

Overview

List of Tables	XV
List of Figures	XVII
List of Abbreviations	XIX
1 Introduction.....	1
1.1 Background and Objective	1
1.2 Organization of the Dissertation	3
2 Literature Review	7
2.1 Fundamentals of Asset Pricing Theory	7
2.2 Cross Section of Equity Returns.....	25
2.3 Real Estate Risk as a Priced Factor	38
2.4 Summary and Implications	45
3 Estimation Methodology	47
3.1 ICAPM Framework	47
3.2 VAR approach	48
3.3 Asset Pricing Tests	49
3.4 Summary	63
4 Data	65
4.1 State Variables of Interest	65
4.2 Test Assets	70
5 Empirical Analysis.....	73
5.1 Derivation of an Alternative ICAPM	73
5.2 Testing the Alternative ICAPM.....	89
5.3 Further Investigations	110
6 Conclusion	149
Appendix	151
References	153

Table of Contents

List of Tables	XV
List of Figures	XVII
List of Abbreviations	XIX
1 Introduction.....	1
1.1 Background and Objective	1
1.2 Organization of the Dissertation.....	3
2 Literature Review	7
2.1 Fundamentals of Asset Pricing Theory	7
2.1.1 Capital Asset Pricing Model.....	7
2.1.2 Intertemporal Capital Asset Pricing Model.....	12
2.1.3 Arbitrage Pricing Theory.....	18
2.1.4 Summary	25
2.2 Cross Section of Equity Returns.....	25
2.2.1 Empirical Evidence	26
2.2.1.1 U.S. Stock Returns	26
2.2.1.2 International Evidence.....	28
2.2.2 Potential Explanations.....	28
2.2.2.1 Data-Based Explanations	29
2.2.2.1.1 Data-Snooping Argument.....	29
2.2.2.1.2 Bad-Market-Proxy Argument.....	30
2.2.2.2 Risk-Based Explanations.....	30
2.2.2.3 Non-Risk-Based Explanations	32
2.2.3 Search For a Coherent Rational-Pricing Story.....	35
2.3 Real Estate Risk as a Priced Factor	38
2.3.1 Impact of Real Estate Risk on the Real Economy.....	38
2.3.1.1 Collateral Channel.....	39
2.3.1.2 Lending Channel	40
2.3.1.3 Housing Channel	41
2.3.1.4 Discussion	42
2.3.2 Impact of Real Estate Risk on Firm-Level Risk.....	42

2.3.2.1	Real Estate Risk and Firms' Exposure to the Macroeconomy	43
2.3.2.2	Real Estate Risk and Firms' Cash Flow Maturities	43
2.3.3	Discussion	45
2.4	Summary and Implications	45
3	Estimation Methodology	47
3.1	ICAPM Framework	47
3.2	VAR approach	48
3.3	Asset Pricing Tests	49
3.3.1	Traditional Beta Method	49
3.3.1.1	Pricing Framework	49
3.3.1.2	Fama-MacBeth Method	51
3.3.1.3	Tests on Model Evaluation	54
3.3.2	Stochastic Discount Factor Method	55
3.3.2.1	Pricing Framework	55
3.3.2.2	Generalized Method of Moments	57
3.3.2.3	Tests on Model Evaluation	59
3.3.3	Discussion	61
3.4	Summary	63
4	Data	65
4.1	State Variables of Interest	65
4.1.1	Real Estate Factor	65
4.1.2	Fama-French Factors	67
4.1.3	Petkova Factors	68
4.2	Test Assets	70
5	Empirical Analysis	73
5.1	Derivation of an Alternative ICAPM	73
5.1.1	Time Variation in Expected Market Returns	74
5.1.2	VAR Estimation	76
5.1.3	Derivation of Risk Factors	79
5.1.4	Preliminary Cross-sectional Results	84

5.1.5	Summary	88
5.2	Testing the Alternative ICAPM.....	89
5.2.1	Descriptive Statistics	89
5.2.1.1	Risk Factors.....	89
5.2.1.2	Test Assets.....	91
5.2.2	Fama-MacBeth Method.....	91
5.2.2.1	First Stage: The Pattern of the Factor Loadings.....	92
5.2.2.2	Second Stage: The Risk Premiums	98
5.2.2.3	Fitted Versus Realized Returns	101
5.2.3	Stochastic Discount Factor Method	103
5.2.3.1	GMM Estimations.....	103
5.2.3.2	Magnitude of Pricing Errors.....	107
5.2.4	Summary	107
5.3	Further Investigations.....	110
5.3.1	Variations in Test Assets.....	110
5.3.1.1	Managed Portfolios	110
5.3.1.2	Industry Portfolios.....	115
5.3.2	Variations in Variables.....	120
5.3.2.1	Role of Portfolio Characteristics.....	120
5.3.2.2	Role of Conditioning Information.....	123
5.3.2.3	Relationship between Distress Risk and the Real Estate Factor.....	127
5.3.2.4	Relationship between GDP Growth and the Real Estate Factor.....	131
5.3.3	Variations in the Real Estate Factor.....	135
5.3.3.1	Innovations in Equity REITs.....	136
5.3.3.1.1	VAR Estimation	136
5.3.3.1.2	Pricing the Cross Section	137
5.3.3.2	Orthogonalized Composite REITs	140
5.3.4	Summary	144
6	Conclusion	149
	Appendix.....	151
	References	153