

Stock Market Reaction to Corporate Real Estate Divestitures and Acquisitions during the Global Financial Crisis

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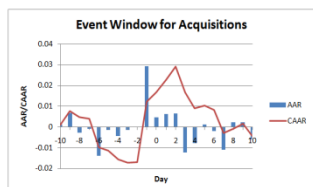
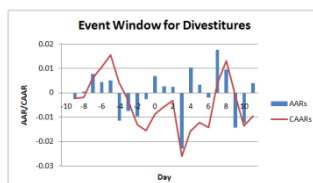
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Graphical abstract



Abstract

Real estate divestitures and acquisitions (D&A) are conducted as part of corporate restructuring. This study aims to fill the knowledge gap on abnormal stock market returns (AR) toward D&A activities during the Global Financial Crisis (GFC) in a developing country. Malaysian listed non-real estate companies that conducted D&A during the GFC are used as sample. Event study is applied to determine AR surrounding D&A announcements within (-10day, +10day) event window. Results for both D&A announcements shows insignificant AR on and around announcement date (-1 to +1). For pre-announcement, divesting (acquiring) companies obtain negative (positive) AR, signifying that the market does not favor (favor) divestitures (acquisitions) due to leakage of information. The outcome of post-announcement proves that divesting companies continue to experience negative ARs, although most divesting companies were paid premium prices. However, acquiring companies experience significant and negative post-announcement AR. This is probably due to the price premium which most acquiring companies paid exceeding valuation for their acquisitions. In summary, the market disapproves divestitures in general and acquisitions of real estate assets exceeding their valuations during economic recessions.

Keywords: Divestiture; acquisition; real estate assets; economic recession

Abstrak

Pelucutan dan perolehan harta tanah (D&A) dilakukan sebagai sebahagian daripada penyusunan semula korporat. Kajian ini bertujuan untuk mengisi jurang pengetahuan mengenai pulangan pasaran saham yang tidak normal (AR) terhadap D&A aktiviti sepanjang tempoh kemelesetan ekonomi di negara membangun. Syarikat bukan hartanah Malaysia yang tersenarai yang mengendalikan D&A sewaktu krisis kewangan 2008 digunakan sebagai sampel. Kajian Acara digunakan untuk menentukan AR sekitar pengumuman D&A dalam (-10day, +10day) tingkap acara. Keputusan untuk kedua-dua pengumuman D&A menunjukkan AR insignifikan pada dan sekitar tarikh pengumuman (-1 kepada +1). Untuk pra-pengumuman, syarikat pelucutan (perolehan) mendapati AR negatif (positif), menandakan bahawa pasaran tidak memihak (memihak) pelucutan (perolehan) disebabkan kebocoran maklumat. Hasil selepas pengumuman membuktikan bahawa syarikat-syarikat pelucutan terus mengalami AR negatif, walaupun kebanyakan syarikat melupuskan telah dibayar harga premium. Walau bagaimanapun, syarikat-syarikat perolehan mengalami AR yang signifikan dan negatif selepas pengumuman. Ini mungkin kerana kebanyakan syarikat perolehan membayar premium melebihi penilaian untuk perolehan mereka. Ringkasan, pasaran tidak bersetuju akan pelucutan secara umum dan perolehan harta tanah melebihi penilaian dalam situasi kemelesetan ekonomi.

Kata kunci: Pelucutan; perolehan; aset harta tanah; kemelesetan ekonomi

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1.0 INTRODUCTION

Companies execute real estate divestiture and acquisition (D&A) activities to restructure or reorganize to keep up with shifting economic environment.¹ Specifically, D&A can be interpreted as a company's adjustments of its ownership and business portfolio structure. The motives for D&A activities may vary contingent

upon existing economic circumstance and therefore the announcements of similar activities may obtain differing market reaction on the companies' share prices. This is particularly crucial in economic recessions as companies divest and acquire assets to urgently enhance their operating performance.² There is very little evidence on market reactions for D&A activities by listed public companies in depths of recessions. In addition,

previous empirical studies on the announcements of D&A activities are typically focused on the developed markets.

