The Long Run Share Price Performance of Malaysian Firms Issuing Equity Private Placements

(Prestasi Jangka Panjang Syarikat-Syarikat Malaysia yang Menerbitkan Tawaran Persendirian Ekuiti)

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ABSTRACT

The result of this study reveals an evidence of long run underperformance of equity private placements in Malaysia using market index as a benchmark. When the firms are matched to firms with similar size and market-to-book, they neither over-perform nor underperform the matching firms over the three-year period under the equal-weighting scheme. However, a considerable difference exists between the CARs and BHARs under the value-weighting scheme. Unlike previous studies that find small firms underperform more than large firms, results of this study show the opposite. We find that large firms show greater degree of underperformance than small firms. The result definitely does not conform to the widely acceptable idea that smaller firms are more likely to issue equity when they are overvalued due to higher degree of information asymmetry. Further results indicate that the underperformance is driven by the outlier in the sample. When it is excluded from the sample, no significant result is detected for the two-year period. Nevertheless, it is interesting to note that for both CAR and BHAR, the underperformance under equal-weighted scheme is worse when the returns are benchmarked against market index but in sharp contrast, the underperformance under value-weighted scheme is worse when the returns are benchmarked against matching firms.

ABSTRAK

Keputusan kajian menunjukkan prestasi jangka panjang syarikat-syarikat Malaysia yang menerbitkan tawaran persendirian ekuiti adalah lebih rendah berbanding dengan indeks pasaran. Tiada sebarang keputusan signifikan dicatatkan apabila syarikat-syarikat padanan saiz and nisbah nilai pasaran kepada nilai buku digunakan untuk jangka masa tiga tahun bagi skim berwajaran sama. Walau bagaimanapun, wujud perbezaan antara pulangan abnormal kumulatif (CAR) dan pulangan abnormal belian-pegangan (BHAR) bagi skim berwajaran nilai. Keputusan kajian ini menunjukkan keputusan yang bercanggah dengan kajian-kajian terdahulu di mana prestasi syarikat-syarikat kecil adalah lebih teruk berbanding dengan syarikat-syarikat besar. Keputusan ini adalah tidak selari dengan pendapat bahawa syarikat-syarikat kecil lebih cenderung menerbitkan ekuiti terlebih nilai (overvalued) disebabkan oleh maklumat tidak seimbang (information asymmetry) yang lebih tinggi. Keputusan kajian ini juga dipengaruhi oleh data ekstrem (outlier), yang mana apabila data ini dikeluarkan, tiada keputusan signifikan yang direkodkan. Sesuatu yang menarik adalah untuk skim berwajaran sama, pulangan yang rendah dicatatkan bagi indeks pasaran tetapi bagi skim berwajaran nilai, pulangan yang rendah dicatatkan bagi syarikat-syarikat padanan.

INTRODUCTION

This paper investigates three-year performance of firms issuing private placements in Malaysia. The returns of the issuing firms are compared against two benchmarks which are the market index and matching firms. Private placement is defined as issuance of concentrated equity to investors such as banks, mutual funds, insurance firms, pension funds, foundations and high-net-worth individuals. The transactions are done privately rather than publicly where the buyers can have direct negotiations with the issuer.

In contrast to public equity issues which are associated with negative announcement effects (Myers & Majluf 1984; Asquith & Mullins 1986) private equity issues are associated with positive announcement effects (Wruck 1989; Hertzel & Smith 1993; Kato & Schallheim 1993; Molin

1996; Hertzel & Rees 1998; Ferreira & Brooks 1999; Goh, Gombola, Lee & Liu 1999; Hertzel, Lemmon, Linck & Rees 2002; Tan, Chng & Tong 2002; Brooks & Graham 2005; Cronqvist & Nilsson 2005; Krishnamurthy, Spindt, Subramaniam & Woidtk 2005; Wruck & Wu 2009). Despite the fact that the announcement effect of public and private equity issues show opposite directions, the long run stock price performance following both methods of raising funds is very similar. Loughran and Ritter (1995, 1997) and Jegadeesh (2000) report that the stocks of firms making public seasoned equity offerings significantly underperform various benchmarks over three to five year period following the offerings. Hertzel et al. (2002), Chen, Ho, Lee, and Yeo (2002), Krishnamurthy et al. (2005), Barclay, Holderness, and Sheehan (2007) and Wruck and Wu (2009) find similar results for companies placing shares privately.

One of the explanations for the underperformance is that firms time equity issues to take advantage of "windows of opportunity" by issuing overvalued equity. "Windows of opportunity" refers to a situation when investors are being overoptimistic about the economy or industry condition. Other explanations offered include managerial entrenchment, investors' overoptimisms and investors' identities. Barclay et al. (2007) claim that private placements involve entrenchment as majority of the placements are passive placements. Passive placements refer to placements that show no evidence of interactions between the purchasers and the issuing firms either before or after the placements. Passive buyers do not provide the monitoring benefit which leads to agency cost reduction. Krishnamurthy et al. (2005) claim the long run underperformance is less severe when the shares are placed to affiliated investors than when they are placed to unaffiliated investors. Hertzel et al. (2002) suggest the underperformance is due to the investors' overoptimism at the time the initial placements are made. They find that private equity offerings follow periods of relatively poor operating performance and investors are over confident that private placements will improve the firm's operating performance. However, as time passes this expectation might not be true.

This study is motivated in part by the lack of research on private equity placements in Malaysia especially on the long run performance. It is extremely important to understand the long run performance because not only they will affect the shareholders' wealth but will also influence the ability of the firms to raise additional funds in the future. To the investors, the long run stock price performance provides trading strategy. The existence of price patterns gives opportunities for active trading strategies investors to earn abnormal returns. In addition, test for long run stock price performance is important to look for any market inefficiency.

The findings of this study reveal when market index (Kuala Lumpur Composite Index) is used as the benchmark, the issuing firms underperform the market index over the three-year period. The underperformance is observed both in CAR (cumulative abnormal return) and BHAR (buy-and-hold abnormal return) regardless of the weighting schemes used. In all cases, the underperformance is statistically significantly different from zero. To ensure robust results and to alleviate the biases that arise using market index as a benchmark, CAR and BHAR returns are also computed using a matching firm approach. When matching firms and equal weighting scheme are adopted the abnormal returns disappear. Despite previous studies find small firms underperform more than large firms, results of this study show the opposite. The underperformance of Malaysian firms issuing private placements seems to be driven by large firms rather than small firms.

