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Characteristics of Norwegian Rights Issues

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Abstract

In this paper we study Norwegian rights issues with focus on the announcement effects of raising seasoned equity. The abnormal returns at announcement in Norway are around −8% to −10% for rights issues, and this is much higher than what is found in other countries. The average book-to-market and debt-to-assets ratios are lower for companies that issue equity with other SEO types than with rights issues. This indicates that firms using rights issues are less able to time the equity issuance than the firms that use other SEO types. In addition, the listed rights lose on average around 30% of their value during the offer period.

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1 Introduction

From 1998 to 2010 the stock price effect of announcing a rights issue is on average between -8% to -10% (three-day effects). These indirect costs are considerable compared to other international studies that report announcement effects from between 1% to -4%. Understanding the announcement effect of Norwegian SEOs is important since these costs will affect both new and current shareholders.

Internationally, there are differences in the announcement effect between countries. When companies in the US issue capital with uninsured rights and standby rights the abnormal return is -0.59% and -1.33% respectively (Eckbo et al., 2007). In Europe, uninsured rights have on average positive abnormal returns (0.70%) while standby rights have negative abnormal returns (-1.32%). Due to the fact that European companies use more rights issues than US companies, researchers are interested in why European companies choose rights issues. In Norway, Bøhren et al. (1996) investigated SEO announcement effects using data from 1980 to 1996. Uninsured rights (1.55%) and private placements (1.39%) have positive abnormal returns. Standby rights (-0.58%) had negative abnormal returns.

This paper studies the properties of rights issues in Norway with focus on announcement effects. We also show underpricing and some accounting ratios. The book-to-market and debt-to-assets ratios are much lower for companies that use private placements than for rights issues, suggesting that firms on average prefer other SEO types when selling seasoned equity. Last, we consider the average development of listed rights. These listed rights lose around 30% of their original value during the two weeks of offering.

The remainder of this paper is organized as follows: data are explained in Section 2, characteristics are shown in Section 3, and Section 4 concludes.

2 Data

We use a database of Norwegian SEOs collected from webpages of the Oslo Stock Exchange. The Oslo Stock Exchange database contains equity issues from 1980 to the present. The database only distinguishes between right issues and private placements. Throughout this paper, the private placement is therefore defined as firm commitments (bought deals, accelerated bookbuilt and fully marketed offerings) and cash placements if nothing else is specified. The data from Oslo Stock Exchange do not contain information about syndication (i.e. if the rights issue is uninsured or is standby rights), but we know from other sources that most of the equity issues are guaranteed. This dataset does not include the announcement dates of the SEO announcement. Hence, the press releases from the Oslo Stock Exchange are used to find this date manually for SEOs from 1998

to 2010. In addition we use a historical source of press releases[1] that covers the period between 1992 and 1998. Table 1 lists all the observations identified with an announcement date.

Table 1: Number of right issues and private placements

Using the Oslo Stock Exchange register of SEOs, this table shows the number of right issues and private placements that we have identified with an announcement date in each year from 1992 to 2010. The announcement date is found by going through press releases from the Exchange. The private placements also include accelerated bookbuild, bought and fully marketed deals because the register does not split between the SEO types except for rights issues.

Years	Rights issues	Private placements	Sum All
1992	11	8	19
1993	6	20	26
1994	7	13	20
1995	9	33	42
1996	12	129	141
1997	19	270	289
1998	13	134	147
1999	33	293	326
2000	21	364	385
2001	19	163	182
2002	17	131	148
2003	22	78	100
2004	14	124	138
2005	11	211	222
2006	15	142	157
2007	22	159	181
2008	20	50	70
2009	37	70	107
2010	12	43	55
Total	320	2435	2755

[1]Many press releases are missing in this source. Thanks goes to Bernt Arne Ødegaard for providing us with this database.

3 Right issue characteristics

In this section, we first discuss underpricing, next the book-to-market and debt-to-assets ratios of companies issuing rights, thereafter we show the announcement effects, and finally the average development of listed rights is presented.

3.1 Book-to-market and debt-to-assets ratios

As Table 2 shows, there are some changes in the book-to-market and debt-to-assets ratios for companies issuing seasoned equity. Firms that issue rights issues have no significant change in their book-to-market value, but when using private placements firms have a significant negative book-to-market ratio change after the issue when using other SEO types than rights. Rights offering firms have a higher book-to-market value compared to companies that use other SEO types. On average, all SEO companies experience significantly lower debt-to-assets ratios after the issue. The debt level is higher for firms issuing rights than for firms choosing different SEO types.