This study aims to contribute by examining market reaction towards D&A announcements during the 2008 Global Financial Crisis (GFC). Distinctively, this study deduces whether D&A announcements create wealth for the announcing company through abnormal market returns (AR) over a (-10day to +10day) event window around the announcement date. The recession period began from Q4 in 2008 to Q3 in 2009 are bounded with the Gross Domestic Product. Samples of Malaysian listed non-real estate companies that conduct D&A activities during the 2008 financial crisis is used.

2.0 LITERATURE REVIEW

2.1 Corporate Real Estate

Real estate holds an essential capacity in a company as resources. Real estate is a prime asset that can be restructured in order to

meet occupational, operational, development and investment requirement.³ This is because real estate is a noteworthy substantial asset for Malaysian listed non-real estate companies.

The selected 500 non-real estate companies in 2001 collectively owned RM96.27billion, corresponding to 20.7% of the total market capitalization (RM465billion) of Bursa Malaysia and 24% of the total tangible assets of these companies.⁴ Asian non-real estate companies have higher real estate holding intensity (i.e. percentage of real estate held as total tangible assets) than their US and European counterparts, with numerous large corporations possess their own prestigious administrative headquarters in turn to intensify their corporate image.⁵

2.2 Market Reaction to D&A Announcements

Table 1 below summarizes recent studies conducted on AR from D&A activities. Majority studies do not categorize the underlying economic climate.

Table 1 Empirical studies on assets divestitures and acquisitions

Divestiture studies			Acquisition studies		
Authors	Event window	Summary of Findings	Authors	Event window	Summary of findings
Glascok <i>et al.</i> (1989)	(-5, -1)	The empirical evidence had shown a weak positive market reaction.	Owers and Roger (1986)	(-1, 0)	Ambiguous and inconclusive. Averagely, acquirer experienced positive ARs
Ronald (1990)	(0,0)	Significant effect on AAR for overall sample	Glascok <i>et al.</i> (1989)	(0, 0)	No ARs for property acquirers
Lasfer <i>et al.</i> (1996)	(-1,0)	Market reaction to sell-off announcements is positive	Glascok <i>et al.</i> (1991) ^a	(0, 0)	No significant ARs for property acquirer making multiple acquisitions except there are significant returns for a sub-sample of sole property purchasers.
Liow (1997)	(0,0)	Corporate creates significant positive value enhancement to property trades disposal announcements	Booth <i>et al.</i> (1996)	(0, 0)	No ARs for property acquirers
Alexandrou and Sudarsanam (2001) ^a	(-2, 0)	Sell-offs announcements result in positive during recession period which generate larger wealth gains than those during economic boom.	Ooi <i>et al.</i> 2002	(0,0)	Significant positive grow linked with announcements of successful land acquisition
Campbell <i>et al.</i> (2003)	(0, 0)	positive significant abnormal returns to sell-offs announcement	Brounen and Eichholtz (2001)	(0,0)	positive share price reaction to the announcement
Francis <i>et al.</i> (2004)	(0, +1)	The study has shown positive abnormal return.	Fu and Ching (2003)	(0,0)	Positive abnormal share price return subsequent to land acquisitions news for both economic booming and recession period
Ting <i>et al.</i> (2006) ^a	(+1, -1)	Significant positive response for buoyant period and significant negative price effect during recession period.	Ooi & Sirmans (2004)	(0,0)	No significant impact take place to whole real estate industry after test real estate firm which involve acquires land
Fogh (2009)		not statistical significant found during booming and recession period	Ting (2007) ^a	(0, 0)	Not significant on announcement date but there are significant pre- and post-announcement ARs.

^a Denote studies which differentiated buoyant and recession economic conditions.

