last two digits, the largest difference being 0.2% of the recorded quotes of the indexes in the final data and the remaining five being substantially smaller.

## Appendix 2. Major Financial Market-Related Events, March 1976

Information on events is from *DN* and the weekly business magazine *Affärsvärlden*.

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Date	Event
March 2	The Bank of Sweden announced it will raise the requirement on banks' liquidity ratios by one percentage point, but the earlier guidelines allowing banks to increase their lending by 12% in 1976 remains unchanged.
March 3	The Bank of Sweden allows commercial banks to increase their lending rates by another 0.2 percentage points.
March 3	Profits in Swedish banks were unexpectedly high in 1975.
March 6	The UK currency reserve increased in February by SEK 1.050 trillion and the minimum interest rate was lowered from 9.25% to 9%.
March 6	The number of unemployed decreased from 92,000 in January to 74,000 in February. In February last year this number was 77,000.
March 6	President Ford's expert group on steel imports softens their tone on plans to implement import barriers.
March 6	The British pound hits a new bottom in currency exchanges.
March 10	The government proposes expanded credit guarantees for shipbuilding. In total, guarantees would thus amount to SEK 17.5 billion.
March 11	The government invites opposition parties to talks on economic policy on March 23.

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March 12	Parliament passes a proposal to contribute a further SEK 500 million to the Fourth National Pension Insurance Fund for buying shares. The voting rights in the companies may exceed 5%.
March 12	The Swedish Trade Union Confederation presents a revised proposal about employee funds. All companies with at least 50 employees shall allot 20% of their profits to funds.
March 12	The GBP hits yet a new bottom in currency exchanges.
March 15	France leaves the cooperation of the European currency snake and lets the FF float following extensive speculation on currency markets.
March 15	Sweden's currency reserve increased by SEK 567 million in February.
March 16	The Swedish Trade Union Confederation and the Swedish Central Organization of Salaried Employees say no to the round table conference on the economic policy.
March 16	The insurance company Skandia increases boat insurance by more than 20%.
March 17	The DM reaches one percentage point above the level prescribed by the currency snake. The currencies of Belgium, Norway, and the Netherlands fall out of the bounds of the currency snake, where only the SEK remains.
March 17	It is reported that, effective April 1, the Handelsbanken and the PK Banken will lower overdraft fees from 1.0% to 0.75% and interest on postal cheque credit will be lowered similarly.
March 18	Revaluation is expected for the DM

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- March 18 Italy implements austerity measures against imports and home consumption to stop the exchange rate fall of the lira. The official discount rate is increased from 8% to 12%.
- March 18 Denmark and Belgium raise the discount rate by one percentage point each.
- March 18 Proposition 1975/76:53 is processed by parliament.
- March 19 Ship owners request government credit guarantees for SEK 1.5 billion.
- March 19 The SEK remains firm despite the tightening currency crisis.
- March 19 President Ford postpones the final decision on the import of special steel until June and requires the negotiation of “voluntary” agreements with exporting countries.
- March 19 The National Debt Office decides on a new bond with a 9% coupon and 10-year maturity.
- March 23 The Minister for Trade suggests that exporting companies should obtain state guarantees for losses when payments are made in foreign currency.
- March 24 The government and the opposition discuss inflation and taxes at the Chancery Building. No concrete results are reported. A new meeting is set for April 1, but, then, the leader of the Moderate Party will not participate.
- March 25 It is announced that the government has struck an agreement about a new provisional tax arrangement for 1977 with the Swedish Trade Union Confederation and the Swedish Central Organization of Salaried Employees that will give income earners up to SEK 2000 in tax reductions and employers a 1% increase in expenses.
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March 25	The insurance company Atlantica recalls the proposal about double issue after profits were substantially reduced after storm damages.
March 25	The government and businesses deliberate youth unemployment at Haga Palace.
March 26	The Bank of Sweden's governor warns of inflationary risks if the economic upswing is accompanied by increased credit expansion.
March 26	Consumer prices increase by 10.8% between February 1975 and February 1976.
March 30	Heavy exchange rate falls for the GBP and Italian lira continue. The UK currency reserve declines by the equivalent of USD 1.1 billion in March.
March 30	The Organisation for Economic Co-operation and Development warns Sweden about the development of costs that threaten to weaken the country's competitiveness.
March 31	The government presents a proposal for a law on co-determination for employees.

