Does consideration matter to China’s split share structure reform?

This paper investigates the effects of the reform of split share structure on the Chinese capital markets. The study adopts an event study methodology to examine the share price performance around the announcement of the reform by using a sample of companies included in the China Securities Index 300. We find the three-day cumulative abnormal returns (CAR) to be negative and significant around government announcement of the reform on 29 April 2005, but the three-day CAR around company’s announcement of the reform is positive and significant. This change of sentiment in the market is attributed to the release of information about the reform process specifically, the type and level of consideration. By regressing the company’s CAR on the type and level of consideration, we show evidence to suggest that type of consideration matters, where investors prefer payment of shares from capital reserves or retained profits, cash, warrants or any combination of these methods as opposed to payment of shares made by non-tradable shareholders. However, no relation is observed between level of consideration and CAR suggesting that investors perceive the consideration to be adequate based on the company’s financial and operating conditions at the time of the reform. Overall, these results suggest that the reform of split share structure (the second time around) exerts a positive impact on a company’s share price and the extent of this effect is a function of the type of consideration.

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