Chapter 16
Insider Transactions and Performance:
The Portuguese Case

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ABSTRACT

This study investigates the relevance of stock buy/sell transactions by insiders in Portuguese companies' performance. To achieve this aim, the sample covers the period from 2013 to 2017. The data from buy/sell transactions by insiders were collected in the internal transaction reports delivered by the companies to the Portuguese Securities Market Commission for the same time interval. The results, using panel data methodology, suggest a negative relationship between the long/short positions and the companies' performance, although the volume traded is not significant. Therefore, the increased control of Portuguese companies by their managers signals the existence of conflicts of interest of the managers, whether due to financial reasons or to strengthen their continuity in the position. As far as the authors are aware, this is the first time that a study has been carried out using insider transactions for Portuguese companies and their influence on corporate performance.

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INTRODUCTION

The abuse of privileged information is an almost unexplored topic in Portugal and this was the main motivation for carrying out this work. Portuguese law prohibits the improper transmission and use of this information to improve investor confidence in the functioning of the market. However, these situations still prevail, and we feel an increased motivation to work on this topic in a country where the market benchmark consists of only 18 companies, with very little liquidity and little international recognition.

We all know the power of information in terms of its influence on the economic performance of companies. Fama (1970) suggests that the efficient market theory is closely related to information and the market price, and it proposes that the market as a whole is efficient concerning information, that is, the prices of assets reflect the information available.

Thus, investors who are theoretically rational and have access to all existing information, will not be able to obtain abnormal returns above the market average. For example, Clarke, Dunbar & Kahle (2001) argue that insiders exploit windows of opportunity by attempting to issue overvalued equity and by canceling the issue when the market reaction to the announcement eliminates the overvaluation. In another point of view Collin-Dufresne and Fos (2015) also studied the problem of insider trading and concluded that when informed traders can select when and how to trade, standard adverse selection measures may fail to capture the presence of informed trading and consequently change prices and performance.

However, there is no consensus in the literature among the authors regarding the impact of the use of information, as well as insider information, on corporate performance.

This article tends to contribute to recent studies in the literature, which seek to define factors that may be significant in the performance of companies, among them, the use of privileged information for stock purchase/sale operations, insider trading, by their managers. Such performance was evaluated based on the accounting indicator Return On Assets, ROA, given some financial indicators, such as liquidity, level of financial leverage, operating expenses, and company size. For example, exploring the fact that insiders trade for a variety of reasons, Cohen, Malloy, & Pomorski (2012) show that routine trading is predictable and identifiable, with inside information but that may not be informative about the future of companies. This may imply that the effects are current and that our measure of performance may be adequate.

Portugal is an embryonic market, not very liquid, where the benchmark consists of only 18 companies. This is an underexplored market, namely in these issues of risk and performance inherent to the misuse of private information.

Given this scenario, in addition to investigating the effect of corporate performance metrics, this work also aims to research the impact of transactions carried out by insiders and their respective volumes on the performance of non-financial companies listed on the PSI-20 index during the years of 2013 to 2017. The results obtained after estimating the model with panel data show that insiders can have a negative impact on corporate performance, through their share purchase/sale transactions, however, the volume of shares traded was not shown significant.

This study is organized as follows: Section 2 presents the literature review, with some of the indicators that are most used to determine the companies performance. In addition to formulating the hypotheses, this section also presents other variables, since we believe that these variables complement our investigation. Section 3 presents the research design, database, and sample construction, as well as the estimation method used. Section 4 sets out the results and respective analyzes, finally, the conclusions of the authors, limitations of the study, and points for future studies are covered in section 5.