Only two divestiture studies were conducted under distinct economic conditions and both had contrasting results.⁶⁻⁷ The responder are significantly positive during buoyant period and significantly negative throughout recession period.⁴ In contrast, the sell-offs announcements result in positive AR during recession period such induce larger wealth taking than those found during economic burst.⁶

The acquisition announcement during recession are generally no significant AR on acquisition announcements within recession period.¹⁰⁻¹¹

3.0 METHODOLOGY

This research is conducted using event study to determine any AR surrounding real estate divestiture and acquisition announcements. The event study is competent in assessing the effect of various singular events.¹² This method is comprehensively used as tool to calculate consistent and valid outcome of any signals in depicting management’s outlook opportunity.¹³

The event window is defined as the no. of days surrounding the announcement date (day 0). The event window used in this study consists of 21days which begins 10 days prior to announcement up to 10 days after (-10days to +10days) to capture both leak and/or lag effects.

The estimation window is the specific period of time used as proxy for normal return. The length of estimation window used in this study is 120 days (i.e. day -130 to day -11) prior to event window. The AR is the actual return of company subtracts actual return of Bursa Malaysia FTSE Index throughout the estimate period and event window. This is based on the Market-Adjusted Return Model.

The share prices are obtained from DataStream and the daily closing share prices must be accessible, but not less than 130 trading days prior to announcement until 10 trading days after. The samples are announced D&A activities within 1 October 2008 to 30 September 2009 from publicly listed non-real estate companies during the Malaysia economic recession. In addition, the transactions are only paid by cash-based. The D&A announcement dates were identified from company announcements on Bursa Malaysia.

$$\epsilon_{i,t} = R_{i,t} - R_{m,t}, \quad (1)$$

where,

$$R_{i,t} = \frac{P_{i,t} - P_{i,t-1}}{P_{i,t-1}}, \quad (2) \quad R_{m,t} = \frac{P_{m,t} - P_{m,t-1}}{P_{m,t-1}}, \quad (3)$$

$\epsilon_{i,t}$ are normal return or abnormal return; $R_{i,t}$ are the actual return of i company at t day, where $P_{i,t}$ are share price for i company at t day and $P_{i,t-1}$ are share price of i company a day before t day; and $R_{m,t}$ are actual market return, Bursa Malaysia FTSE Index, where $P_{m,t}$ are share price of market, m at t day and $P_{m,t-1}$ are share price of market, m a day before t day.

Cumulative Average Abnormal Return (CAAR) can define the strength of market adjustment in response to the new information signal attained from the company-related announcement.¹⁴ The computation of average abnormal return (AAR) of CAAR for window period from -10 day to +10 day are reckon as following:

$$CAAR_{a,b} = \sum_{t=a}^{t=b} AAR_t, \quad (4)$$

where,

$$AAR_t = \frac{\sum_{i=1}^n \epsilon_{i,t}}{n}, \quad (5)$$

$CAAR_{a,b}$ = cumulative average abnormal return in an event window from day a until day b .

AAR_t = average abnormal returns on day t

The significance of AAR is tested using t-test while verification on time series abnormal return tested using paired-sample t-test.

The hypothesis for this study is:

H_0 : no AR from D&A announcement within the event window.

H_1 : AR from D&A announcement within the event window.

4.0 RESULTS AND DISCUSSION

4.1 Descriptive Analysis

From the data compounded, there are 35 and 40 announcements for divestitures and acquisitions of non-real estate companies respectively. The breakdown of announcements as specified by sectors is shown in Table 2 below.

Table 2 Numbers of property divested and acquired according to sectors

Sectors	Number Real Estates of Announcements	
	Divestiture	Acquisition
Construction	2	-
Consumer	8	8
Finance	2	-
Industrial Product	14	16
Plantation	1	3
Trading Services	5	13
Technology	3	-
Total	35	40

Table 3 Types of property divested and acquired

Types of Property	Number of Companies	
	Divestiture	Acquisition
Vacant Land	17	19
Land Together with Buildings	9	7
Office Building	4	5
Factory	1	2
Others	4	7
Total	35	40

The type of properties divested and acquired within the recession period from fourth quarter in year 2008 to third quarter in year 2009 for listed non-real estate companies are tabulated in Table 3 as follows. According to the table, the most ordinary type of property divested and acquired is vacant land.

