

# **The Characteristics and Performance of Chinese ADRs: Sponsored vs. Unsponsored**

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## **ABSTRACT**

This research empirically investigates the characteristics and performance of American Depository Receipts (ADRs) issued for Chinese companies or the Chinese ADRs. In particular, it compares the financial characteristics and investment performance of the different sponsored ADRs with the unsponsored ADRs. It further attempts to ascertain the major factors influencing the selection of the types of ADRs and to examine the impact of the ADR issuance on the volatility and liquidity in local market for the cross-listed firms.

## **BACKGROUND AND MOTIVATION**

The topic of ADR is not a new one. In fact, the first ADR was created by JPMorgan as a means for U.S. institutional investors to indirectly own shares of foreign companies back in 1927. Today, ADRs have increasingly become an important investment vehicle for both U.S. institutional and individual investors to invest in foreign equities and to diversify risk globally. In the U.S., the ADRs account for more than 15% of the entire U.S. equity market in excess of \$2 trillion, reflecting a growth of 100 times since 1980. As one of the largest emerging markets, China has also emerged as one of the major participants in the U.S. ADRs market. As for July 17, 2015, there are about 310 Chinese ADRs of which 158 are sponsored ADRs and 152 are unsponsored ADRs. Out of the 158 sponsored ADRs, 9 are private offerings. The sponsored Chinese ADRs started back in 1993 while all except one the unsponsored Chinese ADRs were created after 2008. This is an impressive development given the fact that China only opened its stock exchanges in 1990 and China has not been recognized as a market economy by its major trading partners. Since China has huge amount of capital for the local companies to tap into, it is therefore interesting to examine the motivation for the Chinese ADRs. Given the stage of Chinese economic development and the structure of its financial markets, it is conceivable that the requirements for being listed on the U.S. markets should be higher than those in the local markets. Therefore, the reputation and prestige effect of being able to trade in the U.S. markets should be a major factor for the sponsored ADRs, which may help increase the liquidity and reduce the volatility of the cross-listed firms in the local markets. Certainly, for those Chinese ADR companies that are not traded in the local markets, the main reason is probably the higher valuation concern through ADRs public offerings. In addition, for those large state-owned companies, ADRs offerings can be considered a step in the privatization process and an effort to enhance the corporate governance so as to increase the companies' global competitiveness. However, for the unsponsored ADRs, the main motivation is U.S. investors' demand for participating in the Chinese equity markets.

## **DATA AND RESEARCH DESIGN**

The data sample in this study includes a total of 301 Chinese ADRs with issuance dates from July 23, 1993 to July 17, 2015 covering all four types of ADR offerings. For the 149 publicly traded ADRs, 60 are traded on the New York Stock Exchange (NYSE), 46 on the Nasdaq Stock Market (NASDAQ), and 43 are on the OTC markets. There are 103 ADRs with new capital raised mainly offered at NYSE and NASDAQ. In addition, there are 48 Chinese ADRs that are single-listed depository receipts whose underlying shares are not publicly traded in China.

The basic financial information for these firms is retrieved from the COMPUSTAT database and the stock return information is obtained from the CRSP database. Stock daily abnormal returns are estimated relative to both the S&P 500 Index and the Chinese Shanghai Stock Exchange Composite Index (SSEX).

Both nonparametric and parametric tests are used to examine the important financial variables that may help explain the difference in sample firms between

- Sponsored ADRs with unsponsored ADRs
- ADRs without raising capitals and ADRs with capital raised
- Single-listed ADRs and cross-listed ADRs
- NYSE ADRs and NASDAQ ADRs

Stock returns and abnormal returns after the ADRs issuance are used to examine

- The short-term and long-term investment performance of the ADRs
- The explanatory power of a single-index factor using the S& P 500 Index and the SSEC Index

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