Table 2: Accounting variables before and after SEO

The table shows the means, standard deviations and observations of book-to-market and debt-to-assets and after the rights issue and private placements. Book-to-market and debt-to-assets are reported at year end, but the ownership variable is reported each month. T-tests are performed to see if the means are significantly different. Private placements include accelerated bookbuilt offerings, bought deals and fully marketed offerings. Data are from the Oslo Stock Exchange.

		Before		After		Both	
Description	Type	Mean	St.dev.	Mean	St.dev.	Obs	t-test
Book-to-,arket	Rights issues	0.98	0.35	1.03	0.39	175	-1.19
	Private placements	0.83	0.77	0.71	0.53	55	2.90
Debt-to-assets	Rights issues	0.46	0.13	0.42	0.12	164	2.67
	Private placements	0.37	0.20	0.32	0.18	164	2.33

3.2 Underpricing

Norwegian underpricing for rights issues is quite similar to other European countries for all SEO types with some small differences (Krakstad and Molnár, 2014). Table 3 shows the annual underpricing, which is on average of around 20%. Companies in different industry sectors on Oslo Stock Exchange have roughly the same underpricing when they choose to issue equity using rights.[2]

Table 3: Underpricing in rights issues and private placements

Using the SEO register from the Oslo Stock Exchange, the table shows the underpricing for rights issues and private placements per year between 1992 to 2010. Rights issue underpricing = (issue price - price the day before announcement(P))/P. Private placement underpricing = (issue price (if not listed, the price the day before announcement)-price 25 trading days before announcement(P25)/P25. The announcement date is found by going through the Oslo Stock Exchange press releases.
* to take account for errors in the sample, observations which are not in the interval, [-70%,+20%], are excluded.

	Rights issue		Private placement	
Year	All	All*	All	All*
1992	-20.5%	-15.2%	-9.7%	-20.0%
1993	-6.2%	-10.8%	-0.9%	4.3%
1994	-27.5%	-34.2%	-9.4%	-11.4%
1995	-22.1%	-21.5%	0.7%	-0.4%
1996	-13.2%	-9.7%	- 2.0%	-3.7%
1997	-17.8%	-16.5%	-0.4%	-2.1%
1998	-16.8%	-16.8%	-8.6%	-0.5%
1999	-22.8%	-18.6%	-5.0%	-5.0%
2000	-18.4%	-16.0%	-6.3%	-6.6%
2001	-29.0%	-14.3%	-9.0%	-14.0%
2002	-20.1%	-15.4%	-7.7%	-6.0%
2003	-15.5%	-16.9%	-4.1%	4.6%
2004	-18.6%	-22.2%	-8.9%	-5.4%
2005	-17.6%	-17.6%	-10.6%	-3.7%
2006	-13.5%	-13.5%	-3.0%	0.2%
2007	-16.0%	-18.0%	-3.7%	-2.8%
2008	-24.7%	-25.1%	-8.6%	-6.2%
2009	-33.9%	-31.7%	-8.0%	-9.6%
2010	-43.0%	-39.5%	-11.1%	-5.7%
Average	-20.9%	-19.7%	-6.1%	-5.0%

3.3 Announcement effects in Norway

An event study for the Norwegian market is performed to quantify the announcement effects. The standard hypothesis to be tested is that there are no abnormal returns (strong market efficiency: all information including private information should be reflected in the stock price). In the Pecking Order Theory, raising equity is seen as the last resort. According to this theory, we would expect that the cumulated abnormal returns should be negative.

We estimate the announcement effects by calculating abnormal returns from the market model. In the literature, an event window of two- or three-days is common to use. However, ± 1 to 30 trading day windows are chosen in this paper to take account for all the announcement effects (see Figure 1). The drawback with a longer window is that other effects are often included.