LITERATURE REVIEW

Most of the studies on long run performance document underperformance results. Ritter (1991) for example finds that in the long run 1,526 IPOs issued for the period of 1975 to 1984 in the United States significantly underperform their benchmarks using both CAR and BHAR methods. The same result is reported by Loughran and Ritter (1995, 1997), Brav and Gompers (1997) and Jegadeesh (2000). According to Loughran and Ritter (1995), during the five years after conducting the offerings, the average annual return for firms issuing SEOs (seasoned equity offerings) is only seven percent compared to fifteen percent for non-issuing firms.

Hertzel et al. (2002) investigate the long run stock price performance of a sample of 619 publicly traded firms conducting private equity issues for the period of 1980 to 1996. In particular, they examine whether under-reaction hypothesis can be applied to explain long run abnormal returns. Under-reaction hypothesis states that the long run abnormal returns will continue in the same direction as the announcement period returns. However, results indicate the directions of announcement period returns and long run abnormal returns are not consistent with the under-reaction hypothesis. In contrast to the positive initial performance, they find that the firms experience negative long run stock price performance of -23.8 percent for the mean three-year buy-and-hold abnormal returns. They suggest that the investors' over-optimisms are more likely to explain the opposite directions of initial and long run performance.

Krishnamurthy et al. (2005) also find in the long run private placement investors earn negative abnormal returns. However, the result of the study shows that the effect is less severe when the shares are placed to affiliated investors than when they are placed to unaffiliated investors. The negative abnormal returns (-47.05 percent) are observed when the placements are made to unaffiliated investors. Yet, when the placements are made to affiliated investors, the abnormal returns are not statistically significantly different from zero. Affiliated investors are perceived to be better informed about the true prospects of the firm. Thus, could serve as a certification and signal positive information. Affiliated investors are those who belong to one or more of the following groups: (1) officers or directors of the firm; (2) relatives of officers or directors; (3) consultants or attorneys of the firm; (4) current large block holders of the firm; (5) institutions affiliated with firms; and (6) firms with product market agreements with the firm.

Barclay et al. (2007), claim the stock price performance depends on the type of buyers. According to them, the long run underperformance is driven by the placement placed to passive investors as those investors are not able to provide monitoring and expert advice as expected but helps to solidify the management's control. They report for the period from day -10 to day 120, the mean returns for passive placements are -9.9 percent compared

to 9.6 percent for active placements. Majority of private placements are placed to passive buyers instead of active buyers. Approximately, 85 percent of the total buyers are passive buyers. Passive buyers refer to those who play no role in the issuing firms, pre- or post-placements.

Consistent with previous studies, Wruck and Wu (2009) find poor long run performance. Particularly they find statistically significant average three-year match-adjusted return of -25.27 percent. However, they claim the negative performance is influenced by the relationships between the issuers and the investors. They further claim the result show a significant difference performance between issuers making placements with new relationships compared to those making placements without new relationships. Placements to investors with new relationships prove to have less severe underperformance. This is shown by the results that the mean three year match adjusted return of -38.13 percent (p-value = 0.000) for placements to investors with no new relationships and -11.98 percent (p-value = 0.205) for placements to investors with new relationships. However, in contrast to Barclay et al. (2007) who claim majority of the placements are passive placements, they claim that 64 percent of private placements are placed to those who have relationships with the issuers. They conclude that the findings are consistent with private placements create value through increased monitoring, stronger governance and resolution of information asymmetry.

In conclusion, previous studies show that firms that issue private placements experience long run underperformance. Among the explanations offered to explain the underperformance are investors' overoptimism, investors' identities and managerial entrenchment.

DATA AND METHODOLOGY

Tests are conducted using a sample of private placement issuances from 1999 to 2007. Sample firms comprise of all firms listed by Bursa Malaysia (prior to 1st May 2004, Bursa Malaysia was known as Kuala Lumpur Stock Exchange (KLSE)) on Main Board, Second Board (on 8th August 2009, Main and Second Boards have been merged into a single unified board, called the Main Market) and MESDAQ (on 8th August 2009, MESDAQ Market, which is for technology-based and high growth firms, is known as the ACE Market) that issue equity private placements over the stated period. Sample is gathered by identifying announcements of the first shares issuance on Bursa Malaysia's website. Nevertheless, announcements by finance firms, trusts and closed-end funds are excluded because these firms have different statutory requirements. The share price data and the market index returns are collected from the DataStream database. This process produces a sample of 176 private placements.

To measure long run performance, two different methods are employed. They are event time cumulative abnormal returns method (CAR) and buy-and-hold

abnormal returns method (BHAR). The CAR of τ-period beginning from listing date of private placement for firm i is calculated as:

$$CAR_{i,\tau} = \sum_{t=1}^{\tau} R_{i,t} - R_{c,t}$$

where $R_{i,t}$ is the simple monthly return for sample firm i, while $R_{c,t}$ is the simple monthly return of the control firm that is in the same size and market-to-book value as firm i or the monthly return of the market index.

Next, the cumulative average abnormal returns (CAARs) are calculated as follow for equal-weighting scheme:

$$CAAR_{ew,\tau} = \left(\tfrac{1}{n}\right)\sum_{i=1}^{n} CAR_{i,\tau}$$

where n is the number of firms in the sample.

For the cumulative average abnormal returns (CAARs) under the value-weighting scheme, the calculation is as follow:

$$CAAR_{vw,\tau} = \sum_{i=1}^{n} \omega_i CAR_{i,\tau}$$

where w_i equals to the private placement company's stock market value divided by the stock market value of all sample firms.

The BHAR for firm i over τ-period is calculated as follow:

$$BHAR_{i,\tau} = BHR_{i,\tau} - BHR_{c,\tau}$$

where $BHAR_{i,t}$, $BHR_{i,t}$ and $BHR_{c,t}$ are buy-and-hold return for firm i, buy-and-hold return of the sample firm and buy-and-hold return of the control firm respectively. When the long run abnormal returns are calculated using a market index, $BHR_{c,t}$ is replaced by $BHR_{m,t}$ which refers to the buy-and-hold return of the Kuala Lumpur Composite Index (KLCI).

