ABSTRACT

This research analyzes various aspects of insider trading in India. This thesis can be divided into three parts: first part analyzes insider trading around earnings announcements, the second part addresses the effect of insider trading on stock characteristics like price, return and volume and the third part investigates if corporate governance affects insider trading.

In the first part a modified event study method is introduced. In this method variable event window is used rather than a fixed event window and each event window starts from the day the insider trades. Using this modified event study method, it is explored whether insiders earn abnormal return by trading before earning announcements and whether outside investors can earn abnormal return by mimicking those insider trades. It is also examined whether the abnormal return differs with type of insider. It is found that insiders earn abnormal return from purchases but suffer loss from sales. Directors and executives earn abnormal return from purchases but promoters do not earn abnormal return. These insights would go undetected if standard event study methods were employed. Outsider investors can earn abnormal return by mimicking purchases of directors and executives. Finally, it is observed that abnormal return depends on firm earnings, market capitalization, opportune number of days and type of insider transaction.

The second part documents the effect of insider trading on stock characteristics like price, return and volume, using the event-study method. A novel method is proposed to measure abnormal price. It is found that insider trades affect price, return and volume. The results are identical for both buy and sell transactions. It is also found that stock characteristics react differently to trades of different types of insiders. Further, it is observed that return and volume get affected earlier than price. It is also identified that abnormal return and abnormal volume do not affect each other.

The third part of the thesis seeks to establish the relationship between corporate governance and insider trading by investigating corporate governance’s impact on the probability of insider trading, abnormal return and abnormal volume. A corporate governance index is constructed to study the overall impact of corporate governance. Cox regression for recurrent events is used to analyze the impact of corporate governance index and corporate governance variables on the probability of insider trading. Two-stage least square regression is used to investigate if the corporate governance index affects cumulative abnormal return and cumulative abnormal volume around insider trades. The results indicate that the corporate governance index does not affect the probability of insider trading, abnormal returns and abnormal volumes. Some of the corporate governance variables affect the probability of insider trading positively and some negatively.

Keywords: *insider trading, abnormal return, modified event study method, mimicking, earnings announcement, stock characteristics, corporate governance, cox regression, two-stage least square regression, probability of insider trading.*