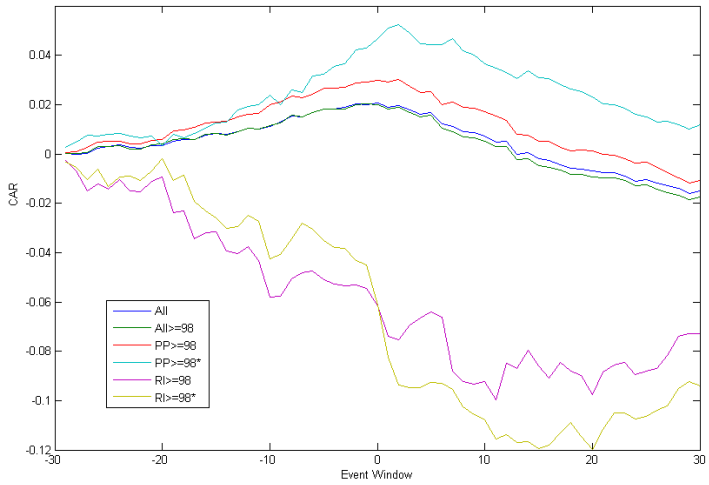

Figure 1: Announcement effects of Norwegian SEOs

The figure presents the cumulated abnormal stock returns (CAR) calculated from the market model for ± 30 trading days for rights issues and private placements. The Oslo Stock Exchange's register of SEOs has been used to identify the observations. The announcement dates are found by using press releases from the Oslo Stock Exchange. There are 6 lines in the figure; the first line, All, calculates CAR by using all the data. The next five lines use only data from 1998 (noted as > 98). In addition the figure distinguishes between rights issue (RI) and private placement (PP). *If the percentage of new equity (new shares divided by old shares) raised is below 5% or above 95%, these events are excluded.

[2]Due to space limitation, the overview for different industries is not included in this paper, but are available upon request.

Table 4: Announcement effects of SEOs in the Norwegian capital market

This table lists the results of an event study performed on Norwegian SEO data. The Oslo Stock Exchange's register of SEOs has been used to identify the observations. The announcement dates are found by using press releases from the Oslo Stock Exchange. The table shows the cumulative abnormal return (by the market model). Two periods are used. The first period is from 1992 to 2010, and the second period is from 1998 to 2010. J1 is the test statistics (typically used in event studies). Obs = number of observations.
* All observation that are larger (less) than 95 (5) percent of new equity issued (new equity/old equity), are excluded.

		All		Private placment		Rights issues	
	Time(t)	All	t ≥ 1998	t ≥ 1998	t ≥ 1998*	t ≥ 1998	t ≥ 1998*
	CAR	-0.02	-0.02	-0.01	0.01	-0.08	-0.10
±1	J1	-1.77	-1.81	-1.13	0.31	-1.86	-4.01
	OBS	1934	1729	1543	412	186	133
	CAR	-0.02	-0.02	-0.01	0.00	-0.08	-0.10
±3	J1	-1.78	-1.89	-1.19	0.00	-1.91	-3.80
	OBS	1935	1730	1544	411	186	133
	CAR	-0.02	-0.02	-0.02	-0.00	-0.08	-0.10
±5	J1	-1.81	-1.92	-1.31	-0.13	-1.73	-3.82
	OBS	1932	1729	1543	411	186	133
	CAR	-0.02	-0.02	-0.02	-0.01	-0.07	-0.08
±10	J1	-1.67	-1.82	-1.37	-0.21	-1.37	-2.71
	OBS	1924	1724	1538	410	186	133
	CAR	-0.03	-0.03	-0.02	-0.02	-0.13	-0.08
±20	J1	-2.15	-2.38	-1.55	-0.63	-2.31	-2.47
	OBS	1904	1707	1519	402	188	133
	CAR	-0.05	-0.05	-0.04	-0.03	-0.18	-0.15
±30	J1	-2.99	-3.27	-2.23	-0.79	-2.98	-4.07
	OBS	1880	1688	1506	397	182	131