Next, the average buy-and-hold abnormal returns (ABHARs) are calculated as follow:

$$ABHAR_{ew,\tau} = \left(\tfrac{1}{n}\right)\sum_{i=1}^{n} BHAR_{i,\tau}$$

where n is the number of firms in the sample.

For the average buy-and-hold abnormal returns (ABHARs) under the value-weighting scheme, the calculation is as follow:

$$ABHAR_{vw,\tau} = \sum_{i=1}^{n} \omega_i BHAR_{i,\tau}$$

where ω_i equals to the private placement firm's stock market value divided by the stock market value of all sample firms.

To calculate returns, both equal and value-weighted schemes are employed in order to enhance the robustness of the results. In line with other studies on long run performance the returns are calculated over the period of three years (see for example, Ritter 1991; Loughran & Ritter 1995; Hertzel et al. 2002; Krishnamurthy et al. 2005; Ahmad-Zaluki, Campbell & Goodacre 2007) starting from the date of listing. Due to the sensitivity of methods and benchmark biases in measuring long run performance (Jegadeesh 2000), the abnormal returns are measured relative to two benchmarks. They are matching or control firm benchmark

and Kuala Lumpur Composite Index (KLCI) with both equal and value-weighting schemes. KLCI comprises of 100 (starting from July 6 2009, the KLCI has been replaced by FBMKLCI which comprises of the largest 30 companies by full market capitalization on Bursa Malaysia's Main Board) largest Malaysian firms listed on Bursa Malaysia. The major limitation of using KLCI as a benchmark is it may introduce the size-related bias. Alternatively, the matching firms are chosen from firms listed on Main Board, Second Board, and MESDAQ based on size and market-to-book ratio in the month prior to the listing month. Size is defined as price per share multiplied by the number of shares outstanding and market-to-book equity ratio is defined as market value of equity divided by book value of equity. Only two variables are chosen because if more variables are added, the quality of the matches might decrease. All firms which have not made any private equity listings within the last three years and the next three years are ranked by their size and market-to-book ratios.

Then Euclidean Distance is calculated. Euclidean Distance is measured by the following equation:

$$ED = \left\| \left(\frac{MV_i}{\sum\limits_{i=1}^{n} MV_i} - \frac{MV_p}{\sum\limits_{i=1}^{n} MV_i} \right)^2 + \left(\frac{MTBV_i}{\sum\limits_{i=1}^{n} MTBV_i} - \frac{MTBV_p}{\sum\limits_{i=1}^{n} MTBV_i} \right)^2 \right\|$$

where,

MV_p : Market value of private placement firm p in the month prior to the month of issuance

MV_i : Market value of firm i

$MTBV_p$: Market-to-book value of private placement firm p in the month prior to the month of issuance

$MTBV_i$: Market-to-book value of firm i

The firms with minimum or closest Euclidean Distance to the issuing firm are chosen as matching firms. One private placement firm is then matched with one, two and four non-issuing private placement firms. The abnormal returns are calculated for up to three years or 36 months

after the event month which is the listing month. For private placement firms which are delisted or dead before their 3-year anniversary, the calculation period ends with their last months of listings. For the matching firms which are delisted or dead before the 3-year period, they will be replaced by the other firms that have the next closest Euclidean Distance.

Table 1 below summarizes the goodness of fit between the sample firms and the matching firms. The average market value of the sample firms is RM320.68 million and the average market-to-book value is 1.53. For one match, the average market value of the matching firms is RM301.69 million and the market-to-book value is 1.52. The average market value for matching firms is slightly lower than the sample firms when the number of matches is increased into two. The average market value for the 352 matching firms is RM319.65 million. The average market-to-book value is also less than the sample firms, which is 1.51. For four matches, the average market value is RM306.87 million and the average market-to-book value is 1.50. To ensure the quality of the matches, we check whether the characteristics of matching firms are similar to those of the sample firms. Results show that for all matches, the differences in size and market-to-book value are statistically insignificant. For one match, the difference in size is an insignificant 18.99 and the difference in market-to-book value is an insignificant 0.01. The p-values of the differences in average market value and average market-to-book value are 0.906 and 0.933 respectively. Similar results are observed for two and four matches. The p-value of the differences in average market value is 0.994 and the p-value of the differences average market-to-book value is 0.880 for two matches. For four matches, the p-value is 0.910 for market value and 0.825 for market-to-book value. Since the null hypothesis that the characteristics of matching firms are similar to the sample firms cannot be rejected, it can be concluded that the matching firms are comparable to the sample firms. Thereby the matching firms serve as good benchmarks.

TABLE 1. Goodness of fit of the matching firms

	MV of private placement firms	MV of matching firms	p-value of difference in MV	MTBV of private placement firms	MTBV of matching firms	p-value of difference in MTBV
1 match	320.677	301.690	0.906	1.528	1.516	0.933
2 matches	320.677	319.650	0.994	1.528	1.510	0.880
4 matches	320.677	306.870	0.910	1.528	1.503	0.825

Notes: MV: market value; MTBV: market-to-book value

RESULTS

ALL SAMPLE FIRMS: CUMULATIVE ABNORMAL RETURNS (CAR)

Table 2 reports the cumulative raw returns of the sample firms over the three-year period following the private placements issuance. Most of the time the returns are

negative for both equal- and value weighted schemes (Refer to Figure 1). For equal-weighting scheme, the lowest return (-19.69 percent) is spotted 18 months after the issuance. The three-year mean raw return is -16.02 percent and statistically significant at five percent level. Different results are observed for the value-weighted cumulative raw returns. Despite its negative figure, the three-year

mean raw return is not significant. Nevertheless, greater negative performance is shown by value-weighted returns where the worst return is reported after two years of issuance. The mean two-year cumulative raw returns are -35.33 percent which is statistically significant at the one percent level.

