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Sequential Warrant Exercise in Large Trader Economies

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Tobias Linder (https://papers.ssrn.com/sol3/cf_dev/AbsByAuth.cfm?per_id=351003)

University of Mainz

Siegfried Trautmann (https://papers.ssrn.com/sol3/cf_dev/AbsByAuth.cfm?per_id=152554)

Johannes Gutenberg University Mainz - Faculty of Law and Economics

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Abstract

It is well known that the sequential (premature) exercise of American-type warrants "may" be advantageous for large warrantholders, even in the absence of regular dividends, because using exercise proceeds to expand the firm's scale increases the riskiness of an equity share. We present sufficient conditions for the non-optimality of sequential exercise implying that for realistic interest rate levels even large warrantholders are better off not to exercise long before maturity. This result, however, does not justify in general the simplifying restriction that warrants or convertible securities are valued as if exercised as a block.

Keywords: Warrants, Large Trader, Sequential Exercise, Partial Exercise Option

JEL Classification: C72, G12, G13, G32

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