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The effect of antidumping and countervailing investigations on the market value of firms☆

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ABSTRACT

Using a sample of listed Chinese firms between 2006 and 2012, we analyze the effect of international business strategy and government assistance on the stock market response to antidumping and countervailing investigations. We find a significantly negative abnormal return surrounding the announcements of antidumping and countervailing investigations. Furthermore, the establishment of a plant in a non-subject or "non-named"[1] country and government assistance are positively related to the abnormal returns of antidumping and countervailing investigations. Our results suggest that government assistance is as important as strategic restructuring to offset the negative effect of trade remedy investigations.

1. Introduction

In an increasingly competitive international market, antidumping and countervailing actions are used as motivation to protect domestic firms from possible injury by unfair trade (Brander & Spencer, 1981; Gayle & Puttitanun, 2009; Jung & Lee, 2003; Reynolds, 2006). With more than 40 World Trade Organization (WTO) member countries initiating 4230 antidumping investigations and 302 countervailing investigations from 1995 to 2012,[2] these types of trade remedy actions against imports have become widespread (Feinberg & Reynolds, 2008; Schuler, Rehbein, & Cramer, 2002).

Previous research on antidumping and countervailing investigations shows that antidumping and countervailing duties result in a significant change in business operation by exporting firms (Peng, Wang, & Jiang, 2008). These trade remedy actions lead to exporting firms' dramatically increasing the unit values of the named products to reduce the dumping margin (Avsar, 2013). However, the increasing price results in the loss of their competitive advantage (Brenton, 2001; Ganguli, 2008). As antidumping and countervailing investigations can directly affect a firm's profitability, it is important to examine the reaction strategy to these temporary trade barriers. Once the antidumping or countervailing duties are imposed, investigated firms may respond by locating production within the destination market to bypass tariff barriers (Belderbos, 1997; Blonigen, 2002; Blonigen, Tomlin, & Wilson, 2004). Expanding other markets is also an effective way to avoid a trade barrier (Bown & Crowley, 2007).

In this study, we analyze the effect of international business strategy and government assistance on the stock market response to antidumping and countervailing investigations. We address two main questions. How does the stock market in an exporting country react to antidumping and countervailing investigations? What factors affect the stock market reaction to antidumping and countervailing investigations?

We use a sample of listed Chinese firms that suffered antidumping and countervailing investigations between 2006 and 2012, to examine stock market reactions. China is a particularly useful starting point for a variety of reasons. First, China was the first leading target of antidumping and countervailing actions filed by other countries from 1995 to 2012.[3] Specifically, there were 442 antidumping cases and 59 countervailing cases launched against Chinese firms from 2006 to 2012. Second, considering that China is a non-market economy country, antidumping agencies are likely to impose higher duties on Chinese firms (Zeng & Liang, 2010). This makes it necessary to find a way to offset the negative effect of trade remedy investigations.

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[1] As antidumping and countervailing investigations are country-specific, antidumping and countervailing duties are imposed only on imports from countries named in the petition. Following Ganguli (2008), we call such country a named or subject country. In contrast, the country not named in the petition is called a non-named or non-subject country.

[2] The data are from the semi-annual reports of WTO Members to the WTO Committee.

[3] These data can be accessed at http://www.wto.org/.

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1057-5219/

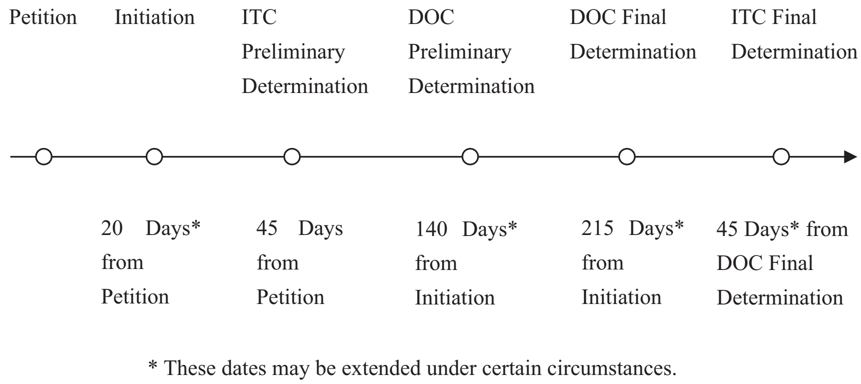

Fig. 1. Statutory time frame for antidumping investigations in the United States. This figure presents the statutory timeframe for antidumping investigations in the United States (US). Source: United States Department of Commerce (http://www.commerce.gov).