TABLE 2. Summary of equal- and value-weighted cumulative raw returns, for 36-month period after the issuing date

Months	No. of Firms	Cum. RAW Returns (%)	
		EW	VW
1 - 6	176	-3.39	5.31**
		(p = 0.330)	(p = 0.035)
1 - 12	176	-11.00**	-6.41**
		(p = 0.011)	(p = 0.050)
1 - 18	173	-19.69***	-28.98***
		(p = 0.000)	(p = 0.000)
1 - 24	173	-19.03***	-35.33***
		(p = 0.000)	(p = 0.000)
1 - 30	153	-17.31***	-13.12***
		(p = 0.009)	(p = 0.004)
1 - 36	134	-16.02**	-0.97
		(p = 0.030)	(p = 0.842)

***Significant at 1 percent level.
**Significant at 5 percent level.
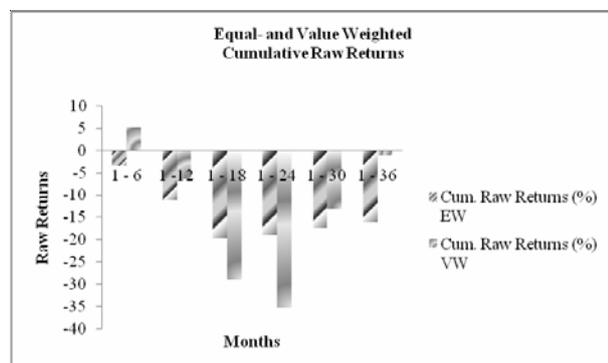*Significant at 10 percent level.

FIGURE 1. Equal- and value weighted cumulative raw returns for the three-year period

Table 3 reports the CAARs adjusted for the market for the period of 36 months after the listing date. There is a downward trend in equal-weighted CAARs adjusted for KLCI, while value-weighted CAARs fluctuate between -12.49 percent and -18.96 percent over the three-year period following the issuance. The private placement firms significantly underperform KLCI during the three-year period. Beginning with the first year CAAR of -6.98 percent, the return plunges to -29.22 percent in the second year and drops further to -39.78 percent in the third year when KLCI equal-weighted is used. The returns are also significant when the t-statistics for CAAR is determined using the t-statistics employed by Ritter (1991). All the one-, two-, and three-year abnormal returns are statistically significant at the one percent level. Consistent with the equal-weighted CAARs, the CAARs of KLCI value-weighted are -17.79 percent, -13.65 percent and -14.62 percent in the first, second and third year respectively. In brief, the long run underperformance is consistent with previous equity issuing studies (Ritter 1991; Loughran & Ritter 1995; 1997; Jegadeesh 2000; Chen et al. 2002; Hertzel et al. 2002; Krishnamurthy et al. 2005; Barclay et al. 2007; and Wruck and Wu 2009).

TABLE 3. Summary of equal- and value-weighted CAARs adjusted for market, for 36-month period after the issuing date

Months	No. of Firms	CAARs (%)	
		KLCI (EW)	KLCI (VW)
1 - 6	176	-6.98**	-4.17**
		(p = 0.030)	(p = 0.044)
1 - 12	176	-15.61***	-17.79***
		(p = 0.000)	(p = 0.000)
1 - 18	173	-26.43***	-18.96***
		(p = 0.000)	(p = 0.000)
1 - 24	173	-29.22***	-13.65***
		(p = 0.000)	(p = 0.001)
1 - 30	153	-33.18***	-12.49***
		(p = 0.000)	(p = 0.009)
1- 36	134	-39.78***	-14.62**
		(p = 0.000)	(p = 0.011)

***Significant at 1 percent level.
**Significant at 5 percent level.
*Significant at 10 percent level.

Table 4 reports the CAARs adjusted for the matching firms for the period of 36 months after the listing date. The private placements neither underperform nor overperform when they are benchmarked with matching firms under the equal-weighting scheme. However, under the value-weighting scheme, the issuing firms significantly underperform the matching firms beginning in the first year up to the third year. The one-year returns are -10.47 percent for two-firm adjusted and -15.35 percent for four-firm adjusted. Worse performance is reported in the second year with -23.57 percent, -25.58 percent and -30.01 percent are reported for one-, two- and four-firm adjusted. Over the three-year period the abnormal returns are -15.23 percent for two-firm adjusted and -19.75 percent for four-firm adjusted.

Abnormal returns from each firm are equally weighted to measure equal-weighted returns. Abnormal returns from each firm are weighted based on the firms' size to measure value-weighted returns. Therefore, using value-weighted approach, large firms carry more weight than small firms. That is why the equal-weighted returns and value-weighted returns reveal different results. Based on the results, it seems that the underperformance is driven by large firms. This is shown by more severe and statistically significant results under value-weighted scheme.

TABLE 4. Summary of equal- and value-weighted CAARs adjusted for control matched firms, for 36-month period after the issuing date

Months	No. of Firms	EW - CAARs (%)			VW - CAARs (%)		
		1 Match	2 Matches	4 Matches	1 Match	2 Matches	4 Matches
1 - 6	176	1.22	2.06	1.47	8.88***	4.26**	-0.02
		(p = 0.737)	(p = 0.526)	(p = 0.645)	(p = 0.000)	(p = 0.040)	(p = 0.992)
1 - 12	176	0.27	-0.87	-1.84	3.19	-10.47***	-15.35***
		(p = 0.956)	(p = 0.836)	(p = 0.648)	(p = 0.322)	(p = 0.000)	(p = 0.000)
1 - 18	173	-7.96	-7.20	-10.46**	-13.34***	-26.05***	-29.31***
		(p = 0.143)	(p = 0.140)	(p = 0.029)	(p = 0.002)	(p = 0.000)	(p = 0.000)
1 - 24	173	-8.87	-7.16	-9.89*	-23.57***	-25.58***	-30.01***
		(p = 0.203)	(p = 0.227)	(p = 0.077)	(p = 0.000)	(p = 0.000)	(p = 0.000)
1 - 30	153	-3.06	-3.74	-7.76	-4.45	-10.59*	-16.09***
		(p = 0.698)	(p = 0.585)	(p = 0.226)	(p = 0.490)	(p = 0.052)	(p = 0.001)
1 - 36	134	-7.91	-7.97	-10.57	1.48	15.23**	-19.75***
		(p = 0.384)	(p = 0.328)	(p = 0.159)	(p = 0.838	(p = 0.011)	(p = 0.001)

***Significant at 1 percent level, **Significant at 5 percent level, *Significant at 10 percent level.

BUY-AND-HOLD ABNORMAL RETURNS (BHAR)

Similar results are reported by buy-and-hold raw returns of the sample firms over the three-year period following the private placements issuance. Refer to Table 5 and Figure 2. The results show negative long run performance but none of the returns are significant in the third year which is in contrast to the 0.21 percent of three-year mean raw buy-and-hold return reported by Hertzel et al. (2002). The worst result is reported by value-weighted returns in the second year, which is -31.15 percent.

