When the Thin Bench Gets Thinner: Investment Bank Consolidation and Municipal Finance

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Background

- The current administration has shown support for major bank antitrust reforms (Reuters, 2021, 2023)
- A key aspect is for the Justice Department to work with bank regulators and heighten the scrutiny of bank M&A deals
- Prior research shows economic impacts of commercial bank M&As
  - Branch closures and reduced credit access (Nguyen, 2019; Fraisse et al., 2018; Ratnadiwakara and Yerramilli, 2022), higher borrowing costs (Garmaise and Moskowitz, 2006), real economic consequences (Garmaise and Moskowitz, 2006)
- Investment banking activities are often overlooked in bank antitrust scrutiny

Background

- Security issuance is a pillar of the financial system
- In the U.S. in 2022, the total amounts of new issuance are
  - Corporate equity: $102 billion
  - Corporate bond: $883 billion
  - Municipal bond: $410 billion

- Do the market structure and market power of security underwriters matter?

- Do powerful underwriters make security issuance expensive?
- How should we view the underwriting fees?
  - Rightfully compensated for the skills demanded and risks involved?
  - Or, do underwriters possess market power and earn economic profits?

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Background

Short on financial knowledge, some school districts get bad deals on bonds

Districts can fall prey to financial firms that put their own interests first

by **SARAH BUTRYMOWICZ** and **NICHOLE DOBO**
April 22, 2019

Investigate Midwest:

- Issuers (school districts) can "*easily be taken advantage of—urged to issue needless or poorly structured bonds, pushed to accept high interest rates or duped into paying hundreds of thousands in unreasonable fees*"

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Background

- To study underwriters' market power, an instinctive strategy is to use M&As as a shifter of market power

- The municipal bond primary market has several advantages:
  - Finances key public infrastructure and services
  - High geographical fragmentation
  - Significant consolidating activities among local and regional underwriters
  - A vast amount of heterogeneous issuers
  - Stable flows of issuance driven by public needs
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Research Question

1. Do M&As among municipal bond underwriters lead to higher underwriting fees?
2. If so, can the evidence be viewed as these underwriters having market power?
3. Do these M&As lead to efficiency gains and better services that could offset the rise in fees from the standpoint of issuers?
4. Do these M&As depress new issuance of local governments?

Overview of Findings

1. The underwriting spread rises by $\approx 5\%$ of the sample mean after M&As
2. Consistent with an enhanced market power interpretation, effects double for larger deals and in more concentrated markets
3. The findings hold in scenarios less likely to be confounded by endogeneity concerns and are absent in three placebo tests
4. Efficiency gains, if any, are too small to offset the rise in the underwriting spread
5. Using Census data, I validate the rise in financing costs and show a reduction in new issuance

Related Literature

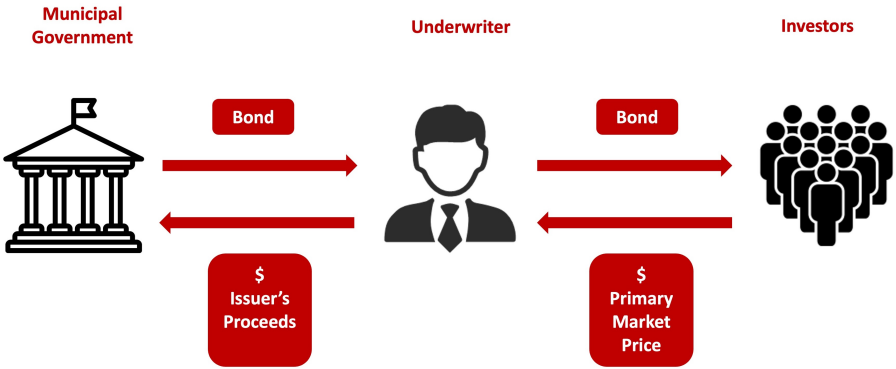
- Underwriter market power: Chen and Ritter (2000), Manconi et al. (2019), Cestau (2019), Cestau (2020), Garrett and Ivanov (2023)
- Financial institution M&As: Prager and Hannan (1998), Sapienza (2002), Focarelli and Panetta (2003), Garmaise and Moskowitz (2006), Erel (2011) Fraisse et al. (2018), Nguyen (2019), Ratnadiwakara and Yerramilli (2022)
  - First paper on investment bank M&A
- Municipal bond market: Butler et al. (2009), Cornaggia et al. (2017), Adelino et al. (2017), Gao et al. (2019), Dougal et al. (2019), Painter (2020), Goldsmith-Pinkham et al. (2023), Garrett (2023), Cao et al. (2024), and many more

Data and Sample

- Municipal bond issues
  - Source: SDC Platinum Global Public Finance Database
  - Variables:
    - Underwriting spread: The difference between the initial offering price paid by initial investors and the proceeds that the government receives, expressed as a fraction of the principal amount

- M&A sample:
  - I hand-collect M&As among municipal bond underwriters active in 1970-2022
  - I complement the sample with SDC Platinum M&A Database and SNL Financial M&A Database
  - 258 M&A deals, among which 162 have geographic overlaps

Data and Sample



Underwriting Spread ($) = Primary Market Price – Issuer's Proceeds

- Underwriters (1) assume inventory risks (2) exert marketing and distributing efforts

Data and Sample

Negotiated Sales

Issuer selects underwriter via a "Request for Proposal" process

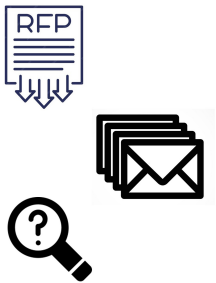
Data and Sample

Negotiated Sales

Issuer selects underwriter via a "Request for Proposal" process

↓

Underwriter analyzes and gauges investors' interest in bonds



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Underwriter buys bonds and then redistribute to investors

Back

Data and Sample

Competitive Bidding

Issuer decides on offering terms with the help of financial advisor

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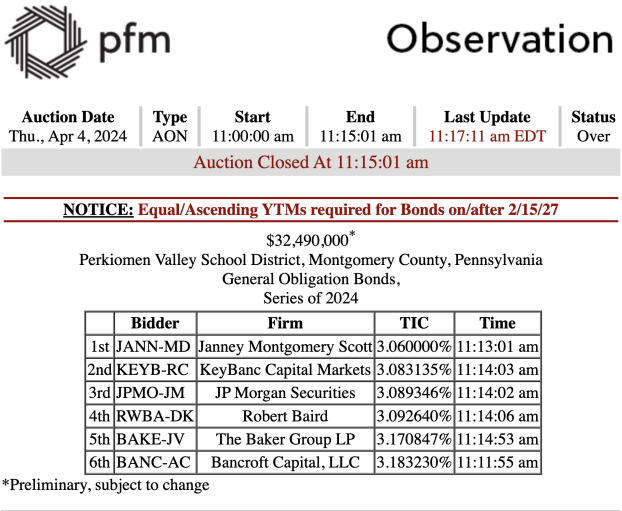
Issuer decides on offering terms with the help of financial advisor

