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Business strategy and financial consequences: The case of antidumping filings

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ABSTRACT

Does predatory pricing in an industry affect firm values? In this paper, we show that firms filing for antidumping benefit from this decision after controlling for endogeneity of filing decision. Firms with shrinking assets in the past are more likely to file an antidumping petition and market price of firms with more employees and more assets increase more compared to ones with fewer employees and less assets when they file for antidumping. Finally, we find that the correlation between market value changes in supplier industries and the filing industry is economically larger than that of customer industries, suggesting that supplier industries would suffer more if a domestic firm faces foreign competition.

1. Introduction

Product market competition often has financial consequences. Countless studies have attempted to assess the value implications of various strategic product market decisions such as entering/exiting markets, expanding/contracting operations, and new product introduction (Giroud and Mueller, 2011; Lippman and Rumelt, 2003; Rumelt, 1984; Barney, 1986; Montgomery and Wernerfelt, 1988; Brandenburger and Stuart, 1996; Cohn et al., 2011). In Giroud and Mueller, for example, relation between corporate governance and company performance is positive, and significant only in non-competitive industries, suggesting that product market competition has non-trivial impact on how firms operate. Similarly, Cohn et al. (2011) find that investors' response to product market related

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announcements (e.g. new products and clients) varies with firm information environment. Collectively, these evidences suggest that investors care about the link between product market competition and firm performance. In our paper, we contribute to this literature by investigating to what extent a particular form of product market competition, predatory pricing (dumping) in an industry, affects firm values.

When a firm in one country exports a product to another country at a price that is below the price it sells in its home country or below its cost of manufacturing, the firm is allegedly "dumping" the product in the foreign markets to gain strategic advantage (e.g., to develop foreign market share). The protection of trade through antidumping policies is an important political issue for economic policy makers. Between 1979 and 2004, U.S. firms filed more than 4900 antidumping petitions with the hope that courts would protect local industry from unfair competition by imposing penalty on suspiciously low-priced imports.

The decision to file an antidumping complaint is costly for firms. There are not only direct (e.g., legal) costs, but also indirect costs – i.e., a firm's reputation may suffer if the petition is turned down. There is also a significant free-riding problem: each firm expects other firms to file. Furthermore, endogenous protection literature argues that import penetration will force domestic parties to lobby more intensely for protection (see Blonigen and Figlio, 1998). Given these factors, it is not a priori clear which firm in an industry will choose to file for antidumping, and what kind of response the market gives to the firm filing the petition.[1]

In this study, we investigate which firm characteristics are correlated with the decision to file for antidumping and whether endogeneity of the antidumping filing decision changes the magnitude and sign of abnormal equity returns surrounding the day of antidumping filing. We use the abnormal change in market value surrounding the day of antidumping filing as a measure of market reaction to antidumping filing. There are two possibilities. First, because filing is voluntary, firms that expect to win an antidumping claim are more likely to file. This hypothesis predicts a positive reaction to antidumping filings. However, antidumping filing also signals a lack of competitiveness to the marketplace, hence the filing may be seen as a negative signal about future profitability and therefore reduces prices.[2] Using event study method, we find that the value of the firm that files for antidumping increases as much as 3% within three days surrounding the event date. In our analysis, we focus on endogeneity of filing decision as this decision can depend on firm characteristics. For example, firms that have been going through some financial troubles in the past may think that the competition coming from foreign firms may reduce their profitability, hence they may think that they are better off by filing an antidumping petition. An OLS specification that overlooks this endogeneity leads to an opposite and economically unreasonable finding. Specifically, using OLS, we show that firms that file for antidumping lose – 1.70% within three days surrounding the event data.

Our findings show that firms that have more assets and more employees are more likely to benefit for antidumping. One standard deviation in the composite firm size measure which captures these two aspects of firm size shows that firm value at the time of antidumping filing increases by 1.03%. Next, we investigate how the bilateral relation between the United States and other firms' countries affects the change in market value. When we test if antidumping filings are less likely to be won if there is a retaliation possibility (measured by existence of a bilateral relation) from the other country, we find no significant result.

Finally, we investigate the returns to industry with an antidumping filing transfer along the supply chain. Specifically, we assume that two industries are vertically related if one of the industries buys more than 10% of its inputs from the other industry (supplier industry) or sells more than 10% of its outputs to the other industry (customer industry). If customers of an industry are more likely to benefit from increased competition, then customer industry returns should be negatively correlated with the returns to the antidumping industry. However, if increased competition forces domestic firms

[1] Studies that have investigated the effect of antidumping filings on firm values include Mahdavi and Bhagwati (1994) and Blonigen et al. (2004), among others. Mahdavi and Bhagwati (1994) investigate the stock price response to cost-based dumping by Japan semiconductor producers and relief of dumping of U.S. semiconductor firms.

[2] Our study of the effect of antidumping on the supply chain complements prior works by Hartigan et al. (1989) and Hughes et al. (1997).