Synopsis Seminar

Seminar Title	: Studying Indian Corporate Hedging Behavior through the Lens of Prospect Theory
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Abstract

: Corporate risk management has evolved as a significant and inseparable part of the management of organizations in the last few years. Almost all organizations undertake hedging and risk management activities to deal with the different types of risks or exposures they face. Moreover, the series of various financial and economic crises has motivated organizations to revisit and modify their risk management rituals. There were several theories related to the concept of risk management and its different aspects, and many researchers tried to confirm the theories with the actual risk management activities throughout the literature. As per the theory given by Modigliani and Miller (1958), risk management activities do not really matter for an organization or are ineffective. In contrast, the theory of Smith and Stulz (1985) shows that risk management activities are actually valuable and can improve the overall performance of an organization. In fact, many researchers tested both empirically and theoretically and revealed that risk management activities can add value to the firm in the presence of imperfect capital market conditions. Such conditions may include information asymmetry, financial distress due to a high debt proportion in the capital structure, presence of taxation system, transaction costs, etc.

This thesis has gone over the unanswered questions from the inconclusive literature once again and attempted to address the numerous additional factors that could influence a company's hedging practices. The thesis examines all non-financial companies listed on the Indian National Stock Exchange and the Bombay Stock Exchange, covering the years 2016 to 2023. The study investigates the financial determinants of hedging based on the available data and finds that size, R&D, leverage, profitability, and managerial ownership are the key variables influencing hedging practices in India. This thesis makes a significant theoretical and empirical contribution by examining the influence of the well-known behavioral theory known as "The Prospect Theory" on the explanation of firms' hedging practices. We look for explanations from prospect theory to help us understand the perplexing impact of hedging on firm value. We propose that hedging practices and the relationship between hedging and firm value are influenced by a reference point. The impact of prospect theory on firms' hedging activities is confirmed by our empirical analysis. When managers are in the more profitable/gain domain, we observe that they have a risk-averse mindset in the less profitable/loss domain, on the other hand, they exhibit a risk-seeking perspective. Concerning the relationship between hedging and firm value, the findings revealed that though hedging has positive impact on the firm value, it was visible that the positive effect is more significant in the higher quartile domain.

The study also attempted to identify additional circumstances in which hedging provides value, and it found that smaller hedging companies benefit more than larger ones, and that hedgers benefit more during times of crisis than during non-crisis periods. Furthermore, it was found that hedgers who have smaller exposures to foreign markets benefit more than those who have larger exposures.