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Maastricht-NUS-MIT Conference 2011 and 2012 Introduction to the Special Issue

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This special issue of the Journal of Real Estate Finance and Economics combines papers of the 2011 conference in Maastricht and the 2012 conference in Singapore. From these two conferences, a total of eight papers were accepted for publication in this special issue. These paper cover three broad topics: REITs, Housing and Housing Finance, and Behavioral Finance.

In their paper "Naked Short Selling and the Market Impact of Fails-to-Deliver: Evidence of the Trading of Real Estate Investment Trusts", Erik Devos, Thomas McInish, Michael McKenzie and James Upson put a widely held notion to rest. From early 2007 to the end of 2008, the US REIT market lost more than half of its market capitalization. Received wisdom has it that short selling was partly to blame for this loss. The authors investigate whether short selling and subsequent failures to deliver the REIT stocks thus sold have indeed contributed to this sharp deterioration in REIT returns. The empirical analysis that is the core of the paper suggests that this is not the case, and the authors conclude that short selling and fails-to-deliver did not play an important role in the adverse REIT performance of that period.

Another oft-cited reason for the sharp drop in real estate returns was that they were overpriced to begin with, implying that the negative returns of the crisis were a correction back to equilibrium. This idea is put under scrutiny in the second REIT paper in this issue, written by Massimo Guidolin, Francesco Ravazzolo, and Andrea Donato Tortora, which is entitled "Myths and Facts about the Alleged Overpricing of U.S. Real Estate: Evidence from Multi-Factor Asset Pricing Models of REIT Returns." The authors investigate whether REIT returns for the years from 2003 through 2006 can be satisfactorily explained by a multi-factor asset pricing model that the authors calibrate using a total sample covering 30 years of data. The main finding is that REITs did exhibit weak overpricing in the years preceding the crisis, but that held mostly for mortgage REITs, while equity REITs were fairly priced. This suggests that overpricing is not likely to have been a considerable cause of the subsequent crisis in REIT returns.

The third REIT paper is not related to the crisis, but deals with REIT financing, and specifically with convertible debt issuance. In their paper "Do Investor Demand and

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Market Timing Affect Convertible Debt Issuance by REITs?", Masaki Mori, Joseph Ooi en Woei Chyuan Wong investigate whether the institutional environment surrounding REITs affects their behavior in convertible debt financing. During 2006 and 2007 US REITs suddenly strongly increased their use of convertible debt as a funding source. Theory would argue that convertible debt issuance is especially attractive to firms facing high information asymmetries, and which are optimistic about their future share price. However, REITs are relatively transparent and the authors hypothesize that investor demand may have been a driver of this surge in convertible debt issuance. This turns out to be the case: the REIT convertibles have been bought mainly by convertible bond arbitrageurs, and REITs have significantly timed the market in their issuing behavior.

In a fourth REIT paper S.K. Wong, Qian Wei and K.W. Chau show how the choice of what stock market to be listed on can signal the quality of a REIT. Their paper, entitled "IPO Location as Quality Signal: The Case of Chinese Developers," focuses on Chinese developers launching IPOs either on the Hong Kong or mainland Chinese stock exchanges. The Hong Kong exchanges have more stringent reporting and governance standards, which are more difficult for lower quality developers to meet, but listing there tends to result in better post-IPO performance. Mainland IPOs show greater underpricing. The findings are consistent with a signaling hypothesis in which better firms signal their quality by listing on the more stringent Hong Kong Exchange.

The second topic addressed in this special issue is Housing and Housing Finance. Hua Sun and Seow Eng Ong's paper "Bidding Heterogeneity, Signaling Effect, and Its Implications on House Seller's Pricing Strategy" investigates how house sellers set their asking prices. The authors create a theoretical model based on reference-dependent seller utility and on a weakly heterogeneous housing market. In this model, willingness to pay is positively related to the level of recent transactions of dwellings regarded as close substitutes, and negatively related to a transaction occurring in the first place, and sellers adjust their asking prices accordingly. Using a sample of condominium sales in Singapore, the authors find that the data confirm these theoretical predictions: after controlling for transaction price, the occurrence of transactions does indeed lead to reductions in asking prices, and sales in the same building have stronger effects than sales in buildings close by.

Shuang Zhu and Kelly Pace investigate home mortgage default decisions in their paper "Modeling Spatially Interdependent Mortgage Decisions." The paper applies spatial regression techniques developed to model house prices to the mortgage market. Traditional models for mortgage default and prepayment implicitly assume independence between the actions of mortgage borrowers, but Zhu and Pace find that the inclusion of spatial variables in the model leads to more predictive precision in mortgage defaults: the data show that it matters what the neighbors do for households' propensity to default.

This empirical finding is in line with the results of the highly original paper by Mike Seiler, Mark Lane and David Harrison entitled "Mimetic Herding Behavior and the Decision to Strategically Default." But they reach that conclusion using a completely different approach and employ experimental techniques to explore the causes or determinants of home-owners' strategic defaults. The issue is how individuals are able to come to a decision that involves some degree of ethical compromise, considering that they have signed a legal contract to service the loan. "Mimetic" herding refers to a non-learned, innate tendency to follow the perceived behavior of a group of one's peers. In the experimental setting, individuals' willingness to strategically default was significantly influenced by their perceptions of their peers' willingness to default. This behavior intensified when the homeowner (falsely) observes a maven's, or market leader's choice in each scenario. But owners having a stronger prior moral viewpoint on strategic default were less likely to herd.

In a second paper in the Behavioral Finance area, "Short Term Buyers & Housing Market Dynamics", Bob Edelstein and Wenlan Qian show that taking into consideration heterogeneous investment horizons improves understanding of price and trading dynamics in the housing market. In their model agents have heterogeneous preferences and investment horizons. With transaction costs, short term investors are more sensitive to changes in fundamentals and are less likely to own (and trade) in a declining market. The model predicts that the ownership composition contains information about current and future price and trading dynamics. Empirically they find that owners' expected holding horizons co-vary negatively with prices, and they also predict future (short term) returns.