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Abnormal Returns in Privatization Public Offerings: The Case of Portuguese Firms

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resumo | résumé / abstract

Neste trabalho analisamos a evidência sobre o comportamento dos retornos das acções das empresas privatizadas em Portugal entre 1989 e 2001. O objectivo do nosso trabalho foi de recolher evidência sobre o desempenho em bolsa de uma amostra abrangente de operações públicas de privatização e avaliar os factores determinantes do desempenho observado. Os resultados obtidos confirmam a existência de retornos anormais positivos no dia e mês após a venda das acções em bolsa, mas os retornos são de reduzida magnitude e com reduzida significância estatística. Além disso, os retornos observados para as acções das empresas privatizadas são inferiores aos observados para empresas privadas que realizaram Ofertas Públicas Iniciais. No longo prazo, o desempenho é negativo mas superior ao observado para as acções de empresas que efectuaram OPIs. Os resultados sugerem assim que há reversão parcial dos retornos iniciais e ainda que os investidores exigem retornos mais elevados para acções de empresas que são privatizadas parcialmente.

La présente étude analyse les rendements excédentaires des émissions relevant de privatisations au Portugal dans le période de 1989 à 2001. Nous étudions les performances boursières, initiale et à moyen et long terme, pour un échantillon qui comporte l’ensemble des privatisations portugaises (ouverture initiale et ventes subséquentes), et les facteurs qui expliquent cette performance. Les offres des entreprises publiques observent un rendement initial positif mais modeste, vis-à-vis le rendement de référence et, en moyenne, sont moins rentables que celles achevées par les entreprises au capital privé. Les rendements excédentaires cumulés registrent une performance négative pendant une période de 3 à 5 ans, mais la perte est inférieure à celle générée par les émissions initiales de entreprises au capital privé. Les résultats suggèrent donc que le rendement initial est partiellement reversé et que les actionnaires demandent des rendements supérieurs pour les privatisations partielles.

This paper provides evidence on abnormal returns of Portuguese privatization public offerings for the period from 1989 to 2001. This study explores the abnormal performance of a comprehensive sample of Portuguese privatization transactions and investigates the determinants of the observed price behavior. We find some evidence of the underpricing phenomenon for privatized offerings but initial returns are low and barely significant. The results show further that privatization IPOs underperform private sector IPOs. In the long run, we observe negative abnormal returns. While in early event months, privatization public offerings yield more negative returns than private sector offerings, this effect is reversed in longer horizon periods. Initial underpricing is thus partially reversed and investors seem to require higher returns in partial privatizations.

JEL Classification: G38; G32

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A considerably high number of studies document the phenomenon of underpricing of privatized firms in the short run and positive abnormal performance in the long run. This study measures short- and long-term abnormal returns to investors in Portuguese privatization public offerings and investigates the determinants of the observed price behavior. The empirical analysis is based on a comprehensive sample of privatization transactions that took place on the Portuguese stock exchange for the period from 1989 to 2001.

Documenting and understanding the short- and long-term market performance of privatization public offerings in different countries can shed light on the debate upon the impact of privatization programs on the firm’s value and on whether the performance is tied to particular characteristics of a privatization program (aims, strategies and methods). The contribution of this paper is to extend the analysis of the literature on privatization public offerings providing additional evidence regarding a single country program. Previous empirical studies are mainly multi-country studies that analyze transactions across markets or single-country studies that focus on “voucher” privatization programs of economies in transition (countries from Central and Eastern Europe).

Our paper tests several theoretical predictions that have been put forward in the literature. In particular we investigate the role of political strategies and dual listing in the short and long run performance of privatization public offerings.

Our results are not supportive of the underpricing phenomenon except when we exclude the very extreme observations. Our results show further that privatization IPOs underperform private sector IPOs. These results contradict most of the previous evidence. The degree of underpricing seems to reflect uncertainty and not a strategic political policy to retain power.

In the long run, we observe negative abnormal returns contradicting the most recent evidence. While in early event months, privatization public offerings yield more negative returns than private sector offerings, this effect is reversed in longer horizon periods. Initial underpricing is thus partially reversed and investors seem to require higher returns in partial privatizations.

This paper is organized as follows: Section 2 provides a brief overview of the Portuguese privatization program. Section 3 describes the sample. In Sections 4 and 5 we review the relevant literature, describe the tests and variables and present the results for, respectively, the short and long run market performance. Section 6 concludes our study.