TABLE 5. Summary of equal- and value-weighted buy-and-hold raw returns, for 36-month period after the issuing date

Months	No. of Firms	Buy-and-hold Raw Returns (%)	
		EW	VW
1 - 6	176	0.66	7.22**
		(p = 0.907)	(p = 0.038)
1 - 12	176	-10.91***	-5.24*
		(p = 0.005)	(p = 0.069)
1 - 18	173	-17.03***	-24.00***
		(p = 0.000)	(p = 0.000)
1 - 24	173	-18.78***	-31.15***
		(p = 0.002)	(p = 0.000)
1 - 30	153	-14.45*	-14.58**
		(p = 0.084)	(p = 0.013)
1 - 30	153	-14.45*	-14.58**
		(p = 0.084)	(p = 0.013)
1 - 36	134	-17.09	0.73
		(p = 0.165)	(p = 0.935)

***Significant at 1 percent level.
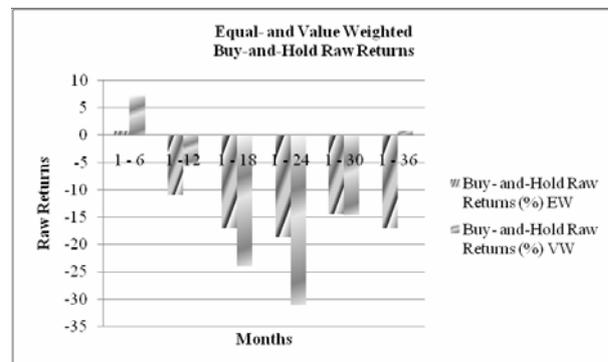**Significant at 5 percent level.
*Significant at 10 percent level.

FIGURE 2. Equal- and value weighted buy-and-hold raw returns for the three-year period

The results of the underperformance shown by CAR hold when BHAR is adopted. As shown in Table 6, using KLCI as the benchmark, the private placement firms underperform the market index for both equal- and value-weighted schemes. The returns for 36-month period are -41.88 percent when KLCI equal-weighted is used and -17.59 percent when KLCI value-weighted is used. Equal-weighted return is significant at one percent level while value-weighted return is statistically significant at 10 percent level.

When observing the results of the market adjusted returns, there is a slight difference between the abnormal returns calculated using equal-weighted and value-weighted schemes. Severe underperformance is observed using equal-weighted scheme. For example, although the CAARs and ABHARs under both schemes are negative, the equal-weighted returns have greater degree of negative effect than the value-weighted returns. For example, the CAAR is -39.78 percent and the ABHAR is -41.88 for the

TABLE 6. Summary of equal- and value-weighted ABHARs adjusted for market, for 36-month period after the issuing date

Months	No. of Firms	ABHARs (%)	
		KLCI (EW)	KLCI (VW)
1 - 6	176	-3.13	-2.98
		(p = 0.570)	(p = 0.346)
1 - 12	176	-16.62***	-18.31***
		(p = 0.000)	(p = 0.000)
1 - 18	173	-25.44***	-27.16***
		(p = 0.000)	(p = 0.000)
1 - 24	173	-29.26***	-25.88***
		(p = 0.000)	(p = 0.000)
1 - 30	153	-30.35***	-19.35***
		(p = 0.000)	(p = 0.001)
1- 36	134	-41.88***	-17.59*
		(p = 0.001)	(p = 0.088)

***Significant at 1 percent level.
**Significant at 5 percent level.
*Significant at 10 percent level.

former group compared to CAAR of only -14.62 percent and ABHAR of -17.59 for the latter group. Refer to Tables 3 and 6.

Table 7 reports equal- and value-weighted ABHARs adjusted for control matched firms three years following the equity issuance. The private placements neither underperform nor overperform when they are benchmarked with matching firms (refer to Table 7). Unlike the results reported by CAARs, none of the three-year ABHARs are statistically significantly different from zero in all cases. However, the value-weighted ABHARs of the issuing firms over the two-year period are statistically significant at the one percent level as those reported by the CAARs. The mean two-year returns are -17.95 percent for one-firm adjusted, -16.18 percent for two-firm adjusted and -18.76 percent for four-firm adjusted. Correspondingly, none of the equal-weighted ABHARs give significant figures. Once again, the results indicate that the underperformance is more likely to be driven by large firms.

TABLE 7. Summary of equal- and value-weighted ABHARs adjusted for control matched firms, for 36-month period after the issuing date

Months	No. of Firms	EW - ABHARs (%)			VW - ABHARs (%)		
		1 Match	2 Matches	4 Matches	1 Match	2 Matches	4 Matches
1 - 6	176	5.36	5.96	5.67	10.09***	4.77	0.15
		(p = 0.325)	(p = 0.261)	(p = 0.292)	(p = 0.002)	(p = 0.115)	(p = 0.961)
1 - 12	176	1.12	-1.48	-1.84	1.36	-16.78***	-18.45***
		(p = 0.800)	(p = 0.717)	(p = 0.618)	(p = 0.655)	(p = 0.000)	(p = 0.000)
1 - 18	173	-2.39	-2.53	-5.84	-11.28***	-28.76***	-26.45***
		(p = 0.630)	(p = 0.592)	(p = 0.205)	(p = 0.002)	(p = 0.000)	(p = 0.000)
1 - 24	173	-0.83	-0.67	-3.89	-17.95***	-16.18***	-18.76***
		(p = 0.900)	(p = 0.913)	(p = 0.515)	(p = 0.000)	*(p = 0.000)	(p = 0.000)
1 - 30	153	7.54	7.31	2.72	-2.24	-4.82	-9.12
		(p = 0.394)	(p = 0.393)	(p = 0.742)	p = 0.741)	(p = 0.458)	(p = 0.142)
1 - 36	134	3.73	3.07	-2.90	7.04	-5.22	-8.88
		(p = 0.778)	(p = 0.808)	(p = 0.814)	(p = 0.526)	(p = 0.628)	(p = 0.395)

***Significant at 1 percent level, **Significant at 5 percent level, *Significant at 10 percent level.

LARGE VERSUS SMALL FIRMS

Since both CAARs and ABHARs adjusted for control matching firm show significant underperformance when value-weighted scheme is adopted, we divided the sample into two to find out whether the two-year under performance is driven by the size of the firm. The two groups are: (1) large firms group; and (2) small firms group. Large firms are those with market capitalisation or market value greater than the sample median (RM101.21 million), while small firms are those with market capitalisation less than the sample median.