Issuer sets up an auction and underwriters place bids for the bonds

Data and Sample

- An auction has a median (mean) number of 4 (4.1) bidders



pfm Observation

Auction Date	Type	Start	End	Last Update	Status
Thu., Apr 4, 2024	AON	11:00:00 am	11:15:01 am	11:17:11 am EDT	Over

Auction Closed At 11:15:01 am

NOTICE: Equal/Ascending YTMs required for Bonds on/after 2/15/27

$32,490,000*
Perkiomen Valley School District, Montgomery County, Pennsylvania
General Obligation Bonds,
Series of 2024

	Bidder	Firm	TIC	Time
1st	JANN-MD	Janney Montgomery Scott	3.060000%	11:13:01 am
2nd	KEYB-RC	KeyBanc Capital Markets	3.083135%	11:14:03 am
3rd	JPMO-JM	JP Morgan Securities	3.089346%	11:14:02 am
4th	RWBA-DK	Robert Baird	3.092640%	11:14:06 am
5th	BAKE-JV	The Baker Group LP	3.170847%	11:14:53 am
6th	BANC-AC	Bancroft Capital, LLC	3.183230%	11:11:55 am

*Preliminary, subject to change

Data and Sample

Competitive Bidding

Issuer decides on offering terms with the help of financial advisor

↓

Issuer sets up an auction and underwriters place bids for the bonds

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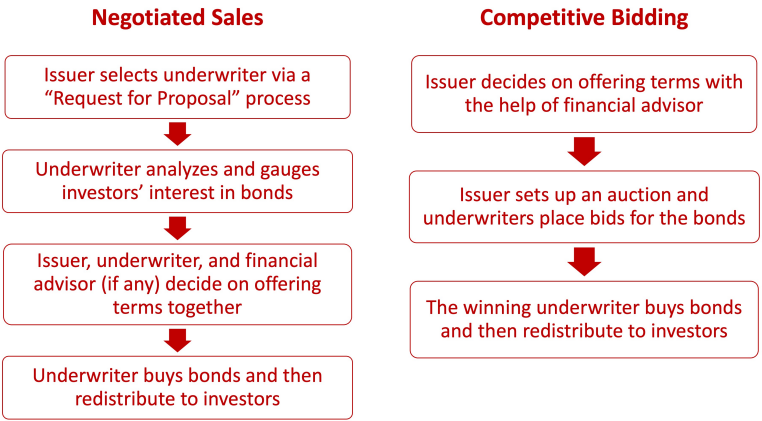
The winning underwriter buys bonds and then redistribute to investors

Data and Sample



- Negotiated sales: Underwriting spread largely determined in "Request for Proposal"
- Competitive bidding: Underwriting spread = Primary market price - Winning bid

Data and Sample

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Data and Sample: Geographic Fragmentation

- The municipal bond underwriting market is much more geographically fragmented compared to corporate securities underwriting
- Average cosine similarity of underwriters for a state-pair is
  - Corporate equity: 0.508
  - Corporate bond: 0.613
  - Municipal bond: 0.193

- Reasons for the highly fragmented form:
  - Local governments' favorism over local businesses
  - Local underwriters have better access to same-state investors, who are the prominent owners of municipal bonds due to tax advantages (Babina et al., 2020)
  - Accumulated, substantial experience in underwriting for nearby governments (Butler, 2008)

Data and Sample: Geographic Fragmentation

Underwriter in CA	Market Share in CA	Underwriter in MA	Market Share in MA
Stifel Nicolaus	14.9%	Eastern Bank	15.4%
Piper Sandler	11.8%	Century Bank	7.2%
Citigroup	7.1%	TD Bank	7.1%
RBC Bank	6.6%	Robert W Baird	5.9%
Morgan Stanley	5.6%	Jefferies	5.1%
Raymond James	5.4%	JP Morgan	4.6%
Stone & Youngberg	5.3%	Morgan Stanley	4.4%
Bank of America	4.8%	Bank of America	4.2%
De La Rosa	3.6%	Fidelity Capital Markets	3.9%
JP Morgan	3.4%	Janney Montgomery Scott	3.6%

Table: Top Ten Municipal Bond Underwriters in 2010-2020 in CA and MA

Data and Sample: Geographic Fragmentation

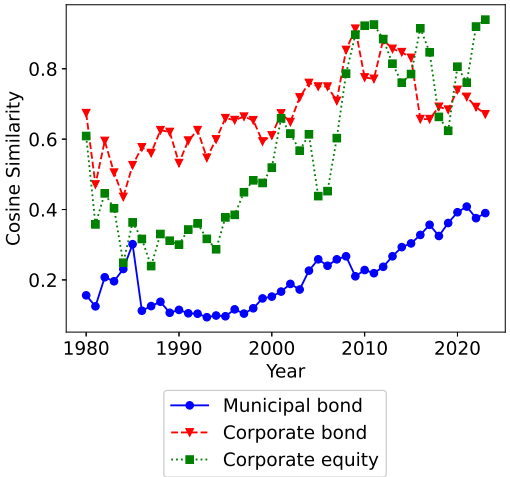

Table: Underwriter Similarity for State-Pairs by Each Security Type

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Data and Sample

- Market: A Combined Statistical Area (CSA), 218 in the U.S.
- Treated: CSAs where M&As would lead to *predicted* Δ_{HHI} >= 100
  - $\Rightarrow$ 219 "local M&A episodes"

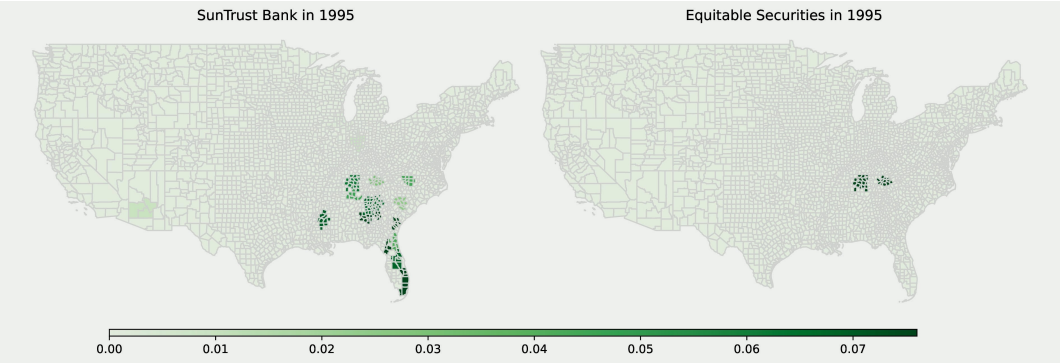
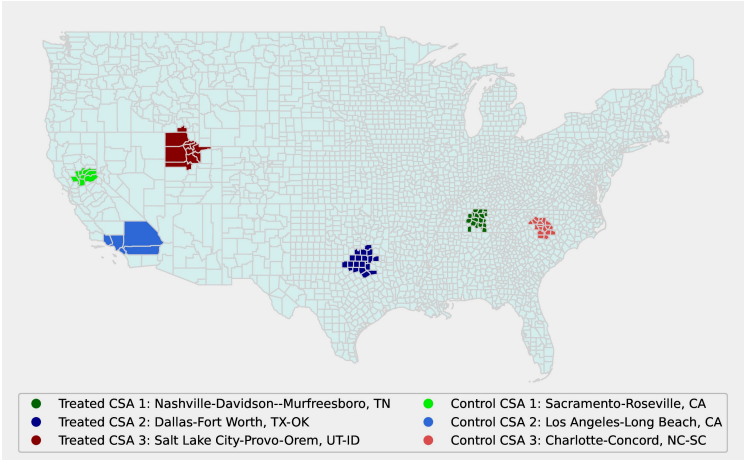


