First-day Stock Returns to Issuing Initial Corporate Bond and Seasoned Equity

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This paper examines the intraday return of stock price in response to announcement of initial corporate debt offerings and seasoned equity offerings. We find that the average stock price reaction to initial debt offerings is positive, in comparison to an established notion that average stock price return to regular corporate debt offerings is not significantly different from zero. Moreover, firms issuing initial debt offerings with higher price/earnings ratio are found to experience more positive stock price return. Although the stock price reaction to initial debt offerings is negatively affected by the expected post-issuance long term debt ratio, the stock price return is interestingly positively correlated with the amount of debt to be issued. These findings support the theory of quality signaling by debt financing and provide evidence to the static trade-off model of capital structure. As for seasoned equity offering, we find that average stock reaction is significantly negative, which is consistent with all existing studies. Firms issuing seasoned equity offerings experience less negative stock price return if they have higher post-issuance long-term debt ratio and lower the pre-issuance liability/assets ratio relative to the industry average, which suggest that, whenever seasoned equity is issued, valuation of the firm goes down with the decrease of leverage, and market participants instead favor higher long term leverage.