Table 8 reports value-weighted CAARs and ABHARs of large and small issuing firms relative to the market index. There is not much difference between the returns of large

and small firms when they are compared against the market index. The mean three-year CAAR of large firms is -20.15 percent and the mean three-year CAAR of small firms is -34.90. Nevertheless, the mean three-year ABHAR of large firms is not significant, while the mean three-year ABHAR of small firms is -55.29 percent and statistically significant at one percent level. Therefore, using ABHAR adjusted for the market index, the underperformance over the three-year period seems to be driven by small firms. Thus, consistent with other studies that find long run underperformance is driven by small firms (see for example, Brav & Gompers 1997; Chen et al. 2002).

TABLE 8. Summary of value-weighted CAARs and ABHARs of large and small firms adjusted for market, for 36 month-period after the issuing date

Months	CAAR - KLCI		ABHAR - KLCI	
	Large Firms	Small Firms	Large Firms	Small Firms
1 - 6	-4.29*	-2.70	-3.98	8.64
	(p = 0.080)	(p = 0.663)	(p = 0.122)	(p = 0.513)
1 - 12	-18.36***	-11.20	-18.65***	-14.38**
	(p = 0.000)	(p = 0.109)	(p = 0.000)	(p = 0.021)
1 - 18	-32.66***	-18.54**	-27.43***	-24.08***
	(p = 0.000)	(p = 0.012)	(p = 0.000)	(p = 0.001)
1 - 24	-31.82***	-19.06**	-26.02***	-24.26***
	(p = 0.000)	(p = 0.020)	(p = 0.000)	(p = 0.009)
1 - 30	-20.37***	-20.37**	-18.66**	-27.62**
	(p = 0.002)	(p = 0.025)	(p = 0.023)	(p = 0.011)
1 - 36	-20.15**	-34.90***	-14.24	-55.29***
	(p = 0.011)	(p = 0.007)	(p = 0.337)	(p = 0.000)

***Significant at 1 percent level, **Significant at 5 percent level, *Significant at 10 percent level.

Table 9 reports value-weighted CAARs and ABHARs of large issuing firms relative to matching firms and Table 10 reports value-weighted CAARs and ABHARs of small issuing firms relative to matching firms.

TABLE 9. Summary of value-weighted CAARs and ABHARs of large issuing firms adjusted for control matched firm, for 36 month-period after the issuing date

Months	No. of Firms	VW - CAARs (%)			VW - ABHARs (%)		
		1 Match	2 Matches	4 Matches	1 Match	2 Matches	4 Matches
1 - 6	88	9.20***	4.27*	-0.46	9.46***	3.78	-1.39
		(p = 0.080)	(p = 0.092)	(p = 0.853)	(p = 0.003)	(p = 0.126)	(p = 0.575)
1 - 12	88	3.39	-11.21***	-16.73***	1.22	-18.01***	-20.04***
		(p = 0.426)	(p = 0.003)	(p = 0.000)	(p = 0.768)	(p = 0.000)	(p = 0.000)
1 - 18	87	-13.72**	-27.86***	-31.30***	-11.81**	-30.97***	-28.36***
		(p = 0.020)	(p = 0.000)	(p = 0.000)	(p = 0.020)	(p = 0.000)	(p = 0.000)
1 - 24	87	-24.76***	-27.45***	-32.21***	-19.40***	-17.59***	-20.41***
		(p = 0.004)	(p = 0.000)	(p = 0.000)	(p = 0.005)	(p = 0.003)	(p = 0.000)
1 - 30	78	-4.89	-11.70	-17.47**	-3.05	-5.91	-10.44
		(p = 0.590)	(p = 0.118)	(p = 0.012)	(p = 0.744)	(p = 0.509)	(p = 0.221)
1 - 36	68	2.56	-15.85*	-20.87***	8.72	-4.68	-8.38
		(p = 0.800)	(p = 0.052)	(p = 0.008)	(p = 0.587)	(p = 0.764)	(p = 0.579)

***Significant at 1 percent level, **Significant at 5 percent level, *Significant at 10 percent level.

TABLE 10. Summary of value-weighted CAARs and ABHARs of small issuing firms adjusted for control matched firm, for 36 month-period after the issuing date

Months	No. of Firms	VW - CAARs (%)			VW - ABHARs (%)		
		1 Match	2 Matches	4 Matches	1 Match	2 Matches	4 Matches
1 - 6	88	5.08	4.06	5.63	17.45	16.28	18.06
		(p = 0.373)	(p = 0.487)	(p = 0.338)	(p = 0.148)	(p = 0.198)	(p = 0.162)
1 - 12	88	0.93	-1.87	0.65	3.02	-2.50	0.03
		(p = 0.898)	(p = 0.792)	(p = 0.926)	(p = 0.619)	(p = 0.706)	(p = 0.996)
1 - 18	86	-9.10	-5.52	-6.88	-5.24	-3.85	-4.82
		(p = 0.177)	(p = 0.440)	(p = 0.348)	(p = 0.347)	(p = 0.545)	(p = 0.478)
1 - 24	86	-10.07	-4.52	-5.12	-1.64	-0.26	-0.08
		(p = 0.257)	(p = 0.584)	(p = 0.538)	(p = 0.868)	(p = 0.977)	(p = 0.993)
1 - 30	75	0.72	2.64	0.47	7.48	8.32	6.67
		(p = 0.938)	(p = 0.779)	(p = 0.958)	(p = 0.506)	(p = 0.452)	(p = 0.536)
1 - 36	66	-10.68	-8.25	-7.10	-11.84	-11.31	-14.49*
		(p = 0.354)	(p = 0.463)	(p = 0.483)	(p = 0.217)	(p = 0.199)	(p = 0.090)

***Significant at 1 percent level, **Significant at 5 percent level, *Significant at 10 percent level.

As reported in Table 9 and 10, when the sample is grouped into two, the underperformance is evident only in the large group. This is especially true for two-year period. Results show that the two-year CAARs and ABHARs relative to the matching firms are between -17.59 percent to -32.21 percent statistically significant at the one percent level. However, there is a great difference in the results of third year CAARs and ABHARs where significant underperformance is reported by CAARs but none by ABHARs.