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TABLE 1—ABNORMAL RETURNS ON THE EVENT DAY

Date	(1)	(2)
March 19	0.655*** (0.035)	0.489*** (0.042)

This table reports abnormal returns ( $AR$ ) in percentage points. Columns (1) and (2) are obtained using the return-generating processes  $R_t = \alpha + ARd_t + e_t$  and  $R_t = \alpha + ARd_t + \beta I_t + e_t$ , respectively, where  $R_t$  is the daily banking sector return for day  $t$ ,  $d_t$  is a dummy variable that takes on a value of one on March 19, 1976, and zero otherwise, and  $I_t$  is the daily return on the Swedish market portfolio. The estimation period starts 252 trading days before March 19, 1976. Heteroscedasticity-consistent standard errors are reported in parentheses. Significance: \*\*\* = 1%, \*\* = 5%, \* = 10%.

TABLE 2— CUMULATIVE ABNORMAL RETURNS BEFORE THE EVENT DAY

Window	(1)
(-6, -1) March 11, March 18	-0.012 (0.138)
(-5, -1) March 12, March 18	0.023 (0.135)
(-4, -1) March 15, March 18	-0.050 (0.108)
(-3, -1) March 16, March 18	-0.006 (0.106)
(-2, -1) March 17, March 18	0.059 (0.052)

This table reports the cumulative abnormal return (*CAR*) values in percentage points. The estimated returns are obtained by means of a one-factor market model estimated for a window from March 15, 1975 (252 trading days prior to the event day, March 19, 1976), to February 27 (15 trading days prior to the event day):  $R_t = \alpha + \beta I_t + e_t$ , where  $R_t$  is the daily return of the banking sector on day  $t$  and  $I_t$  is the daily return on the Swedish market portfolio. The abnormal return ( $AR_t$ ) is obtained as the difference  $e_t$  between the raw return and the return estimated from the market model:  $AR_t = R_t - (\hat{\alpha} + \hat{\beta} I_t)$ . The  $AR_t$  values are aggregated over each respective window:  $CAR = \sum_{t=-n}^{-1} AR_t$ . Standard deviation of the *CAR* is reported in parentheses. Significance: \*\*\* = 1%, \*\* = 5%, \* = 10%.



TABLE 3—CUMULATIVE ABNORMAL RETURNS AFTER THE EVENT DAY

Window	(1)
(0, +1) March 19, March 22	0.684** (0.295)
(0, +2) March 19, March 23	0.890*** (0.289)
(0, +3) March 19, March 24	1.128*** (0.279)
(0, +4) March 19, March 25	0.953* (0.530)
(0, +5) March 19, March 26	1.043** (0.529)
(0, +6) March 19, March 29	0.790 (0.674)

This table reports the cumulative abnormal return (*CAR*) values in percentage points. The estimated returns are obtained by means of a one-factor market model estimated for a window from March 15, 1975 (252 trading days prior to the event day, March 19, 1976), to February 27 (15 trading days prior to the event day):  $R_t = \alpha + \beta I_t + e_t$ , where  $R_t$  is the daily return of the banking sector on day  $t$  and  $I_t$  is the daily return on the Swedish market portfolio. The abnormal return ( $AR_t$ ) is obtained as the difference  $e_t$  between the raw return and the return estimated from the market model:  $AR_t = R_t - (\hat{\alpha} + \hat{\beta} I_t)$ . The  $AR_t$  values are aggregated over each respective window:  $CAR = \sum_{t=0}^n AR_t$ . Standard deviation of the *CAR* is reported in parentheses. Significance: \*\*\* = 1%, \*\* = 5%, \* = 10%.

