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Effect of International Listing on Liquidity and Profitability

KEYWORDS: International Finance, International Listing, Depository Receipts

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ABSTRACT *Globalisation and Liberalisation of the world economy has bring tremendous reforms in the financial sector which leads to the promotion of diversified, efficient and competitive financial system in the nation. International listing is the way our companies can put themselves in the international front by circulating their securities in foreign market. This paper is throwing light on how companies can list their securities in foreign market and the effect of the same on companies' liquidity and profitability. It has been found that international listing does not directly affect the company's liquidity and profitability, but indirectly affects the company's image and scope of operations, which positively affects the fund raising capacity and profitability of the company.*

Introduction

Year 1991 saw first signs of liberalisation of Indian economy under the Prime Minister Mr. P.V.Narsimha Raw with the implementation of L.P.G process. Various sectors of Indian economy have undergone the reform phase, where financial sector is one of them. Various reforms have been brought in the financial market (including capital market). Globalisation has integrated the national economy and has created a new financial environment with lot of opportunities and challenges to the business concerns.

Globalisation and Liberalisation of the world economy has bring tremendous reforms in the financial sector which leads to the promotion of diversified, efficient and competitive financial system in the nation. This financial reform along with the use of technology has increased competition, mergers, takeovers, cost management, quality improvement, financial discipline etc. In this globalised market doors are kept open for the foreign companies to enter in to our country as well as our domestic companies are free to enter in the foreign markets. Now in globalised economy business concerned not only raise capital from domestic market but also from the foreign markets.

International Finance

Companies raise their capital from the public whether in the form of equity or debt. After the globalization and liberalization, domestic company can not only raise the capital from the domestic market but also from the foreign market such finance can be raised by issuing A.D.R, G.D.R & F.C.C.B. and also through the direct listing of the domestic shares either it is fresh issue or not. As a part of globalising the economy, the government undertook two major steps like;

i. Foreign Institutional Investors allowed to invest in Indian capital market and;
ii. Indian companies are permitted to float their stocks in foreign markets.

International Listing

Instead of listing the securities in a domestic security market only, companies now days get listed their securities in various securities markets. Such internationalisation of securities markets has brought the securities of foreign companies within the reach of institutional and house hold investors around the globe.

Why should firms get internationally listed?

The companies go international through cross border listing for the following reasons.

i. Financial reasons

a. In order to enjoy lower cost of capital in markets that gives a higher value to their business.
b. To get the finance at the time of depression in the domestic market.
c. Willingness to pay more to their share holders by creating value in foreign market.
d. To get the benefit of the boom situation of the foreign securities markets.

i. Business reasons

a. To be multinational company.
b. To create their foreign identity.
c. Marketing of product and improving their visibility.
d. To curb the potential market in the foreign countries.

Depository Receipts

As India has followed the route of new economic reforms and liberalisation the Indian corporate too developed a global vision. Until now the Indian companies fulfil their financial requirements from the domestic market only at high interest rates. With the opening up of the financial market, Indian companies joined the 1990's world wide rush to raise capital by issuing Depository Receipts.

Meaning of Depository Receipts

Depository Receipt is a negotiable financial instrument issued by the bank (depository) that represents foreign companies publicly traded securities. The Depository Receipts are traded on local stock exchanges. It facilitates in buying shares of foreign companies. The issuer of DRs pays dividend in terms of domestic currencies, which is converted in the foreign currency by the depository. Payment is also made to the holders in their currency. When such type of Depository bank is in the USA, the instrument issued by it is known as American Depository Receipts (ADRs). European Depository bank issues European Depository Receipts (EDRs) and other banks issues Global Depository Receipts (GDRs).

Objectives of the Study

The study is an effort to find out that, whether international listing affects the liquidity and profitability of the com-

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pany or not by keeping following objectives;

1. To throw light on International finance and International Listing.
2. To examine and evaluate Liquidity position of the companies understudy.
3. To examine the Profitability position of the companies understudy.