In contrast to large firms group, no significant result is shown by small firms except for the three-year value-weighted ABHAR which shows a return of -14.49 percent when four matches are used. The results shown are consistent with those reported in Tables 4 and 7 where the underperformance is observed for large firms. Thus, the findings are not consistent with the notion that smaller firms which usually have higher degree of information asymmetry (Loughran and Ritter, 1995) have more tendency than larger firms to issue overvalued shares. The results that show large firms tend to underperform greater than small firms are also inconsistent with other studies that find long run underperformance is driven by small firms (see for example, Brav and Gompers 1997 and Chen et al. 2002). According to Chen et al. (2002) the long run stock price underperformance is due to the tendency of smaller firms with poorer growth opportunities to issue overvalued shares.

In brief, by looking at the results, it seems that the significant abnormal returns performance is drawn by large firms. To assess the robustness of our results, we then excluded the outlier in the sample which is the largest firm to examine the possibility that the underperformance is driven by that firm. The largest firm has been identified as "Genting Berhad". Genting has a market value of RM 20,641.57 million compared to the average market value of RM320.68 for all sample firms. The result of the analysis is summarised in Table 11 and Table 12.

Table 11 illustrates value-weighted CAARs and ABHARs relative to KLCI when the largest firm is taken out. Once again, for market adjusted returns, the CAARs and ABHARs of the issuing firms exhibit negative abnormal returns and statistically significant for the period of two to three years. In conclusion, the negative results hold even when the outlier is excluded.

Nevertheless, different results are observed for matching firms adjusted returns. When the outlier is excluded, the two-year significant negative CAARs and the two and three-year ABHARs found in Table 4, 7, and 9 disappear (refer to Table 12). Thus, the outcomes support the Efficient Market Hypothesis. Nevertheless, the significant negative three-year CAARs stay for two and four matched firms. This scenario provides further evidence that the underperformance might be driven by the largest firm in the sample which is Genting Berhad.

TABLE 11. Summary of value-weighted CAARs and ABHARs adjusted for market when the largest firm is excluded, for 36 month-period after the issuing date

Months	No. of Firms	Returns Adjusted for KLCI (%)	
		VW - CAAR	VW - ABHAR
1 - 6	175	-8.34***	-5.53
		(p = 0.001)	(p = 0.164)
1 - 12	175	-23.75***	-21.88***
		(p = 0.000)	(p = 0.000)
1 - 18	172	-30.47***	-29.45***
		(p = 0.000)	(p = 0.000)
1 - 24	172	-21.94***	-27.07***
		(p = 0.000)	(p = 0.000)
1 - 30	152	-20.72***	-23.88***
		(p = 0.000)	(p = 0.002)
1 - 36	133	-28.82***	-29.91**
		(p = 0.000)	(p = 0.039)

***Significant at 1 percent level, **Significant at 5 percent level, *Significant at 10 percent level.

TABLE 12. Summary of value-weighted CAARs and ABHARs adjusted for control matched firm when the largest firm is excluded, for 36 month-period after the issuing date

Months	No. of Firms	VW - CAARs (%)			VW - ABHARs (%)		
		1 Match	2 Matches	4 Matches	1 Match	2 Matches	4 Matches
1 - 6	175	9.46***	7.97***	4.11	11.48***	9.99***	6.13
		(p = 0.002)	(p = 0.002)	(p = 0.106)	(p = 0.005)	(p = 0.008)	(p = 0.109)
1 - 12	175	3.72	0.48	-4.31	2.06	-0.77	-4.61
		(p = 0.359)	(p = 0.885)	(p = 0.170)	(p = 0.591)	(p = 0.799)	(p = 0.101)
1 - 18	172	-6.98	-6.54	-14.15***	-2.14	-3.04	-8.68**
		(p = 0.184)	(p = 0.129)	(p = 0.001)	(p = 0.627)	(p = 0.446)	(p = 0.020)
1 - 24	172	-0.81	-0.65	-6.88	3.59	2.32	-3.42
		(p = 0.909)	(p = 0.912)	(p = 0.181)	(p = 0.533)	(p = 0.647)	(p = 0.468)
1 - 30	152	1.88	4.27	-2.00	12.04	12.36	5.18
		(p = 0.820)	(p = 0.525)	p = 0.745)	(p = 0.160)	(p = 0.128)	(p = 0.506)
1 - 36	133	-9.58	-15.58*	-17.76**	12.98	6.85	2.45
		(p = 0.346)	(p = 0.063)	(p = 0.025)	(p = 0.407)	(p = 0.649)	(p = 0.867)

Notes: ***Significant at 1 percent level, **Significant at 5 percent level, *Significant at 10 percent level.

DISCUSSION

Similar to previous studies on long run performance of equity private placements (Chen et al. 2002; Hertzel et al. 2002; Krishnamurthy et al. 2005; Barclay et al. 2007; Wruck & Wu 2009), significant underperformance is found for CAARs and ABHARs using market benchmark for both equal- and value-weighted schemes. The 36-month CAARs market adjusted are -39.78 percent for equal-weighted and -14.62 percent for value-weighted. Both are statistically significant at the one and five percent level, respectively. Consistently, the 36-month ABHARs adjusted for the KLCI show similar results. For equal-weighted, the returns are -41.88 percent and for value-weighted, the returns are -17.59 percent. This underperformance is not much difference from the study by Hertzel et al. (2002) which reports a 3-year BHAR of -45.15 percent for size-matched control firms, -23.78 percent for size- and book-to-market-matched control firms and -38.18 percent for size- and industry matched control firms for a sample of 619 firms during the period of 1980 to 1996. Similar results are reported by Krishnamurthy et al. (2005) and Wruck and Wu (2009) over the same time span. The first study reports a return of -38.39 percent and the latter reports a match-adjusted return of -25.27 percent.

None statistically significant abnormal returns are observed when matching firms are used as the benchmarks under equal-weighting scheme. The three-year CAARs and ABHARs matched for one, two and four firms with similar size and market-to-book show mixed results but none of them are statistically significantly different from zero. However, under value-weighting scheme, different results are observed for CAAR and ABHAR. While no statistically significant abnormal returns are shown by value-weighted ABHARs, the three-year CAARs adjusted for matching two and four firms show statistically significant underperformance.