Figure: An Example of M&A and Local Market Share

Data and Sample

Control: One CSA that is closest in terms of population and income per capita, and not affected by within-market M&As during $[-4, +4]$



Main Findings: Effects on Underwriting Spread

- I estimate a stacked DID (Gormley and Matsa, 2011, 2016):

$$y_{d,c} = \beta_1 Post_{c,t} + \beta_2 Treated_{a,c} \times Post_{c,t} + \theta_{i,c} + \theta_t + e_{d,c}$$

  where
  - d is the subscript for each bond issue, i.e., each deal
  - a is the subscript for each Combined Statistical Area (CSA)
  - c is the subscript for each cohort of treated and control CSAs
  - i is the subscript for each issuer
  - t is the subscript for the calendar year
  - Double-cluster SEs at CSA and year levels

- Theoretically, the direction of the effect is unclear
  - M&As can bolster market power and raise underwriting spread
  - Alternatively, M&As could create synergies and reduce marginal cost, which might pass on to issuers as lower prices

Main Findings: Effects on Underwriting Spread

M&As that would lead to *predicted* Δ_{HHI} >= 100

$\Rightarrow$ A 5.0 bps. increase in underwriting spread from a sample mean of 103.0 bps.

	Predicted Δ_{HHI} >= 100	Market Share >= 5%	*Predicted* $\Delta_{Top\ 5\ Share}$ >= 5%
	(1)	(2)	(3)
	Underwriting Spread (bps.)	Underwriting Spread (bps.)	Underwriting Spread (bps.)
Treated × Post	4.98***	4.48***	4.42***
	(3.15)	(4.47)	(2.68)
Observations	79,642	148,352	74,250
Year FE	Yes	Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year
Adjusted R-squared	0.529	0.513	0.506

Table: Effects of M&As on Underwriting Spread

Main Findings: Effects on Underwriting Spread

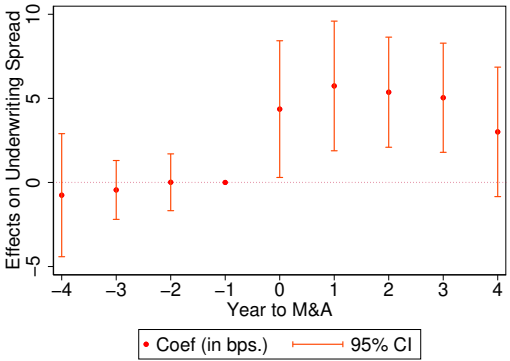


Figure: Underwriting Spread Around M&As that Lead to *Predicted* Δ_{HHI} >= 100

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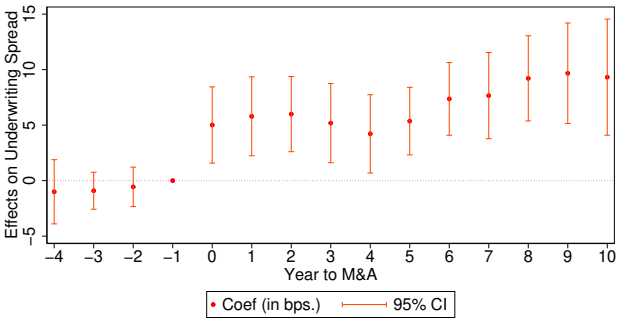


Figure: Underwriting Spread Around M&As that Lead to *Predicted* Δ_{HHI} >= 100

Main Findings: Robustness Tests

- Include state × calendar year fixed effects
- Include underwriter × calendar year fixed effects
- Include issuer-underwriter-match × cohort fixed effects
- Include fixed effects for each method of sale, taxable status, source of repayment, and their interactions with calendar years
- Control for the principal amount, length of maturity, and their squared terms
- Control for whether CBs are eligible to underwrite the bond issue by law
- Define the market at the finer CBSA level
- Use two or three matches or a sample without matching
- Match on local demographic and economic trends and issuance outcomes
- Address critics in Baker et al. (2022)
- Apply corrective weights proposed in Wing et al. (2024)

Main Findings: Effects on Underwriting Spread

Going from 5 equal-sized underwriters to 4 equal-sized underwriters
$\Rightarrow$ A rise in the underwriting spread by 22.3 basis points

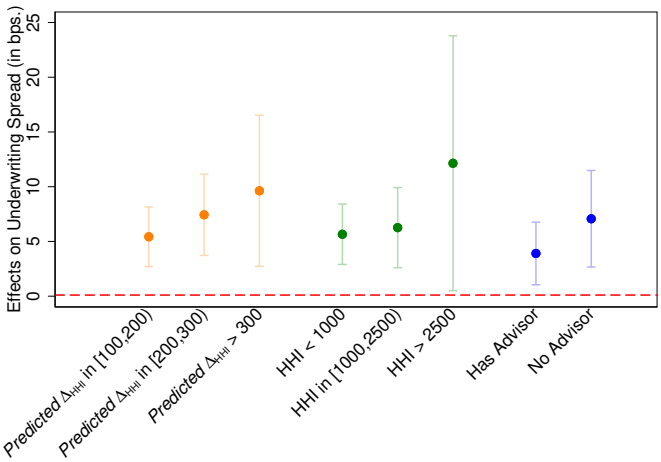
	OLS	IV - First Stage	IV - Second Stage
	(1)	(2)	(3)
	Underwriting Spread (bps.)	HHI	Underwriting Spread (bps.)
HHI	-0.00		0.04**
	(-0.97)		(2.11)
Treated × Post		111.60**	
		(2.59)	
Observations	79,642	79,642	79,642
Year FE	Yes	Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year
Adjusted R-squared	0.529	0.823	

Table: Estimating the Elasticity of Underwriting Spread to HHI

Main Findings: Effects on Underwriting Spread

Consistent with increased market power:

Figure: Cross-Sectional Heterogeneities in Effects



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Continue

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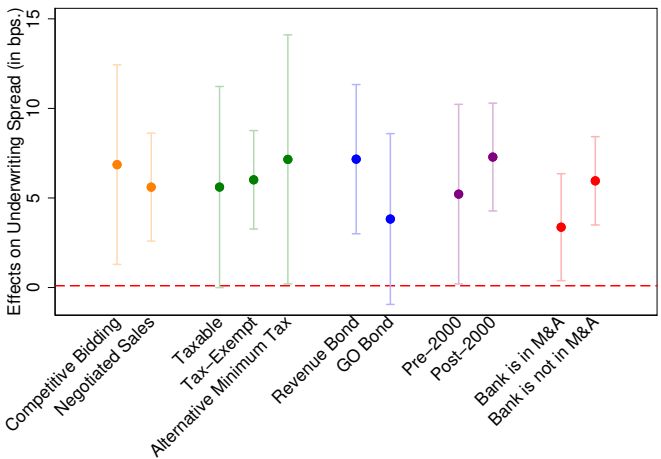