2. The Portuguese Privatization Program

The Portuguese privatization program started in 1989, well after the privatization wave in developed European countries initiated by Margaret Thatcher’s British government back in the early 1980’s. The late launch of the program was due to the political and legal environment created by the 1974 Revolution and the massive process of nationalizations that followed. Only in 1998 as a part of a broad set of economic reforms, was the transfer of state holdings to the

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1 See for example Choi and Nam (1998) that look at 185 PIPOs from 30 countries over the period from 1981 to 1997. Yet some studies on Central and Eastern European privatization offerings also find that the difference in initial returns between IPOs and Private IPOs is insignificant.

2 Megginson, Nash, Netter and Schwartz (2000) find positive and statistically positive long-run (1-5 years) returns for a sample of 158 PIPOs from 33 countries from 1981 to 1997.

3 This result is consistent with recent empirical literature that finds Privatization Initial Public Offers (PIPOs) outperforming private IPOs. Moreover, there is worldwide evidence of negative long-term returns for private IPOs (see for example Jenkinson and Ljungqvist, 2001).

4 The nationalization process in Portugal started in 1975 and was extensive to all sectors in the economy: banks, insurance companies, oil, transport, energy, telecommunications, pulp and paper, beverages, etc.
private sector begun. Initially only sales of minority shareholding positions were allowed but that was changed in 1990, when the Law of Privatization was approved. The main stated objectives of the privatization program therein, were similar to those announced in most European countries. Besides the reduction of state ownership in itself, the program aimed at raising cash to reduce public debt and budget deficits; improving economic efficiency through the use of markets to allocate resources; submitting companies to transparent corporate governance rules; developing domestic capital markets; and disseminating share ownership5.

The privatization methods used by the Portuguese government changed over time but the preferred method was sales through Public Offerings held in the Portuguese stock exchange. The method of Direct Sales was used, exceptionally, for small companies, and supposedly when national political and economic interests were at stake6.

Table 1 shows the annual proceeds of the privatization public offerings over the period from 1989 to 2001. Sales were spread over time but 1992, 1997 and 1998 were important years with sales amounting to respectively, 1.3, 2 and 2.2 billion Euros. Total capital raised amounted to 8.8 billion Euros in 66 transactions. There was a predominance of partial privatizations and over time, there were important differences in the transactions, in particular regarding the industries of the privatized firms7. By 2001, privatized firms accounted for more than 50% of total market capitalization.

3. Sample

We have identified the transactions in Dathis, a financial database compiled by the Portuguese stock exchange and that is the most comprehensive data set on Portuguese stocks. We have collected data on offer size, initial offer prices, offer dates and quotes.

Table 2 shows the descriptive statistics for gross proceeds of the transactions that constitute our sample. The sample includes 42 privatization transactions, of which 19 are initial offers (Privatization Initial Public Offers – PIPOs) and 23 are secondary (seasoned) offers (Privatization Seasoned Public Offers – PSPOs). Inevitably PSPOs are more common in later years, and after 1998, the Portuguese government only launched subsequent offers. The proceeds of the 42 privatization transactions in the sample represent 96% of the total proceeds of all privatization public offers in Portugal for the period analyzed. The remaining transactions refer to sales of small firms that were sold on the stock exchange but were not listed on the main regular market8.

As documented in other privatization studies (see for example Jelic and Briston, 2003), the effective open market trading of the shares of privatized firms after the official IPO date is often a long process and there is a substantial variance in time to listing across firms. This delay results from the design of the operation, in particular legal constraints on trading9. For the PIPOs in the sample, the median time to listing was 43 days.

5 By the end of 1988, the Portuguese stock market was short-lived, illiquid and tiny. Aggregate market capitalization was then below 4 000 million Euros. By the end of 2001, aggregate market capitalization was above 73 thousand million Euros (down from 116 thousand million Euros by the end of 2000).
6 This was the case of GALP, the Portuguese oil refinery and distribution company.
7 The initial transactions involved banks, insurance companies and brewers.
8 In April 1991, the new Capital Markets law (Lei Sapateiro) set up three market segments in the Portuguese stock exchange. Regular firms, i.e. those firms meet all exchange requirements (in terms of capital dispersion, market capitalization and solvency), are listed on Mercado de Cotações Oficiais (Market with Official Quotations). Small and medium firms list on Segundo Mercado (Second Market). The firms that do not meet the exchange requirements are traded on Mercado Sem Cotações (Market Without Quotations). From 2005 on, all stocks listed either on Mercado de Cotações Oficiais or Segundo Mercado became listed on Euronext Lisbon.
9 For example, in Portugal, buying shares of privatized companies allowed tax allowances subject to a minimum required holding period. The same applies for special tranches reserved to employees, immigrants, small investors and even clients, placed at a discount relative to the offer price but again required a minimum holding period.