Bank Loan Announcement Effects—Evidence from a Comprehensive 8-K Sample

Introduction

How does the equity market react to the announcement of new bank loans? There have been many debates in the literature. However, these debates are based on limited data and observations. We on the other hand, present our studies using a comprehensive sample of bank loan announcements by matching all new loan facilities from the Thomson Reuters LPC Dealcan database with all 3.2 million 8-K filings downloaded from EDGAR from 1994 to 2018, out of which we found 11,595 B-K announcements of bank loans. We find significant positive loan announcement effects, which is consistent with the view that of Billett, Flannery and Garfinkel (1995) in that bank loans matter and its announcement can elicit positive response on borrower stock in the equity market. Therefore, our results challenge the findings of Maskara and Malineaux (JFE 2011) and also that of Fields et al (JMBC 2006), which indicated that announcement effect of bank loans on borrower stocks disappeared as of late. In addition, we investigate the determinants of the loan announcement effects. Specifically, we find that bank loans with lower loan spreads than its peers with similar default risk have larger announcement returns. Furthermore, we also find that, although information leakage (in the terms of the run-up of borrowers’ stock price prior to announcements) was quite significant in earlier sample periods, in recent periods there is much less information leakage prior to B-K announcements of bank loans, and at least in this aspect the Dodd-Frank Act can be deemed as quite effective.

Bank Loan Announcement Events

- 11,595 bank loan announcement events from 1994-2018, obtained by analyzing a comprehensive sample of SEC filings from EDGAR.
- EDGAR filings are matched with Dealcan, sample size is orders of magnitude larger than existing studies on similar topic, which was previously done by hand-collecting data rather than from a comprehensive source.

> Note: the 8-K announcement dates (i.e., event date) which we have compiled, turn out to be usually different from loan activation dates on Dealcan (Figure 2)

Loan Announcement Effects

In summary, to verify whether positive bank loan announcement returns still exist in our large sample, we adopt the event study methodology by calculating the cumulative abnormal returns (CARs). We find that significant and positive CARs do exist, even in recent time, contrary to studies that utilizes hand-collected data which conclude that these effects are absent. Table 1 shows the [-2,+2], [-3,+3] and [-5,+5] trading day CARs based on the FFS model and DGTW model for the full sample period and the three subsample periods (before August 23, 2004; between August 23, 2004 to July 21, 2010; post July 21, 2010). Figure 1 plots the CARs based on FFS model during the [-15,+15] window around the B-K loan announcement, indicating that there is a positive and significant announcement effect, although it also alludes to information leakage prior to the announcement date, which will be investigated in detail later.

Single Sort

Table 2 reports CARs across loan and borrower characteristics quintiles and the corresponding high minus low value. Panel A indicates that CARs for small firms are stronger than for large firms. Panel B shows CARs for large loans (measured in terms of loan-to-asset ratio) are stronger than those for small ones. Panel C indicates that CARs for loans with low abnormal spread are stronger than those of high abnormal spread.

Information leakage

To examine if there is any informational leakage (whether the stock price of borrowers started to move prior to the Form 8-K announcement of new bank loans) in context of the evolution of SEC disclosure requirements and the regulatory environment, we plot the CARs for pre loan announcement period and post loan announcement period in Figure 3. Panel A displays the CARs for full sample from January 1, 1994 to December 31, 2018. Panel B displays the CARs in three subsamples, respectively. We find that, although information leakage was quite significant in earlier sample periods, in recent periods, especially after the Dodd-Frank Act (2010), there is much less information leakage that can in part be attributed to more stringent regulations.

Double Sort

Table 3 reports CARs across double sorting groups based on i) firm size, and ii) loan characteristics (Loan-to-asset Ratio, or, Abnormal Spread). We find that positive and statistically significant abnormal returns can still exist for loan announcements of larger firms, in scenarios when the loan-to-asset ratio is high or the abnormal spread is low.

Conclusion

Using a comprehensive sample of 8-K filings, we aim to settle the debate on whether the equity market react to the announcement of bank loans by publicly traded companies. Several recent papers state that bank loan relationships matter less than what was documented in previous literature. However, these studies never utilized a sample of more than 1000 loan facilities. In contrast, we identified 11,595 new bank loan announcements. We find that there is a positive and significant market reaction in the borrower stock to the announcement of new bank loans, even in recent times, and even in larger firms (with large loan size or low abnormal spread) contrary to the claim that only the smallest firms have announcement effects. Furthermore, we also find that borrowers who had a better deal from the bank (lower loan spread relative to the loan spreads of peer firms with similar default risk in the same month) have larger positive returns in the equity market (and vice versa).

Finally, we document that, although information leakage (in terms of the run-up of borrower stock price prior to announcements) was quite significant in earlier sample periods, in recent periods there is much less information leakage prior to B-K announcements of bank loans that can in part be attributed to more stringent regulations, and at least in this aspect the Dodd-Frank Act can be deemed as quite effective.

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