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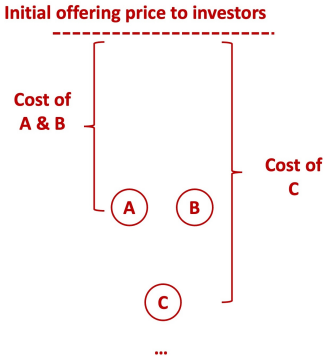

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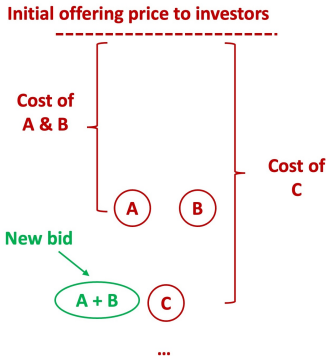

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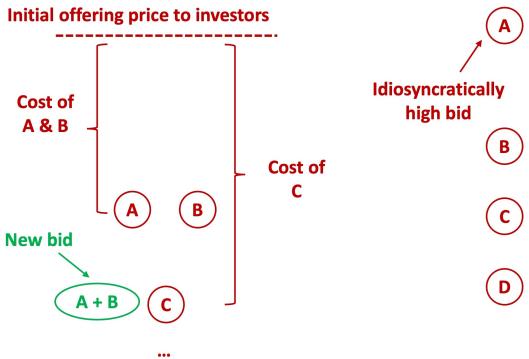

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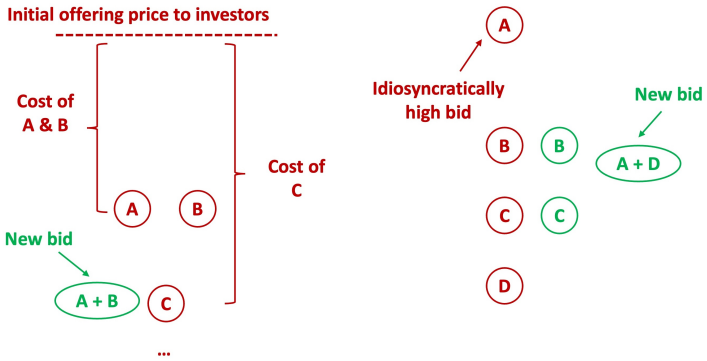

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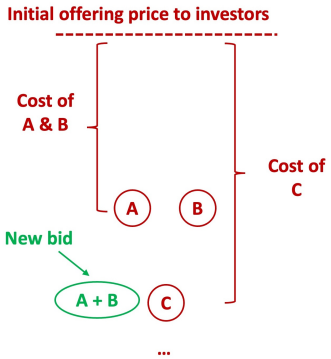

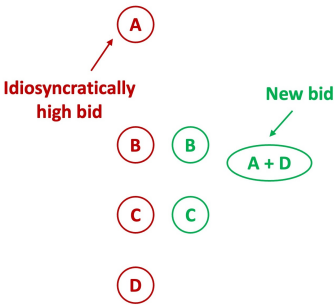

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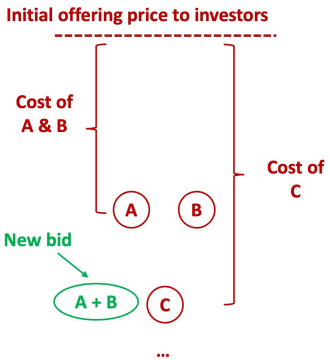

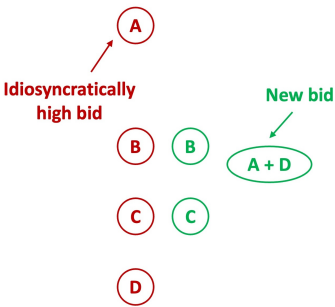

⇒ I examine effects by prior bank-issuer relationships

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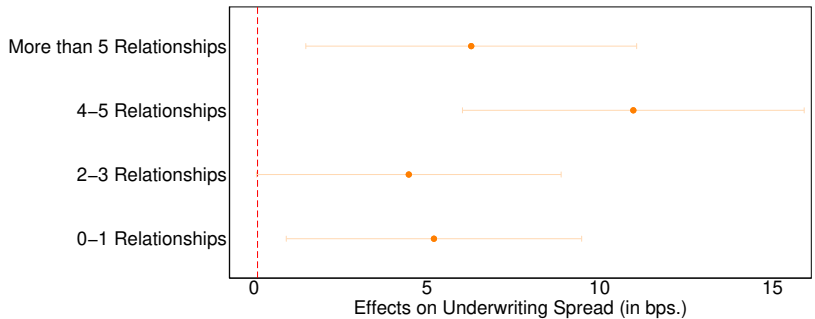
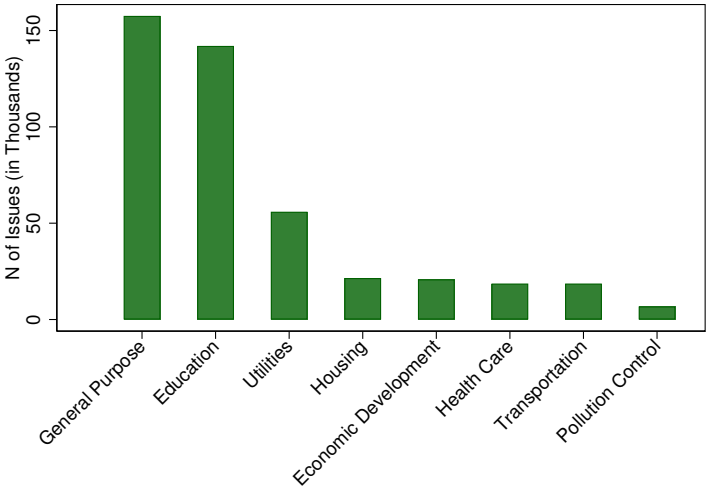
Figure: Effects by Prior Bank-Issuer Relationships



Main Findings: Effects on Underwriting Spread

Figure: Effects by the Main Use of Proceeds



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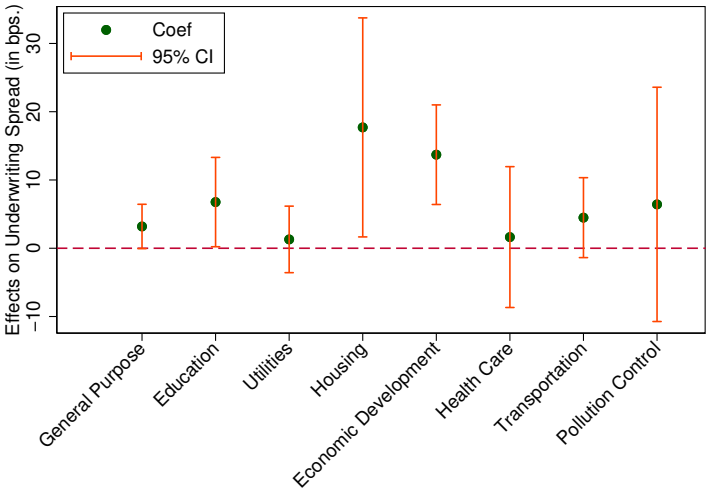