4.1 Data Analysis

Figure 1 illustrates the AARs and CAARs for divestiture companies within the 120-days estimation window. AARs fluctuated randomly and were no constant except CAARs as a whole comprise negatives values. The market is viewed as unfavorably to any potential leakage of information during the estimation window.

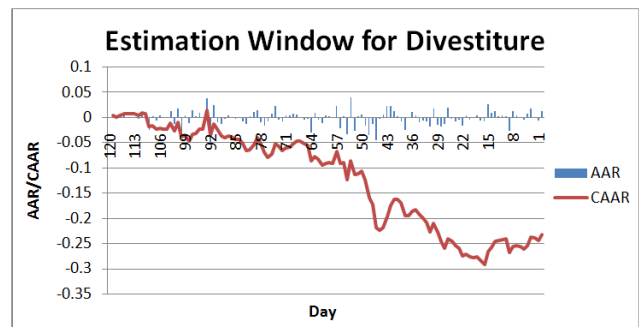


Figure 1 The AARs and CAARs in 120 days estimation window for divestiture

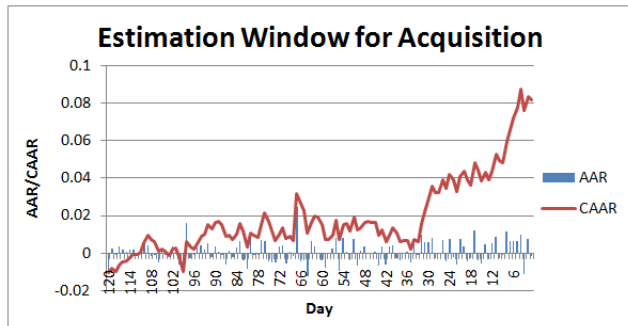


Figure 2 The AARs and CAARs in 120 days estimation window for acquisition

Figure 2 shows the AARs and CAARs for acquiring companies within 120 days estimation window. The AARs in the graph illustrates unsystematic fluctuation and on the contrary, overall CAARs had positive values and were raising though the estimation window. This movement possibly sourced by positive response towards leakage of acquisition announcements that disagrees from divestiture announcements. The CAAR contradicts earlier results on the divestiture sample.

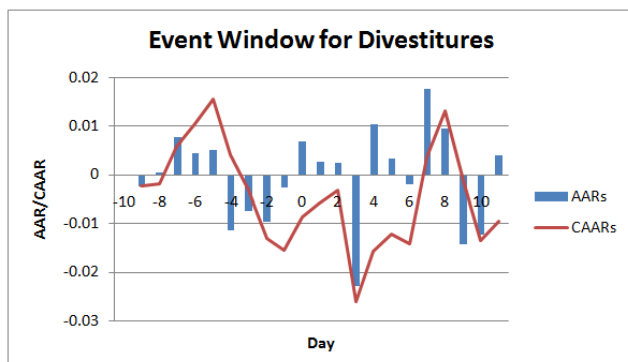


Figure 3 Divestitures: The AARs and CAARs in event window (-10days to +10days)

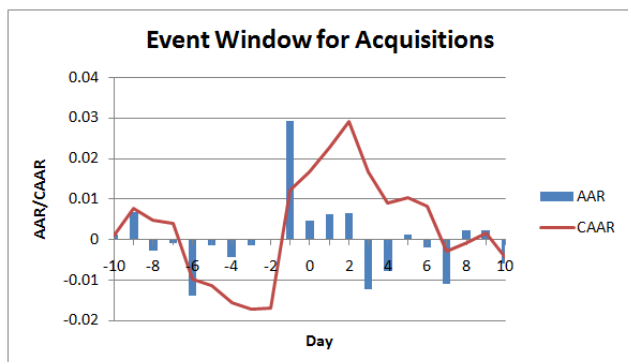


Figure 4 Acquisitions: The AARs and CAARs in event window (-10days to +10days)

