RISK PREMIUMS FROM MARKET DISRUPTIONS: THE RATE FIX FRAUD EVENT 2005-2009

Rafael A. Martínez-Muñoz, University of Puerto Rico - (E.G.A.E.), Río Piedras Campus, PR, USA

dx.doi.org/10.18374/JIFS-14-1.8

ABSTRACT

This study measures the abnormal returns / risk premiums that could be attributed to the rate fix event occuring during 2005 through 2009 using the event study methodology. Market rate spread excess returns above alternative benchmarks are measured for Fed Funds, Eurodollar and Euribor spot rates using daily data series from 2001 through 2011. Risk premium discovery reveals that the market fraud event accounts for risk premiums, due to downside risks and noise risk explained by the behavior and decision choice processes of investors that support and document their investment related actions which cause market prices and returns to deviate from their fundamental intrinsic values in the marketplace. Results uncover that mispricing occurs due to documented rate fixing market fraud, shifting of preferences and incompleteness of the futures market. This implies that asset management requires monitoring and measuring market disruption's risk premiums by controlling market fraud with governance mechanisms.

Keywords: *behavioral finance, corporate governance, market efficiency, event study, rate fix fraudE-Subjects: Behavioral Finance, Convergence, Market Efficiency, Corporate Governance, Market Fraud, Risk Premium; Behavioral Anomalies*