Main Findings: Addressing Endogeneity Concerns

- Main concerns:
  - Omitted Variable Bias: Local economic dynamics drive both M&As among underwriters and the underwriting spread
  - Reverse Causality: Underwriters merge because they anticipate future changes in underwriting spread in the local market
- Effects hold when
  - #1: Consider only scenarios where the M&A-affected markets account for a small fraction of the total businesses of the merging underwriters (Garmaise and Moskowitz, 2006; Dafny et al., 2012; Sunderam and Scharfstein, 2017)
  - #2: Consider only M&As for which the rationales, according to news articles, are unrelated to the local economy (Romer and Romer, 2010)

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Main Findings: Addressing Endogeneity Concerns

CSA	Significance of CSA for RBC Bank	Significance of CSA for Dain Bosworth	
Minneapolis-St. Paul, MN-WI	10.6%	9.5%	✗
Albuquerque-Santa Fe-Los Alamos, NM	5.4%	3.9%	✗
Milwaukee-Racine-Waukesha, WI	2.2%	1.9%	✓
Brownsville-Harlingen-Raymondville, TX	2.1%	1.8%	✓
Dallas-Fort Worth, TX-OK	1.3%	1.4%	✓
Omaha-Fremont, NE-IA	1.0%	1.0%	✓

Table: Significance of Affected Markets for Merging Underwriters

Main Findings: Addressing Endogeneity Concerns

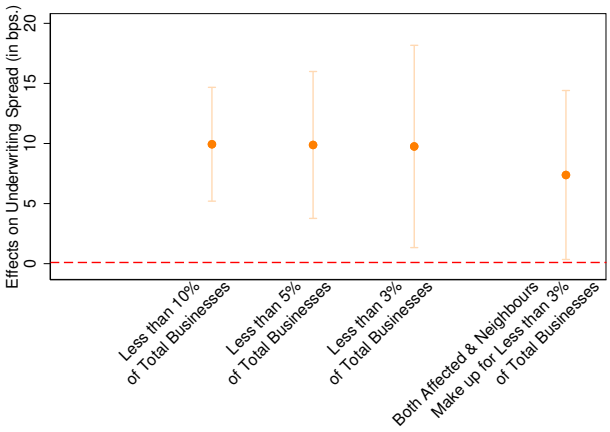

Figure: Using Scenarios Where the M&A-Affected Areas Account for Small Fractions of the Total Businesses of the Merging Underwriters

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- Main concerns:
  - Omitted Variable Bias: Local economic dynamics drive both M&As among underwriters and the underwriting spread
  - Reverse Causality: Underwriters merge because they anticipate future changes in underwriting spread in the local market
- Effects hold when
  - #1: Consider only scenarios where the M&A-affected markets account for a small fraction of the total businesses of the merging underwriters (Garmaise and Moskowitz, 2006; Dafny et al., 2012; Sunderam and Scharfstein, 2017)
  - #2: Consider only M&As for which the rationales, according to news articles, are unrelated to the local economy (Romer and Romer, 2010)

Main Findings: Addressing Endogeneity Concerns

PNC Bank & Midlantic Bank, 1995

The Morning Call: *"The move, along with PNC Bank's pending acquisition of 84 branches of Chemical Bank New Jersey, will strengthen PNC Bank's position in the New Jersey and Philadelphia markets, placing it second in those areas."*

⇒ **The acquiror's desire to gain local/regional dominance**

Main Findings: Addressing Endogeneity Concerns

Morgan Stanley & Dean Witter Reynolds, 1997

The New York Times: *"In recent years, as the securities markets have changed, however, both firms started to covet what the other had. Dean Witter's 9,300 brokers needed more products to sell to the firm's Main Street customers, specifically the initial public offering stocks and municipal bonds that Morgan Stanley frequently underwrites. Morgan Stanley, meanwhile, wanted to broaden its customer base beyond its corporate clients and large institutions to the individual investors who have been flocking to the market."*

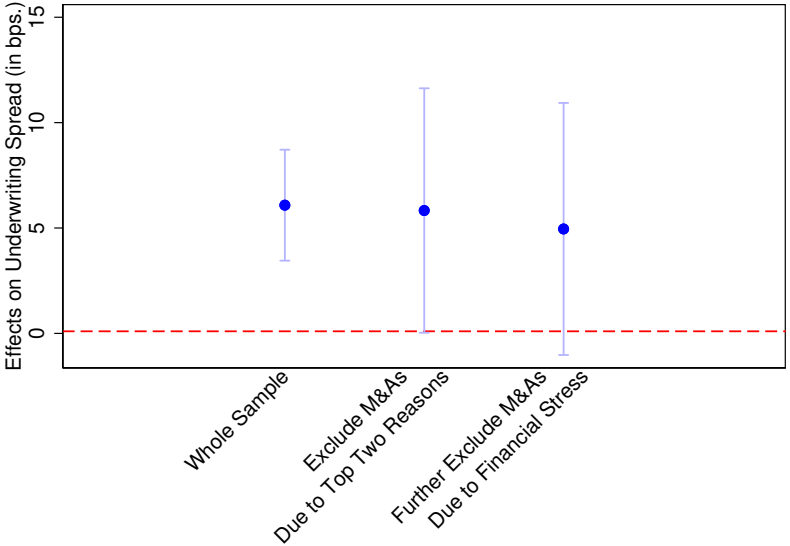
$\Rightarrow$ **Synergy from combining different lines of business**

Main Findings: Addressing Endogeneity Concerns

Reason for M&A	Count
The acquiror's desire to gain local/regional dominance	24
The acquiror's desire to expand geographically	19
The acquiror's desire to gain industry-wide dominance	15
Synergy from combining different lines of business	14
Financial stress of the target	13
Synergy from cost management	12
The acquiror's desire to diversify its revenue sources	12
Acquiror or target's desire to fend off a hostile takeover	1

Table: Top Reasons Behind M&As According to News Reports

Main Findings: Addressing Endogeneity Concerns



Main Findings: Placebo Tests

Effects are absent for

- #1: Cross-market underwriter M&As
  - $\Rightarrow$ Results are not driven by factors that lead to M&A activities of underwriters in general
- #2: Within-market (purely) commercial bank M&As
  - $\Rightarrow$ Results are not driven by factors that lead to within-market consolidation of financial institutions in general
- #3: Within-market withdrawn underwriter M&As
  - $\Rightarrow$ Results are not driven by factors that lead to both successful and withdrawn M&As

Main Findings: Placebo Tests

	Market Share >= 10%		Market Share >= 0%	
	(1)	(2)	(3)	(4)
	Underwriting Spread (bps.)	Underwriting Spread (bps.)	Underwriting Spread (bps.)	Underwriting Spread (bps.)
Treated × Post	-3.01	-0.26	-0.22	1.19
	(-1.36)	(-0.13)	(-0.14)	(0.67)
Observations	33,997	54,052	118,497	113,959
Year FE	Yes	Yes	Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year	CSA & Year
If Similar Population	No	Yes	No	Yes
Adjusted R-squared	0.607	0.608	0.588	0.580