Based on Figure 3, share prices from day -8 to day -2 demonstrated negative AARs. Meanwhile, share price were positive on day -1 until day 2 and the specify AARs were 0.02%, 2.92%, 0.47% and 0.61%. These negative and consequent strong

positive market reactions specify that bad and good information concerning acquisitions may perhaps leaked into the market. CAARs as whole had encountered both negative and positive value throughout the event window. Surrounding the acquisition date, the CAAR from day -2 to day 2 indicated positive AR. Whereas, CAAR fall-offs from then on until day 10.

Figure 4 shows share prices of divesting companies experienced negative AARs from day -4 to day -1. However positive AAR was shown on day 0 until day 2. CAAR was overall negative from day -3 up to day 6 of the divestiture. Hence, the investors seem to react positively to acquisition and negatively to divestitures during the financial crisis.

4.3 Significance Tests of Abnormal Return

4.3.1 T-Test on AARs Values

The t-test and significant level of AARs are analyzed using One Sample t-test as shown in Table 4. On the announcement day, majority divesting companies have exploited improved share prices. Nonetheless, only certain AARs on day -3, day 7, day 8 and day 9 are significant at 0.1 level, and day 2 significant at 0.01 level.

Most of the calculated AARs are not statistical significant at any levels, reasonably affected by the relatively large standard deviation of the sample. This is because the greater the value of the standard deviation, the more spread out or dispersed a data set is expected to be. The standard deviation of the sample might be reduced by involving additional companies in the analysis.

On day 0, the AARs are positive but not significant for both D&A. Acquisition announcements are preceded with significant positive AAR on day -1 while divestiture announcements have significant negative AAR on day -3. Post-announcement results show significant negative abnormal returns for both D&A announcements in day 2 for divestiture and days 3 and 4 for acquisitions.

4.4 T-Test on CARs Values

4.4.1 T-Test on Cumulative Average Abnormal Returns (CARs) Over Selected Window Intervals

Table 5 shows the dissimilarity in AR under the event window, figured using paired t-test. Significant changes for divestiture are negative post-announcement in (+1,+2) and (0,+2). The probable rationale may be caused by discharged of further information into the market to the public after the announcement date.¹⁵ The investors continuously monitor and evaluate the disposal and acquisition property information that spread out into the market over time.

Similarly, significant changes for acquisition are negative pre-announcement (-8,-6), (-7,-3) and (-2, -1). However, the CAAR became significantly positive circulate the announcement date (-2,-1). CAAR surrounding announcement date for acquisitions (-2,+2) are all positive.

Cumulative average abnormal returns (CAARs) were calculated over day -1 to +1 to encapsulate the share price effects of the divestiture announcements after announcement day.¹⁶ This is to cater for all companies that announced D&A activities after trading closed on event date or any leakage of information prior to the announcement. Within day -1 to day 1, there is no significant CAAR of 0.0054 and 0.0107 respectively for divestiture and acquisition announcements.

