

Accepted Manuscript

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PII: S0927-5398(18)30015-X
DOI: <https://doi.org/10.1016/j.jempfin.2018.02.002>
Reference: EMPFIN 1034

To appear in: *Journal of Empirical Finance*

Received date: 4 November 2017
Revised date: 28 December 2017
Accepted date: 26 February 2018

Please cite this article as: Almansour A., Ongena S., Bank loan announcements and religious investors: Empirical evidence from Saudi Arabia. *Journal of Empirical Finance* (2018), <https://doi.org/10.1016/j.jempfin.2018.02.002>

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Bank Loan Announcements and Religious Investors: Empirical Evidence from Saudi Arabia

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December 29, 2017

Abstract

We study how investors in a conservative Muslim society react to announcements of bank loans depending on their compliance with Shari'a law. We hand-collect 173 announcements of bank loans granted to listed corporations in Saudi Arabia, assess their issuance and estimate the reaction of the borrowing firms' stocks. We find that loans that are not Shari'a compliant are larger and are granted to larger firms. Controlling for firm and loan characteristics commonly present in other loan announcement studies, we further document that equity market investors react negatively to non-compliant loan announcements with the two-day cumulative abnormal return preceding the announcement up to 1.8 percentage points lower for the smaller non-compliant loans.

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