

Joint Seminar - Risk Management Institute And Department of Mathematics

Details of Seminar

Date: 29 December 2008, Monday

Time: 3:00pm – 4:00pm

Venue: Colloquium Room A (S14, #03-10)

Speaker

Prof. Wang Hefei

University of Illinois, Chicago

Title

Leverage Management

Abstract

Leverage has often aggravated losses to managed investments. The recent collapses of hedge funds and investment banks heightened concerns over the risks associated with high leverage. Indeed, policy debates about the implications of hedge fund operations for systemic stability and market integrity revolves around their use of leverage. Research on optimal leverage in the money management industry, however, is relatively scarce. In this paper, we provide a theoretical analysis of a fund's dynamic leverage policy. We study portfolio transactions of an asset manager who trades off the benefits of higher leverage against the costs of adjusting leverage in order to mitigate expected insolvency losses. We characterize the implications of liquidation costs and asset-management fee incentives for the optimal management of leverage.