Table 4 T-test on AARs values during the event window for divestitures and acquisitions

Day	Divestiture			Acquisition		
	AARs	Standard Deviation, S_t	p-value	AARs	Standard Deviation, S_t	p-value
-10	-0.002237	0.046620	-0.284	0.001071	0.026866	0.252
-9	0.000447	0.024105	0.110	0.006647	0.032780	1.283
-8	0.007758	0.080986	0.567	-0.002826	0.046719	-0.383
-7	0.004450	0.036842	0.715	-0.000863	0.025103	-0.217
-6	0.005161	0.066022	0.462	-0.013817	0.037238	-2.353 **
-5	-0.011350	0.048861	-1.374	-0.001413	0.043485	-0.206
-4	-0.007441	0.059376	-0.741	-0.004375	0.033922	-1.207
-3	-0.009740	0.030896	-1.865 *	-0.001576	0.054957	-0.181
-2	-0.002527	0.053858	-0.278	0.000171	0.047539	0.023
-1	0.006903	0.056736	0.720	0.029177	0.104327	1.769 *
0	0.002833	0.056009	0.299	0.004663	0.059463	0.496
1	0.002592	0.041774	0.367	0.006052	0.028912	1.324
2	-0.022894	0.043198	-3.135 ***	0.006318	0.041077	0.973
3	0.010432	0.053501	1.154	-0.012390	0.038257	-2.048 **
4	0.003421	0.056335	0.359	-0.007782	0.024735	-1.990 *
5	-0.001860	0.076941	-0.143	0.002165	0.055671	0.144
6	0.017679	0.083303	1.256	-0.002156	0.027745	-0.491
7	0.009540	0.028567	1.976 *	-0.011050	0.041913	-1.667
8	-0.014336	0.044861	-1.891 *	0.002170	0.032670	0.420
9	-0.012369	0.038435	-1.904 *	0.002251	0.029850	0.477
10	0.004070	0.034658	0.695	-0.005883	0.036678	-1.015

Note: $p < 0.1 = *$, $p < 0.05 = **$ and $p < 0.01 = ***$ with 2 tail statistical significant.

Table 5 Test of significant cumulative average abnormal return (CAARs) for D&A announcement over different cumulative periods

Period(a,b)	Divestiture		Period(a,b)	Acquisition	
	$CAAR_{a,b}$	t-test		$CAAR_{a,b}$	t-test
(-10,-4)	-0.001	-0.070	(-10, -8)	0.004	0.387
(-8,-6)	0.010	0.835	(-8, -6)	-0.015	-2.536 **
(-4,-2)	-0.012	-1.252	(-7, -3)	-0.021	-1.908 *
(-2,-1)	0.007	0.720	(-2, -1)	0.029	1.769 *
(-1,+1)	0.005	0.449	(-1, +1)	0.011	1.058
(+1,+2)	-0.023	-3.135 ***	(0, +2)	0.012	1.656
(0,+2)	-0.203	-2.118 **	(+1,+2)	0.006	0.973
(+3, +6)	0.192	1.156	(+2, +4)	-0.020	-3.099 ***
(+7,+10)	-0.023	-2.338 **	(+5, +7)	-0.013	-1.650
(+8, +10)	-0.004	-0.490	(+8, +10)	-0.004	-0.490

Note: $p < 0.1 = *$, $p < 0.05 = **$ and $p < 0.01 = ***$ with 2 tail statistical significant.

5.0 DISCUSSION AND LIMITAATIONS

The results of AARs surrounding **divestiture** and **acquisition** announcement dates (-1,0,+1) are not significant at any levels. However, the result differs from previous studies shows that share prices of divesting companies will sustain a positive abnormal return on the date of the announcement of the divestiture, even during the period of worldwide financial catastrophe.^{6,8}

Moreover, the outcome of acquisition and divestitures of CAARs (-1, +1) is not significant. The CAAR (-1, +1) was found

coherent with several previous studies.^{1,17,11} The results exemplify that there is no significant abnormal return for acquisition and divestiture announcements. However, studies during economic growth from the UK and US confirm positive abnormal returns for divestiture announcement. Also, pervious discovered significant positive reaction to Malaysia property acquisition announcement for the period of economic burst.¹¹ As a result, the economic condition at the time of announcement initiate significant in influencing wealth return in terms of AR.

