

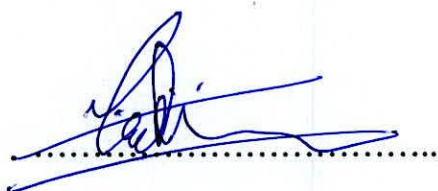
Stock Price Reaction to Announcements of Right Issues and Debenture Issues: Evidence from Colombo Stock Exchange

By

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**A thesis submitted to the University of Sri Jayewardenepura in
partial fulfillment of the requirements for the Degree of Master of
Science in Management on 31st January 2013**

The work described in this thesis was carried out by me under the supervision of Dr. P.D. Nimal and a report on this has not been submitted in whole or in part to any university or any other institution for another Degree/ Diploma



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Date: 6th June 2013

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I certify that the above statement made by the candidate is true and that this thesis is suitable for submission to the University for the purpose of evaluation.


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Dr. P. D. Nimal

Date: 6th June 2013

Supervisor

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List of Abbreviations

CSE – Colombo Stock Exchange

SEC – Security and Exchange Commission

MAR – Mean Adjusted Return

IM– Market Adjusted Return

MM - Market Model

CAPM – Capital Asset Pricing Model

ASPI – All Share Price Index

ASTRI – All Share Total Return Index

SEO - Seasonal Equity Offering

DW- Durbin Watson

EW - Event Window

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Stock Price Reaction to Announcements of Right Issues and Debenture

Issues: Evidence from Colombo Stock Exchange

Udani Chathurika Edirisinghe

ABSTRACT

This study was carried out to investigate the stock market reaction for right issues and debenture issues of Colombo Stock Exchange (CSE) during the period of 2005 to 2011. In absence of seasonal equity issues in CSE, right issues have been considered as equity issues and debenture issues have been considered as debt issues. During the sample period, 138 right issue announcements and 30 debenture issue announcements were reported, from which only 96 right issue and 20 debenture issue announcements were qualified for the sample. Study Methodology was used to investigate the ex-ante and ex-post market reactions, for the two types of security announcements while predicting abnormal returns, based on three alternative normal/expected returns modeling methods. Namely Mean Adjusted Model, Market Adjusted Model, and Capital Asset Pricing Model, further, a cross sectional regression analysis was carried out to assess the factors affecting price reaction, around security issue announcements.

For right issue announcements listed companies of CSE reacted positively during the 30 days prior to the announcement and started to react negatively from 2 days after the announcements according to all three methods utilised to generate abnormal returns. Though a cumulative abnormal return (CAAR) of the three day event window is

positive, the CAAR after Day 2 was significantly negative. Market reacted negatively during the period prior to debenture issues and continued to do so during the post event window as well. Though the non-zero CAAR on immediately around announcement day (day -1,0,+1) was not statistically significant, the negative returns of 30 days and 10 days pre and post to the announcement were significant. Again the direction of the price reaction was not significant. Though the magnitude and significance of abnormal return generated through three alternatives normal return modeling methods differs, the pattern of the CAAR of all three models were similar, this confirms the previous findings on multiple model usage. Cross sectional regression analysis reveals a significant positive influence of issue size on price reaction/abnormal returns of issuing firm and significant negative impact of pre offer leverage ratio on price reaction/abnormal returns of the issuing firm. Finally the analysis reveals that CSE is not efficient in semi strong form sense