

Issuers' credit risk and pricing of warrants in the recent financial crisis

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Purpose

- The purpose of this paper is to investigate whether factor sensitivities of margins of bank-issued warrants depend on issuers' credit risk during the period of economic turmoil between January 2008 and June 2010.

Design/methodology/approach

- Therefore, first, Fama–MacBeth estimations were applied and it was demonstrate that the sensitivities of margins in terms of time to maturity and moneyness vary substantially over time; the average outcomes are similar to the results of classical pooled estimations.

Findings

- Then, time-series tests were used and it was found that the steepness of the issuers' credit default swap (CDS) spread curves correlates negatively with the time-to-maturity sensitivities as well as with the explanatory power of Fama–MacBeth estimations.

Research limitations/implications

- These findings indicate that the life-cycle hypothesis is weakened when the issuers' CDS spread curves become steeper.

Originality/value

- Thus, this study offers a new approach to gain insights into the role of issuers' credit risk on price setting behavior.

Keywords: [Crisis](#), [Credit spread curve](#), [Fama–MacBeth estimations](#), [Warrants](#)

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