Table: A Placebo Test Using Cross-Market Underwriter M&As

Main Findings: Placebo Tests

Effects are absent for

- #1: Cross-market underwriter M&As
  - $\Rightarrow$ Results are not driven by factors that lead to M&A activities of underwriters in general
- #2: Within-market (purely) commercial bank M&As
  - $\Rightarrow$ Results are not driven by factors that lead to within-market consolidation of financial institutions in general
- #3: Within-market withdrawn underwriter M&As
  - $\Rightarrow$ Results are not driven by factors that lead to both successful and withdrawn M&As

Main Findings: Placebo Tests

Trace out geographic distribution of CBs using Summary of Deposits (Cetorelli and Strahan, 2006; Kundu, Park, and Vats, 2022)

	Predicted $\Delta_{CB\ HHI}$ >= 100	*Predicted* $\Delta_{CB\ HHI}$ >= 50	*Predicted* $\Delta_{CB\ HHI}$ >= 20
	(1)	(2)	(3)
	Underwriting Spread (bps.)	Underwriting Spread (bps.)	Underwriting Spread (bps.)
Treated × Post	1.45	3.76	3.33
	(0.55)	(1.41)	(1.44)
Observations	10,969	15,883	20,014
Year FE	Yes	Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year
Adjusted R-squared	0.521	0.535	0.547

Table: A Placebo Test Using (Purely) Commercial Bank M&As

Main Findings: Placebo Tests

Effects are absent for

- #1: Cross-market underwriter M&As
  - $\Rightarrow$ Results are not driven by factors that lead to M&A activities of underwriters in general
- #2: Within-market (purely) commercial bank M&As
  - $\Rightarrow$ Results are not driven by factors that lead to within-market consolidation of financial institutions in general
- #3: Within-market withdrawn underwriter M&As
  - $\Rightarrow$ Results are not driven by factors that lead to both successful and withdrawn M&As

Main Findings: Placebo Tests

	Predicted Δ_{HHI} >= 50	*Predicted* Δ_{HHI} >= 20	*Predicted* Δ_{HHI} >= 10
	(1)	(2)	(3)
	Underwriting Spread (bps.)	Underwriting Spread (bps.)	Underwriting Spread (bps.)
Treated × Post	-5.80	-9.85	6.02
	(-0.49)	(-1.71)	(0.58)
Observations	129	1,358	3,972
Year FE	Yes	Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year
Adjusted R-squared	0.168	0.471	0.384

Table: A Placebo Test Using Withdrawn Underwriter M&As

Efficiency Gains

- Two major themes of M&A research: Market power and efficiency gains
- Do issuers benefit from efficiency gains that could compensate for the rise in the underwriting spread?

I examine potential efficiency gains on two fronts:

- Lower bond yield?
  - Underwriters might have gain stronger abilities to market and distribute the bonds
  - However, powerful underwriters might instead precipitate higher yield at initial offering under Negotiated Sales Back
- Reduced need for other issuer-paid services?
  - Bond insurance, credit ratings, and financial advisors

Efficiency Gains

Outcome variables:

- Yield at Initial Offering: Yield-to-maturity based on the price at which the underwriter resells the bond to initial investors
  - Mean = 351.0 bps.
- Yield Spread: Spread between municipal bond and U.S. treasury securities at the initial offering
  - Mean = 90.1 bps.
- Initial Underpricing: Day 15-30 trading price minus initial trading price
  - Mean = \$0.4 per \$100 face value

Efficiency Gains

	(1) Yield at Initial Offering (bps.)	(2) Yield Spread over Treasury (bps.)	(3) Yield Spread over Treasury (bps.)	(4) Initial Underpricing	(5) Initial Underpricing
Treated × Post	-4.69	-2.72		0.09**	
	(-0.78)	(-1.14)		(2.61)	
Treated × Post × Competitive Bidding			-5.37		-0.02
			(-1.24)		(-0.30)
Treated × Post × Negotiated Sales			-1.70		0.15***
			(-0.84)		(3.37)
Observations	157,522	143,905	143,905	33,248	33,248
Year FE	Yes	Yes	Yes	Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year	CSA & Year	CSA & Year
Adjusted R-squared	0.693	0.393	0.406	0.131	0.140

Table: Effects of M&As on Offering Terms

Efficiency Gains

Outcome variables:

- If using bond insurance
  - Mean = 18.7%, average cost = 80.4 bps.
- If using credit ratings
  - Mean = 15.4%, average cost = 12.4 bps.
- If using financial advisors
  - Mean = 49.2%, average cost = 49.8 bps.
- I can observe *if* any issue is using these three services, but their costs are only available for California and Texas
  - I predict expected costs for all issues following Cornaggia et al. (2022)

Efficiency Gains

	(1) Has Rating	(2) Insured Ratio	(3) Has Advisor
Treated × Post	-0.02	-0.02	-0.01
	(-1.05)	(-1.03)	(-1.24)
Observations	249,168	249,168	249,168
Year FE	Yes	Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year
Adjusted R-squared	0.401	0.413	0.625

Table: Effects of M&As on the Use of Credit Rating, Insurance, and Financial Advisor

Efficiency Gains

- Total issuing cost = underwriting spread + three kinds of other fees
- "Modified True Interest Cost" accounts for both issuing costs and bond yield at initial offering

	(1) Total Issuing Cost (bps.)	(2) Modified TIC Spread (bps.)
Treated × Post	5.15**	8.22*
	(2.48)	(1.70)
Observations	78,549	55,132
Year FE	Yes	Yes
Issuer × Cohort FE	Yes	Yes
Clustering	CSA & Year	CSA & Year
Adjusted R-squared	0.497	0.410

Table: Effects of M&As on Total Issuing Costs and "Modified True Interest Cost" Spread

Local Government Finances

- Data: The Annual Survey of State and Local Government Finances conducted by the U.S. Census Bureau
- 1,778 counties, 10,233 townships, 14,019 municipalities, and 12,903 school districts from 1970 to 2022
- Motivation:
  - Validate findings from issuance outcomes
  - Fully quantify the total effects of M&As on local government finances
    - Municipal bond issues can have complex features beyond the underwriting spread and yield at initial offering (Brancaccio and Kang, 2023)

Local Government Finances

- Outcome variables:
  - Interest Paid/Total Expenditures ⏩ Interpretation
  - New Issuance/Total Expenditures
  - Surplus Ratio $= \frac{\text{Total Revenue}}{\text{Total Expenditure}} - 1$
- Findings are robust to using per-capita/per-student amounts

Local Government Finances

I estimate

$$y_{l,t,c} = \beta_1 Post_{c,t} + \beta_2 Treated_{a,c} \times Post_{c,t} + \theta_{l,c} + \theta_t + e_{l,t,c},$$

where

- l is the subscript for each local government
- a is the subscript for each Combined Statistical Area (CSA)
- c is the subscript for each cohort of treated and control CSAs
- t is the subscript for the calendar year
- Double-cluster SEs at CSA and year levels