Private placements investors are skilled investors who have access to the firm's true value. Therefore, private placements equity should be undervalued or at least fair valued. Consequently, market judges the willingness of these investors to purchase the shares as good signal. Unfortunately, results of the long run performance of equity private placements in Malaysia do not reveal the expected result. In the long run it seems that these institutional buyers are not well versed about the firms' true value and end up buying overvalued shares as pictured by the poor long run underperformance. Other explanation might be the underperformance is caused by their reselling activities. They might immediately sell the overvalued shares after purchasing them to the uninformed investors.

Regulations on private placements in Malaysia might also contribute to the poor performance. In particular, private placements in Malaysia are subjected to a two percent cap for the number of shares placed to one placed. As a result, it is so unlikely that they will form any post placement relationship between the issuers and the purchasers. Therefore, they do not increase monitoring and provide stronger governance which in turn can create value to the firms as suggested by Wruck and Wu (2009). The idea is also in line with Barclay et al. (2007) who claim that the underperformance is due to passive investors. This is especially true in the Malaysian context given that with only two percent of shares, the investors will only be passive investors who have limited ability to directly affect the firm performance.

Another plausible explanation for the three-year underperformance is managers time equity issues or listings to take advantage of windows of opportunity to issue overvalued equity since the shares are sold to new investors. As stated by the SC's (Securities Commission) regulations, the issue may not be placed to the directors or existing substantial shareholders and other "related" parties. Even though no evidence of significant abnormal returns prior to the announcements dates, we find stock price run-ups during the stated period. The issuing firms' cumulative unadjusted returns for the period of 56 days (-60,-5) are 4.76 percent which suggests that they do time equity issues when the price is high. Likewise, Hertzel et al. (2002) find that for the period of 12 months which end one month prior to the issuance month (-13 to -2), the issuing firms exhibited a mean raw buy-and-hold return of 52.78 percent. The return is statistically significantly higher than the returns of the matching firms.

As for the case of large firms perform worse than small firms, we expect that large firms have lower information asymmetry as they are followed by more analysts. Therefore, their prices should be more efficient. We expect small firms to have higher price deviation from true value. However, it is not something unusual to see large firms perform worse as they probably might issue overvalued shares. Logically, large firms can easily obtain a loan to raise capital. Therefore, their decision to issue new shares might reflect their belief that the shares are overvalued, as suggested by Myers and Majluf (1984). Furthermore, given the fact that the substantial shareholders of these firms are willing to lose some control by issuing common stock, there is a great possibility that the stocks are overvalued. Given the likelihood that the managers might issue overvalued shares, the question now is why the investors still want to purchase the shares? One possibility is that the investors are anticipating to earn profit by reselling the shares as most of private placement shares are sold at discount. The results might also suggest that the investors are overoptimistic about the prospects of the firms (Hertzel et al. 2002). However, their over-optimism only will result in poor long run performance when later the firm shows dissatisfied performance not as expected.

Another explanation is the underperformance does not mean that the market is inefficient; instead it only reflects normal random variations that constitute efficient market (Fama 1998). As a matter of fact, the results based on equal-weighted CAAR and equal- and value-weighted ABHAR do support the idea that Malaysian market is an

efficient market. In addition, the result when the outlier is excluded also provides evidence to support the claim. Lastly, the underperformance might be due to inappropriate benchmark. The KLCI used in this study comprises the 100 largest firms listed on Bursa Malaysia, while the sample comprises of all large and small firms listed on Main Board, Second Board and MESDAQ. Therefore, the use of KLCI might not be appropriate.

CONCLUSION

In conclusion, there is an evidence of long run underperformance of private placements in Malaysia using KLCI as the benchmark. This result is in contrast with Kamarun and Rohaida (2007) who find in the long run, performance of the IPOs in Malaysia is comparable if not higher than their matches. The result also contradicts the results by Ahmad-Zaluki et al. (2007) which report significant long run over performance of Malaysian IPOs using equally-weighted CARs and BHARs relative to market benchmarks. However, the abnormal returns disappear when value weighting scheme and a matched company benchmark is used.

For our sample, irrespective of the methods and weighting schemes employed, the share prices underperform for the period of three years after the listing date when the returns are adjusted for the market index. The results are for sure against the notion of market efficiency. Thus suggesting that to earn good returns investors should not invest in a private placement firm, instead KLCI is a better alternative. When the firms are matched to firms with similar size and market-to-book, they neither over-perform nor underperform the matching firms over the three-year period under the equal-weighting scheme. The findings might be due to the differences in average riskiness of the sample firms and KLCI. Hence, suggesting KLCI might not be an appropriate benchmark. However, a considerable difference exists between the CAARs and ABHARs under the value-weighting scheme. Plausible explanation for the difference in CAARs and ABHARs might be due to the different ways both methods are calculated and the influence of the largest firm in the sample which is Genting Berhad. The difference between ABHAR and CAAR might be caused by the price of Genting that went up after the second year. The price of Genting started at RM6.60 at the time of issuance (December, 2006) and increased to RM7.60 in the next month. The price fluctuated around RM8.00 and RM7.00 for about one and a half years following the issuance. After that, the price started to decline until it reached the lowest price of RM3.46 in month 26. At the end of the third year the price was RM7.34. In comparison, the prices of two controlling firms which are Petronas Berhad (first matched) and PLUS Expressway Berhad (fourth matched) are more stable over the three year period. The other two, IOI Berhad (second matched) and Sime Darby Berhad (fourth matched) show similar trend with Genting Berhad. The increase in price of Genting at the end of year three has caused the difference in CAAR and ABHAR, since CAAR is calculated as the summation of abnormal returns for each month while ABHAR is calculated as the difference between returns in month 36 and month 0.

In addition, the result of this study also reveals that large firms show greater degree of underperformance than small firms. Unlike previous studies that find small firms underperform more than large firms, results of this study show the opposite. The result of this study is inconsistent with the argument that less information is available for small firms than for large firms. Further results indicate that underperformance is driven by the largest firm in the sample. When it is excluded, no significant result is detected for the two-year period. In brief, significant long run underperformance of Malaysian private placements is found for CAARs and ABHARs using market benchmark. The underperformance is also found for value-weighted CAARs using matched firms benchmarks but disappeared for ABHARs using matched firms benchmark. Nevertheless, it is interesting to note that for both CAARs and ABHARs, the underperformance under equal-weighted scheme is worse when the returns are benchmarked against market index but in sharp contrast, the underperformance under value-weighted scheme is worse when the returns are benchmarked against matching firms.

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