TABLE 4— CUMULATIVE ABNORMAL RETURNS AROUND THE EVENT DAY

Window	(1)
(-1, +1) March 18, March 22	0.740* (0.384)
(-2, +2) March 17, March 23	0.949** (0.422)
(-3, +3) March 16, March 24	1.121** (0.488)
(-4, +4) March 15, March 25	0.903 (0.605)
(-5, +5) March 12, March 26	1.066* (0.599)
(-6, +6) March 11, March 29	0.779 (0.697)

This table reports the cumulative abnormal return (*CAR*) values in percentage points. The estimated returns are obtained by means of a one-factor market model estimated for a window from March 15, 1975 (252 trading days prior to the event day, March 19, 1976), to February 27 (15 trading days prior to the event day):  $R_t = \alpha + \beta I_t + e_t$ , where  $R_t$  is the daily return of the banking sector on day  $t$  and  $I_t$  is the daily return on the Swedish market portfolio. The abnormal return ( $AR_t$ ) is obtained as the difference  $e_t$  between the raw return and the return estimated from the market model:  $AR_t = R_t - (\hat{\alpha} + \hat{\beta}I_t)$ . The  $AR_t$  values are aggregated over each respective window:  $CAR = \sum_{t=-n}^n AR_t$ . Standard deviation of the *CAR* is reported in parentheses. Significance: \*\*\* = 1%, \*\* = 5%, \* = 10%.

TABLE 5—ABNORMAL RETURNS ON OTHER KEY DATES

Percentage points	(1)	(2)
January 15	-0.720*** (0.035)	-0.802*** (0.040)
February 11	0.302*** (0.037)	0.461*** (0.057)

This table reports the abnormal return ( $AR$ ) values in percentage points. The results in columns (1) and (2) are obtained using the return-generating processes  $R_t = \alpha + ARd_t + e_t$  and  $R_t = \alpha + ARd_t + \beta I_t + e_t$ , respectively, where  $R_t$  is the daily banking sector return for day  $t$ ,  $d_t$  is a dummy variable that takes on a value of one on the respective date and zero otherwise, and  $I_t$  is the daily return on the Swedish market portfolio. The estimation period starts 252 trading days before each respective date. Heteroscedasticity-consistent standard errors are reported in parentheses. Significance: \*\*\* = 1%, \*\* = 5%, \* = 10%.

TABLE 6— ABNORMAL RETURNS FOR ALL BUSINESS SECTORS ON THE EVENT DAY

	Banking	F&A	Banking – F&A	Manufact.	Banking – Manufact.	Industrials	Banking – Industrials	ST&I	Banking – ST&I
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
<i>Panel A</i>									
March 19	0.655*** (0.035)	0.459*** (0.054)	0.196*** (0.064)	0.766*** (0.050)	-0.111* (0.061)	0.379*** (0.045)	0.277*** (0.057)	0.550*** (0.035)	0.105** (0.049)
<i>Panel B</i>									
March 19	0.489*** (0.042)	-0.026 (0.054)	0.515*** (0.069)	0.193*** (0.034)	0.297*** (0.054)	-0.048 (0.046)	0.538*** (0.063)	0.261*** (0.042)	0.228*** (0.060)

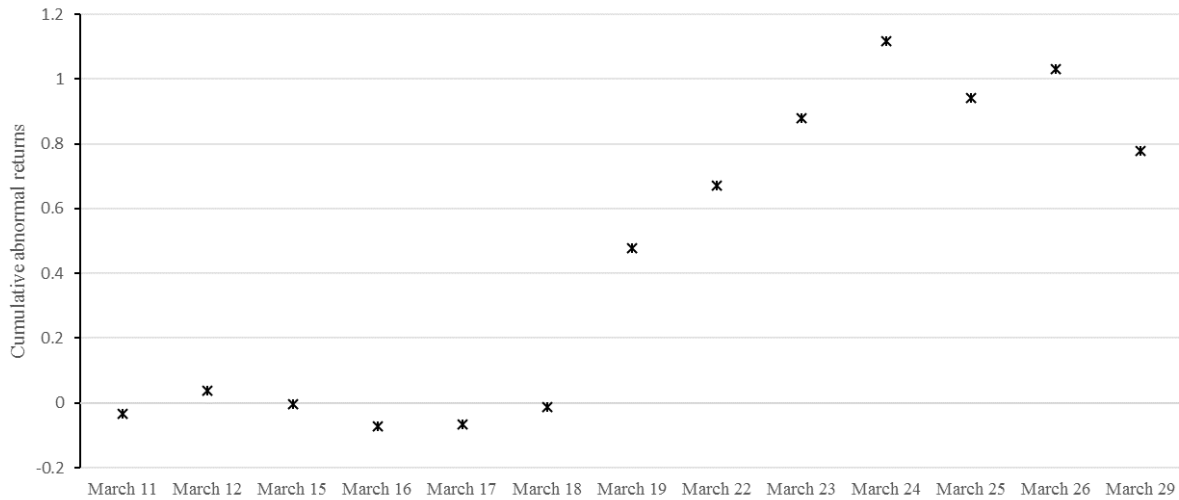
This table reports the abnormal return ( $AR$ ) values in percentage points. Panels A and B are obtained using the return-generating processes  $R_{it} = \alpha_i + AR_i d_t + e_{it}$  and  $R_{it} = \alpha_i + AR_i d_t + \beta_i I_t + e_{it}$ , respectively, where  $R_{it}$  is the daily sector return of business sector  $i$  for day  $t$ ,  $d_t$  is a dummy variable that takes on a value of one on March 19, 1976, and zero otherwise, and  $I_t$  is the daily return on the Swedish market portfolio. The estimation period starts 252 trading days before March 19, 1976. The business sectors are banking, forest and agriculture (F&A), manufacturing (manufact.), industrials, and shipping, trade, and investment (ST&I). Heteroscedasticity-consistent standard errors are reported in parentheses. Significance: \*\*\* = 1%, \*\* = 5%, \* = 10%.