Local Government Finances

VARIABLES	(1) Interest Paid/ Exp. (in %)	(2) New Issuance/ Exp. (in %)	(3) Budget Surplus Ratio (in %)
Treated × Post	0.05	-0.66**	-1.09
	(0.91)	(-2.15)	(-1.47)
Observations	361,463	361,463	361,463
Year FE	Yes	Yes	Yes
Gov. × Cohort FE	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year
Sample Mean	2.56	5.70	1.30

Table: Effects of M&As on Local Government Finances

Local Government Finances

	(1) Interest Paid/ Exp. (in %)	(2) New Issuance/ Exp. (in %)	(3) Budget Surplus/ Exp. (in %)
Panel A: School district			
Treated × Post	−0.02	−1.20***	−0.07
	(−0.53)	(−2.70)	(−0.15)
Panel B: Municipality/township/county			
Treated × Post	0.16*	−0.31	−1.55
	(1.84)	(−1.14)	(−1.48)
Government × Cohort FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year

Table: School District Versus Municipality/Township/County

- School districts: New issuance drops by $178.9 (t = -2.19) and expenditure changes by -$279.7 (t = -1.60) per student
- Municipalities/townships/counties: Interest paid rises by 5.4% of the sample mean

Local Government Finances

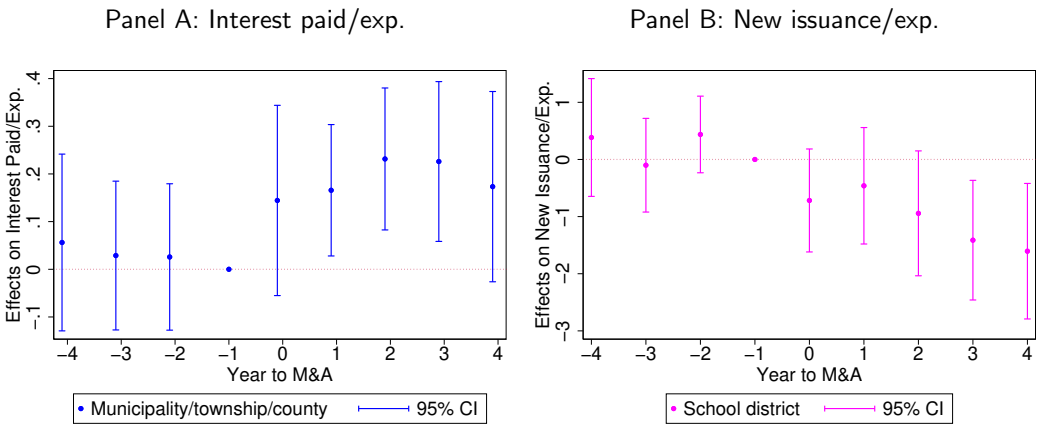


Figure: Effects of M&As on the Local Government Finances

Conclusion

- The underwriting spread for municipal bonds rises after M&As among underwriters
- Cross-sectional heterogeneities are consistent with a market power interpretation
- The effects hold in scenarios where endogeneity concerns are less likely
- Efficiency gains, if any, are insufficient to offset the rise in the underwriting spread
- Census data confirm increased financing costs and show reduced new issuance

- The findings provide a novel perspective on bank antitrust regulations
  - Traditionally limited to deposit-taking and lending activities
  - Investment banking activities should also enter consideration

⏩ More Discussion

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Main Findings: Effects on Underwriting Spread

	(1) Underwriting Spread (bps.)	(2) Underwriting Spread (bps.)	(3) Underwriting Spread (bps.)	(4) Underwriting Spread (bps.)
Treated × Post	5.79*	3.69**	3.91*	5.22***
	(1.98)	(2.32)	(2.00)	(3.21)
Observations	79,552	78,417	57,112	79,642
Year FE			Yes	Yes
Issuer × Cohort FE	Yes	Yes		Yes
State × Year FE	Yes			
Underwriter × Year FE		Yes		
Issuer × Underwriter × Cohort FE			Yes	
Clustering	CSA & Year	CSA & Year	CSA & Year	CSA & Year
Weights	None	None	None	Wing et al. (2024)
Adjusted R-squared	0.540	0.621	0.671	0.553

Table: Robustness Tests to Alternative Regression Specifications, Part I Back

Main Findings: Effects on Underwriting Spread

	(1) Underwriting Spread (bps.)	(2) Underwriting Spread (bps.)	(3) Underwriting Spread (bps.)
Treated × Post	3.84**	4.50***	4.41***
	(2.21)	(2.82)	(2.78)
If Commercial Banks Eligible			-15.92***
			(-8.17)
Observations	79,641	64,664	79,642
Controls		Yes	
Year FE		Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes
Taxable × Year FE	Yes		
Method of Sale × Year FE	Yes		
Source of Repayment × Year FE	Yes		
Clustering	CSA & Year	CSA & Year	CSA & Year
Adjusted R-squared	0.548	0.577	0.533

Table: Robustness Tests to Alternative Regression Specifications, Part II Back

Main Findings: Effects on Underwriting Spread

	(1) Underwriting Spread (bps.)	(2) Underwriting Spread (bps.)	(3) Underwriting Spread (bps.)	(4) Underwriting Spread (bps.)	(5) Underwriting Spread (bps.)
Treated × Post	4.03**	3.84**	3.80***	3.90***	3.36**
	(2.63)	(2.51)	(2.79)	(2.89)	(2.52)
Observations	103,956	123,364	76,104	79,527	1,000,870
Year FE	Yes	Yes	Yes	Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes	Yes	Yes
Clustering	CSA & Year	CSA & Year	CSA & Year	CSA & Year	CSA & Year
Number of Matches	2	3	1	1	Unlimited
Matching Co-variates	Local Income and Population	Local Income and Population	Local Income and Population plus Demographics Dynamics	Local Income and Population plus Issuance Outcomes	None
Adjusted R-squared	0.513	0.511	0.535	0.529	0.537

Table: Robustness Tests to Alternative Matching Back

Main Findings: Effects on Underwriting Spread

	(1) Underwriting Spread (bps.)	(2) Underwriting Spread (bps.)
Treated × Post	4.94	4.31*
	(1.19)	(1.98)
Observations	17,419	70,402
Year FE	Yes	Yes
Issuer × Cohort FE	Yes	Yes
Clustering	CSA & Year	CSA & Year
Number of Matches	1	1
Matching Co-variates	Local Income and Population	Local Income and Population
Restrictions	Treated Once	Requiring No Prior Treatment
Adjusted R-squared	0.492	0.522

Table: Robustness Tests to Addressing Concerns in Baker et al. (2022) Back

Main Findings: Effects on Underwriting Spread

	(1) Underwriting Spread (bps.)	(2) Underwriting Spread (bps.)	(3) Underwriting Spread (bps.)
Treated × Post	7.04***	5.84***	7.71***
	(4.18)	(3.79)	(4.81)
Observations	76,821	125,303	63,450
Year FE	Yes	Yes	Yes
Issuer × Cohort FE	Yes	Yes	Yes
Clustering	CBSA & Year	CBSA & Year	CBSA & Year
Adjusted R-squared	0.536	0.528	0.531