We find a significantly negative abnormal return surrounding the announcements of antidumping and countervailing investigations. When firms establish at least one manufacturing plant in a non-named country or obtain more government assistance, the market responds more favorably to antidumping and countervailing investigations. This result suggests that government assistance is as important as strategic restructuring when firms undergo antidumping and countervailing investigations.

This study contributes to the literature in theoretical and practical ways. First, this study focuses on investors' expectations of the change in future firm value caused by antidumping and countervailing investigations. The influence on the export prices of products, trade diversion, and technology adoption decisions is considered in previous research (Avsar, 2013; Crowley, 2006; Prusa, 2001). In comparison, this study directly assesses how investors in the exporting country respond to antidumping and countervailing investigations and what factors affect this reaction. Our findings suggest that investors perceive the announcement of antidumping and countervailing investigations as an indication of the increasing operation risk and decreasing profitability in these firms.

Second, the findings of this study also have important practical implications. Our results are consistent with those of Belderbos, Vandenbussche, and Veugelers (2004) and Peng et al. (2008), who investigated how firms may react to antidumping and countervailing duties using foreign direct investment to bypass tariff barriers. We find that, along with a timely adjustment of international business strategy, government assistance is another important way to offset the negative influence of antidumping and countervailing investigations. These findings significantly add to our knowledge about the role of government in antidumping and countervailing investigations. Furthermore, as antidumping and countervailing investigations are worldwide phenomena, the findings from this study can be extended to other counties that are a target for antidumping and countervailing actions. China's experience of offsetting the negative influence of trade remedy actions may be of benefit to other countries.

The remainder of this paper is organized as follows. Section 2 develops the hypotheses and Section 3 lays out the methodology. In Section 4, we present a discussion of our results. Section 5 concludes the paper.

2. Hypothesis development

To protect domestic producers from unfair trade, antidumping duties and countervailing duties are imposed on foreign export firms if they export a product at a price lower than normal value or receive specific subsidies (Gallaway, Blonigen, & Flynn, 1999; Wang, 2010).

Antidumping and countervailing investigations comprise three basic events: petition, initiation, and decision. For example, Fig. 1 presents the statutory time frame for antidumping investigations in the United States (US). A petition is filed by a domestic industry injured by dumped imports. If the United States Department of Commerce (USDOC) determines that a petition satisfies all requirements under the law, it will publish a notice of initiation. The United States International Trade Commission (USITC) determines whether the imports are materially injuring domestic industry within 45 days. If both the USDOC and USITC make affirmative findings, the USDOC assesses duties against imports of that product as a percentage of the value of the imports and publishes a preliminary decision. The USDOC final determination comes out 75 days later and the final event is the USITC final determination, which leads to the imposition of antidumping or countervailing duties.

If one country launches its own investigation and ultimately charges extra duty on imports that are found to be hurting domestic producers, the price of these imports will increase. For example, Avsar (2013) finds that to reduce the dumping margin and avoid that threat, Brazilian exporters respond to antidumping duties by increasing the prices of their products to the target country. However, the increasing price results in them losing their competitive advantage. The market share of these exports decreases, and they are replaced by domestic products or other countries' products (Nieberding, 1999). Brenton (2001) and Ganguli (2008) focus on the trade diversion caused by antidumping cases and show that antidumping investigations divert trade flow from named countries. For example, in the case of US antidumping and countervailing investigations of photovoltaic modules and components from China, after the US made a ruling of 18.32%–249.96% antidumping duties and 14.78%–15.97% countervailing duties, the exports from China's photovoltaic producers to the US declined by 80% in 2012.[4]

As antidumping and countervailing investigations have a profound effect on firm business operation and profitability, exporting firms suffering the antidumping and countervailing investigations give a signal to the market that their firm performance is likely to be influenced by temporary trade barriers. Therefore, investors may perceive the announcement of antidumping and countervailing investigations as an indication of an increasing operation risk and decreasing cash flows in these firms. Thus, hypothesis 1 predicts that the announcement of antidumping and countervailing investigations is associated with a negative stock market reaction.

Uncertainty about antidumping and countervailing investigations makes it difficult for investors to identify the earning prospects of investigated firms. Therefore, investors will look for alternative sources of information to differentiate the quality of firms. We argue that effective strategies responding to temporary trade barriers can serve as a strong signal to ascertain the prospects of the investigated firm.

[4] The data is from the Ministry of Commerce of China (http://www.mofcom.gov.cn/).