MARKET IMPACT OF COVID-19 TO ANNOUNCEMENTS OF CANADIAN EQUITY OFFERINGS

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ABSTRACT

Did COVID-19 period (March 11, 2020 – Nov. 29, 2021) have differential impact on the market reaction of Canadian bought deal seasoned equity offering announcements compared with pre-COVID-19 period (Jan.13, 2012- March 10, 2020)? How did expected determinants of equity offers affect the market reaction in COVID-19 period compared with pre-pandemic period? Using univariate and multivariate analysis, this study shows no significant difference on the market reaction between pre- and COVID-19 periods. On the other hand, results show determinants have more significant effect on market reaction in the COVID-19 period than in the pre-pandemic period, which was mostly insignificant. For example, in COVID-19 period, offers with favorable market effect are those from health care companies, and those which intended uses of funds are capital investments, debt decrease, and exploration or development. Similarly, positive effect occurs for offers audited by the Big 4 accounting firms, and those sold by existing shareholders (not capital raising) among others. Surprisingly, stock market volatility had favorable market effect in the COVID-19 period. This is an unexpected finding since investors usually unwelcome market volatility.

Keywords*: COVID-19, Market Reaction, Seasoned Equity Offerings, Bought Deals.*

1. INTRODUCTION

This paper examines the impact of COVID-19 period (03/11/2020 - 11/29/2021) and pre-pandemic period (01/13/2012 - 03/10/2020) on the market reaction to Canadian bought deal seasoned equity offerings. Did COVID-19 period have different impact on the market reaction to announcements of Canadian bought deal seasoned equity offerings compared with pre-pandemic period? The novel coronavirus (COVID-19) is an unexpected infectious disease that caught off ward world economies. The pandemic has created high uncertainty in financial markets reflected in high market volatility. For example, in the U.S., the stock market volatility in March 2020 surpassed 'those last seen in October 1987 and December 2008 and before that, in late 1929 and the early 1930s' (Baker et al., 2020). On the other hand, the pre-pandemic period includes years of moderate economic and financial stability following the aftermath of financial crisis of 2008-2009.

The market reaction to seasoned equity offerings (SEO) is an important signal that investors give to issuing companies about value of the offer. Seasoned equity offerings are offers following an initial public offering (IPO). Their main objective is getting funds to support working capital, capital investment projects, reducing debt and others. Normally, the market reaction is negative – usually around minus two to three percent of price decline after adjusting for risk (Lee and Masulis, 2009). Most accepted theory for the price decline is the adverse-selection theory by Myers and Majluf (1984). This theory says that managers have advantage of information about firm value than outside investors. Specifically, when a public company announces an equity offer investors assume the stock is above its fair value and push its price downwards. Bought deal seasoned equity offering is a method of choice for issuing equity in the stock market, others are marketed underwritten, and best efforts. (These methods of choice are described in the literature review section).

Contributions of this paper are as follows. First, to the best of my knowledge, it is the first study that explores the market impact of COVID-19 on seasoned equity offerings in Canada. It tests whether different impact on SEO market reaction occurs between the COVID-19 period and pre-pandemic period