Table: Robustness Tests to Defining Markets at the CBSA Level Back

Main Findings: Addressing Endogeneity Concerns

PNC Bank & Midlantic Bank, 1995

The Morning Call: *"The move, along with PNC Bank's pending acquisition of 84 branches of Chemical Bank New Jersey, will strengthen PNC Bank's position in the New Jersey and Philadelphia markets, placing it second in those areas."*

⇒ **The acquiror's desire to gain local/regional dominance**

Back

Main Findings: Addressing Endogeneity Concerns

RBC Bank & Dain Bosworth, 2000

The Wall Street Journal: *"The acquisition, which is subject to approval by regulators and Dain Rauscher shareholders, would give Royal Bank the toehold it has long sought in the U.S. wealth-management market."*

⇒ **The acquiror's desire to expand geographically**

Back

Main Findings: Addressing Endogeneity Concerns

JP Morgan & Banc One, 2004

The New York Times: *"The merger would create a financial behemoth and a true rival to the world's largest banking company, Citigroup , with $1.1 trillion in assets and 2,300 branches in 17 states."*

⇒ **Acquiror's desire to gain industry-wide dominance**

Back

Main Findings: Addressing Endogeneity Concerns

Morgan Stanley & Dean Witter Reynolds, 1997

The New York Times: *"In recent years, as the securities markets have changed, however, both firms started to covet what the other had. Dean Witter's 9,300 brokers needed more products to sell to the firm's Main Street customers, specifically the initial public offering stocks and municipal bonds that Morgan Stanley frequently underwrites. Morgan Stanley, meanwhile, wanted to broaden its customer base beyond its corporate clients and large institutions to the individual investors who have been flocking to the market."*

⇒ **Synergy from combining different lines of business**

Back

Main Findings: Addressing Endogeneity Concerns

Wells Fargo & First Security, 2000

The New York Times: *"(First Security) operates similar to a savings institution, with a business that is generally weighted toward low-return products like mortgage and car loans. 'The mortgage business has gotten really crushed in this rate environment,' Mr. Ryan (of the research firm Byrne-Ryan) said. 'But Wells Fargo is one of the top operators in the mortgage business and is well positioned to resuscitate First Security.'"*

$\Rightarrow$ **Financial stress of the target (vulnerability to the rate environment)**

Back

Main Findings: Addressing Endogeneity Concerns

Stifel Nicolaus & City Securities, 2016

Indianapolis Business Journal: "*'Post Dodd-Frank, one of the effects that it had on the entire industry was to lay a lot of additional regulatory costs on everybody—probably disproportionately on smaller firms,' Bosway (City Securities CEO Mike Bosway) said. 'So that was clearly a factor in considering this more so than I had in the past. The need for scale today, because of that, is greater than it ever had been.'*"

⇒ **Synergy from cost management**

Back

Main Findings: Addressing Endogeneity Concerns

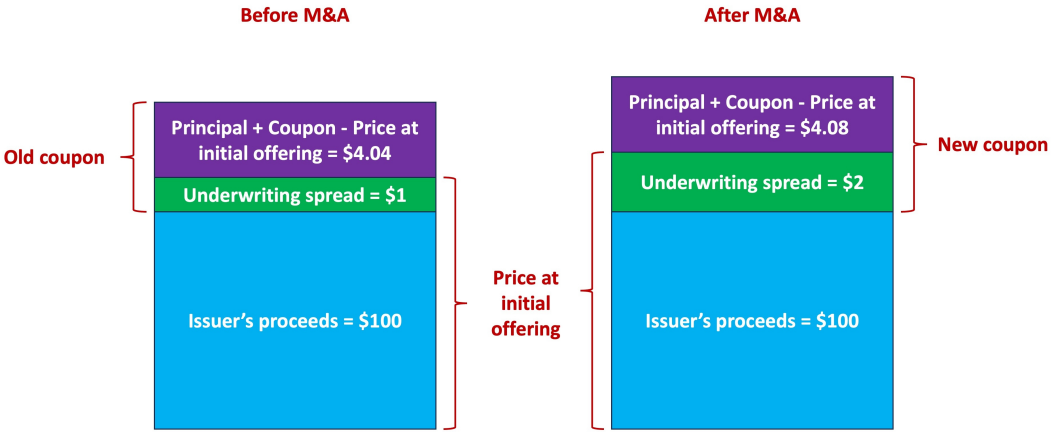
Capital One Financial & North Fork Bank, 2008

The New York Times: *"'With North Fork, Capital One will be more balanced and more diversified and my growth prospects will be enhanced,' Mr. Fairbank said during a conference call today with investors and analysts. 'That is a very important milestone in a journey that started many years ago.'"*

⇒ **Acquiror's desire to diversify its revenue sources**

Back

Local Government Finances



- "Interest paid" reflects coupon amount rather than yield at initial offering

Back

Discussion

- My findings echo research on market power in corporate securities underwriting
  - Staffs in corporations might have more effective financial training
  - However, potential collusive benefits per deal is greater for corporate securities
  - I call for future research building on the contribution of Chen and Ritter (2000) and Manconi et al. (2019)
- My findings are not at odds with the secular trend in underwriting spread
  - In a counterfactual absent consolidation, the underwriting spread would be lower
- My findings are not at odds with internal efficiency gains from M&As

Discussion


FINANCIAL TIMES

myFT

US + Add to myFT

OECD criticises high fees and tacit collusion in IPO underwriting

Costs for European issues about half that paid by US and Japanese companies

OECD:

- "*(For corporate IPOs,) high levels of fees and parallel pricing (akin to tacit collusion) appear to have increased (in recent years)*"
- This could have contributed to the "*decline in the number of companies tapping the public equity markets over the past decade*"

Discussion

- My findings echo research on market power in corporate securities underwriting
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  - However, potential collusive benefits per deal is greater for corporate securities
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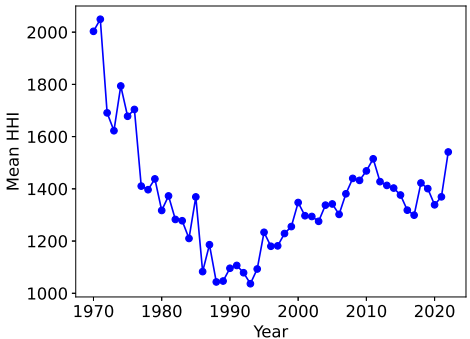
Local Government Finances

Panel A: HHI



Panel B: Underwriting spread

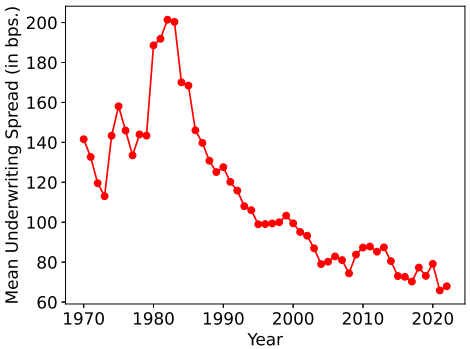


Figure: Time trends, 1970-2022

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