Figure 1 illustrates that the announcement effects for rights issues are between −7% and −10% depending on how long the event window is. Table 4 shows a strong significant CAR when companies announce that they are going to raise equity with rights. This large effect is surprising when compared to international seasoned equity issues. The market reaction for US rights issues in a three-day window is around −1.66% (Eckbo et al., 2007). In Japan the reaction is 2.21% (Kang and Stulz, 1996), and in Sweden the reaction is 0.72%, but not significant (Cronqvist and Nilsson, 2005). In France, Hong Kong and the UK the reactions are significantly negative. Gajewski and Ginglinger (2002) find that it is −0.74% in France, Slovin et al. (2000) find −2.9% in the UK, and in Hong Kong the effect is −3.37% (Wu and Wang, 2006). Bahnemann (2008) finds in the period between 2000 and 2008 that announcement effects for rights issues are −2.51% in the UK, −0.67% in Germany and −2.51% in Switzerland. In China, between 1998 and 2008 the abnormal returns are −1.36% (Shahid et al., 2010). Owen and Suchard (2008) find that the abnormal returns are 6.41% in an 11-day window. Eckbo and Norli (2004) report −0.58% (insignificant) in Norway between 1980 and 1996. It is puzzling that the abnormal returns have decreased as much as we find in our paper compared to what other researchers have found. One of the reasons could be the relatively larger shares of smaller companies than in their samples. Another reason could be that more recent data have made it easier to determine the announcement day.

Figure 1 indicates that the CAR for private placements are not significantly different from zero for the 61-day window. In other countries the announcement effects of private placements are significant and positive in the three-day window. Positive and significant abnormal returns of 2.45% are found in the US (Eckbo et al., 2007), 2.21% in the UK (Slovin et al., 2000), 7.27% in Sweden (Cronqvist and Nilsson, 2005), 1.97% in Hong Kong (Kang and Stulz, 1996) and 3.88% in Japan (Wu and Wang, 2006). Eckbo and Norli (2004) find in Norway in the period between 1980 and 1996 that the abnormal returns are 1.39%, but they are not significant. One of the reasons for the seemingly zero effect in our sample, could be that private placements include firm commitment offerings while the Oslo Stock Exchange only distinguishes between rights issues and other issues.

3.4 Rights price development

In a rights issue offering, the current stockholders receive rights such that their company share is not diluted. Compared to firm commitments and cash placements, the current stockholder does not lose value because they get the option to buy the discounted stocks. However, we find that the average rights prices tend to fall 30% during the 2-week offer period. Our dataset for rights prices is 280 observations at the Oslo Stock Exchange in the period between 1990 and 2010. Figure 2 shows the development of 220 rights issues. Here, 60 rights are excluded because they do not meet the following criteria: $9 \leq$ number of days traded ≤ 11 and the rights price cannot increase by more than 1000%. The graph clearly indicates that the optimal trading strategy is to sell the rights on day 1. The value has declined roughly by 30%.

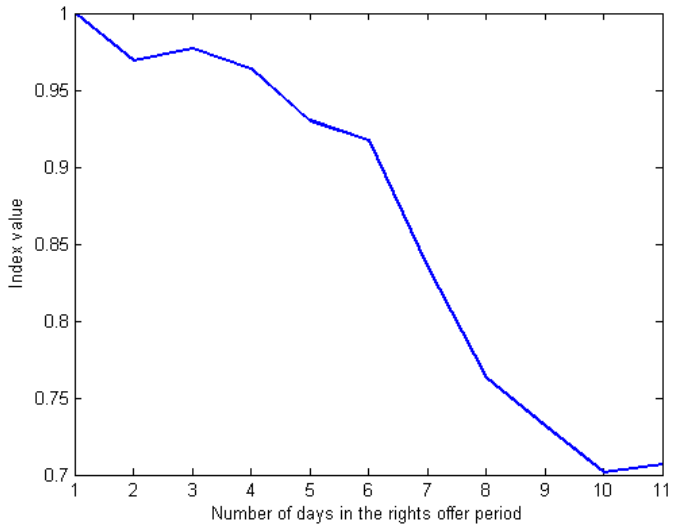

Figure 2: Rights price development

This figure shows the average development for 220 daily rights at the Oslo Stock Exchange from 1990 to 2010. All rights prices have been normalized to be equal 1 at time 1. The index value equals the average of all normalized prices. The change in this value is equal to average development of all normalized prices.

4 Conclusion

This paper describes some characteristics of rights offerings in Norway. The cumulated abnormal returns for announcing new rights issues are around -7% to -10% which is quite high compared to the announcement effects in other countries. Hence, companies should think about these large costs when they are planning a rights issue. If the costs are so high, old investors would be better off by not accepting a new equity increase if the companies could get other refinancing. Underpricing is roughly around 20% in the period between 1992 and 2010. Book-to-market and debt-to-assets ratios are higher for firms issuing rights than firms using other SEO types. It is also found that on average, it is much better to sell the listed rights when they are received, because they lose around 30% of their value within the last day of the offer period.

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