**Moral Hazard with Excess Returns**

***Matthias Blonski***

***Joint with*** *Ulf von Lilienfeld-Toal*

**Abstract:**

We consider a public firm characterized by a moral hazard problem.

A distinguished player is a CEO or activist shareholder who (i) is unrestricted to trade shares and (ii) has discretion to increase the value of this firm by exerting costly effort.

Von Lilienfeld-Toal and Rünzi (2014) investigate and confirm the empirical relevance of both these properties.

This article shows that a distinguished player cannot be "priced in" correctly.

In particular, such a firm is traded at a discount below its equilibrium value in a market equilibrium.

Buyers can systematically earn excess returns on their investment.

This prediction is indeed consistent with substantial positive abnormal returns for distinguished player firms within the S&P500 and S&P1500 sample reported in von Lilienfeld-Toal and Rünzi (2014).