TABLE 7—EVENT DAY MODELS AUGMENTED WITH EXCHANGE RATES

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
March 19	0.598*** (0.051)	0.647*** (0.036)	0.654*** (0.035)	0.655*** (0.035)	0.536*** (0.057)	0.425*** (0.049)	0.484*** (0.043)	0.487*** (0.043)	0.487*** (0.043)	0.383*** (0.058)
$I_t$						0.355*** (0.064)	0.349*** (0.065)	0.353*** (0.065)	0.356*** (0.065)	0.349*** (0.064)
DM	21.481* (12.570)				37.850*** (13.956)	23.446** (9.776)				34.509** (13.540)
FF		-9.214 (6.583)			-19.699** (8.892)		-6.369 (5.747)			-16.748** (7.726)
GBP			-2.055 (4.589)		1.725 (6.309)			-2.753 (2.937)		2.225 (5.639)
USD				2.108 (4.733)	-1.973 (6.803)				3.472 (2.884)	0.224 (5.913)
Constant	0.024 (0.035)	0.026 (0.035)	0.025 (0.035)	0.025 (0.035)	0.024 (0.035)	0.005 (0.033)	0.006 (0.033)	0.005 (0.033)	0.005 (0.033)	0.005 (0.033)
Observations	252	252	252	252	252	252	252	252	252	252
$R^2$	0.019	0.010	0.007	0.007	0.035	0.158	0.144	0.145	0.147	0.169

This table reports the abnormal return ( $AR$ ) values in percentage points. Columns (1) to (5) and columns (6) to (10) are obtained using the return-generating processes  $R_t = \alpha + ARd_t + \lambda X_t + e_t$  and  $R_t = \alpha + ARd_t + \beta I_t + \lambda X_t + e_t$ , respectively, where  $R_t$  is the daily return of the banking sector for day  $t$ ;  $d_t$  is a dummy variable that takes on a value of one on March 19, 1976, and zero otherwise;  $I_t$  is the daily return on the Swedish market portfolio; and  $X_t$  is a vector of daily returns of currency exchange rates for the DM, the FF, the GBP, and the USD. The estimation period starts 252 trading days before March 19, 1976. Heteroscedasticity-consistent standard errors are reported in parentheses. Significance: \*\*\* = 1%, \*\* = 5%, \* = 10%.

FIGURE 1—CUMULATIVE ABNORMAL RETURNS AROUND THE EVENT DAY



This figure reports the cumulative abnormal return ( $CAR$ ) for the banking sector in percentage points. The estimated returns are obtained by means of a one-factor market model estimated for a window from March 15, 1975 (252 trading days prior to the event day, March 19, 1976), to February 27 (15 trading days prior to the event day):  $R_t = \alpha + \beta I_t + e_t$ , where  $R_t$  is the daily return of the banking sector on day  $t$  and  $I_t$  is the daily return on the Swedish market portfolio. The abnormal return ( $AR_t$ ) is obtained as the difference  $e_t$  between the raw return and the return estimated from the market model:  $AR_t = R_t - (\hat{\alpha} + \hat{\beta} I_t)$ . The plotted  $CAR$  values are obtained by aggregating the  $AR_t$  values day by day from March 11 to March 29.