Table 6 Companies divested property under valuation or net book value

Companies	Disposal Price (RM)	Valuation (RM)	Latest Net Book Value (RM)	Loss* (RM)
Ho Wah Genting Bhd	7,000,000	7,500,000	8,409,942	500,000
Tracoma Holdings Bhd	7,800,000	-	8,547,000	747,000
Rhythm Consolidated Bhd	7,000,000	-	8,011,641	1,011,641
Sarawak Concrete Industries	20,000,000	22,000,000	-	2,000,000
Woodlandor Holdings Bhd	3,000,000	3,400,000	2,447,936	400,000
FSBM Holdings Berhad	4,154,726	4,400,000	-	245,274
PMB Technology Bhd	5,071,429	-	5,123,369	51,940

* Loss is calculated by Valuation minus Disposal price. When the valuation is not available, we use the net book value.

Divestiture results showed weak positive AR on announcement day and CAARs (+1, +2) and (+0, +2) that are negative and significant at 0.01 and 0.05 levels, correspondingly. The dissimilarity possibly explained by the financial wellbeing of divesting companies in the sample.⁶ This study contained 35 divesting companies, where 20% appear to be distressed companies. These companies disposed their properties at prices

lower than valuation and/or latest net book value, as shown in Table 6. Hence, these companies confront with financial distress where it requires to immediately carrying out financially motivated divestitures. Even though most of companies divested at premium prices, the market does not exerted to observe divestitures favorably.

Table 7 Companies acquired property under valuation or net book value

Companies	Acquisition Price (RM)	Valuation (RM)	Gain* (RM)
HiapTeck Venture Berhad	71.0 million	73.0 million	2million
Parkson Holding Berhad	84.04 million	104.4 million	20.36mil
Sitt Tatt Berhad	70.0 million	91.9 million	21.9million
Lii Hen Industries Bhd	4,800,000.00	2,580,000/-and 2,850,000/- respectively	630,000
Advance Synergy Berhad	26.78 million (5,450,000 euro)	5,600,000euro	150,000euro
Concrete Engineering Products Berhad	4,500,000.00	4,750,000	250,000
Spritzer Bhd	32.50 million	37,000,000.	4.5million

* Gain is calculated by Valuation minus Purchasing / Acquire price. When the valuation is not available, we use the net book value

In the acquisition sample, the aftermaths show significant positive return prior to and significant negative return subsequent to announcement day. The preliminary favorable response from market investor signifies the presence of leakage of information regarding potential acquisitions. This proves that the market views information on acquisitions favorably as positive events that can increase company wealth. The subsequent negative return possibly caused by market insight that the acquisitions were overrated in value. From the total acquisition sample of 40 companies, only 7 companies paid prices lower than valuation and/or initial acquired value. This is presented in Table 7 above. The remaining 33 companies (approximately 82%) might have overrated their capacity to extort value of acquired properties. Consequently, the acquirers have paid a premium over valuation for these acquisitions, which consecutively are not favored by the market.

This study faced a limitation of smaller size of 35 divestiture and 40 acquisition companies due to the recession time span. The study limitation on rather small number of sellers useable for analysis and the observed evidence had shown a weak positive market response simultaneously.

6.0 CONCLUSION

The results prove that both divestiture and acquisition announcements lead positive insignificant AR on and near announcement date (-1 to +1). Pre-announcement results explain

that divesting (acquiring) companies turn out negative (positive) abnormal return, signifying that any possible leakage of information on divestiture (acquisition) is not favored (favored) by the market. The results contravene studies carried out within economic burst, signifying that the elemental economic condition is particularly considerable in determining market reaction towards D&A activities.

Subsequent to announcement, results prove that divesting companies keep on encountering negative AR after announcements albeit most of similar companies divested at premium prices. The results are opposite for acquiring companies that subsequently encountering significant and negative abnormal return instead. This is credibly due to approximately 82% of acquiring companies paid a premium above valuation for the real estate assets.

This study documents that in an economic decline, the market detracts upon divestitures in general and acquisitions of real estate assets exceeding their valuations.

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