Literature Review

Karoyli (1998) research on Foreign Listing has mixed evidence- in this majority of studies envisaged an increase in liquidity where as a few studies recorded decrease in liquidity. Amihud and Mandelson (1994) in their study shows dual effect of multi-market trading, on one hand they suggested that competition between markets should foster innovation and reduce trading costs, it resulted in to narrow bid-ask spread and hence the market liquidity improve. On the other hand they pointed to the possibility of fragmentation of trade in the multiple exchanges. Nathani, Sandhar, Vigg and Holani (2007) According to the researcher's study, listing on foreign stock exchanges should not affect a firm's liquidity. International listing should result in higher proportion of current assets, which in turn balances the liquidity position of the company.

Research Methodology

The study has been carried out on two Indian internationally listed companies Satyam Computer Services Ltd. and Dr. Reddy's Laboratories Ltd. Both the companies got listed internationally in the year of 2001. Under this study researcher has taken period of two years before and after, to examine and evaluate the effect of international listing on Liquidity and Profitability. To study liquidity researcher has considered Current, Cash and Liquid ratios whereas to study Profitability Net Profit, Return on Capital Employed and Return on Equity ratios have been calculated and Paired T- test has been applied.

Data Analysis

Data has been analysed to check whether international listing positively affect Liquidity and Profitability of selected companies or not. Following is the table showing Liquidity and Profitability ratios of both the companies before and after international with the hypothesis;

H_1: There is no positive effect of international listing on liquidity of the companies under study.

H_2:-There is no positive effect of international listing on Profitability of the companies under study.

Table:-1 Table showing Average Liquidity ratios to selected companies

Companies	Satyam Computer Services Ltd.		Dr. Reddy's Laboratories Ltd.	
Ratios/Period	Before	After	Before	After
Liquidity Ratios				
Current	4.55	6.33	4.18	5.96
Liquid	4.44	6.26	2.67	4.61
Cash	1.81	4.36	0.23	2.48

(Source: Calculated from the Annual Reports)

The above table clearly shows that there was no big change in current ratio of both the companies after international listing where as the drastic improvement is observed in the cash ratio of both the companies.

Table:- 1.1 Test values at 5% level of Significance

Liquidity Ratios	Calculated value of T	Critical value of T
Current	0	- 6.314
Liquid	0	- 6.314
Cash	-17.14	- 6.314

From the test values it can be seen that in case of current and liquidity ratio null hypothesis is accepted as the calculated value of T lies in the acceptance region whereas in case of cash ratio null hypothesis is accepted.

Table:- 2 Average Profitability Ratios and Test Values

Companies	Satyam Computer Services Ltd.		Dr. Reddy's Laboratories Ltd.	
Ratios/Period	Before	After	Before	After
Profitability Ratios				
Net Profit	22.98	25.52	13.46	27.58
Return on Capital Employed	27.02	22.95	17.80	24.55
Return on Equity	48.48	18.84	19.99	26.62

(Source: Calculated from the Annual Reports)

The above table shows positive as well as negative effect of international listing on profitability ratios. Net profit ratios of both the companies improved after international listing. Return on capital employed and Return of equity improved in case of Dr. Reddy's but declined in case of Satyam computers.

Table: 2.1 Test values of Profitability ratios at 5% level of significance

Profitability Ratios	Calculated value of T	Critical value of T
Net Profit	-1.43	-6.314
Return on Capital Employed	-0.25	-6.314
Return on Equity	-0.63	-6.314

Although there seems positive effect in terms of improvement in the ratios, but test values clearly indicate that this improvement is not significant as the calculated values lie in the acceptance region and thus, the null hypothesis is accepted.

Conclusion

From the findings it can be said that there is no any direct effect of international Listing on Liquidity and Profitability of the company but, certainly it affects the company image and put it on the global front and thus, indirectly International Listing increases the value of company in domestic as well as foreign market which helps in expanding the business operations of the company and hence, increase the possibility of improvement in profitability in future.

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