Applied Financial Economics ›

Volume 14, 2004 - Issue 18

Original Articles

Joint venture investments and the market value of the firm

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Pages 1325-1331 | Published online: 02 Feb 2007

Cite this article https://doi.org/10.1080/09603100412331313569

Abstract

The impact of Joint Venture announcements on the market value of UK listed companies is examined. Based on a sample of 158 announcements of either joint venture formation or joint venture activities, significant positive market-adjusted abnormal returns of 0.5% on the announcement date are observed. Cross-sectional analysis reveals that abnormal returns are significantly lower when undertaken by large companies, or where the project is located in Asia. On the other hand, market-adjusted returns are found to be significantly higher when the project is large compared to the size of the company undertaking the investment, and where the project is either domestic or located within the European Union.

Acknowledgements

The authors would like to express thanks to Ian Hirst and Seth Armitage for comments on earlier drafts of this paper.

Notes

Burton et al. (1999) restricted their analysis to a sample of asset purchases for which the value of the transaction was disclosed. Here, asset purchases (which are categorized as capital expenditures in the sample) are also analysed, but the analysis is extended to also include research and development announcements and product/market diversification projects by joint ventures. The size of the project was announced in 69 of the 158 cases of joint venture activity in our sample.

Emerging economies were classified as former communist countries in Eastern Europe and China.

The dataset was identified from various categories in the Extel database. Each announcement in the Extel categories of activities, assets, commercial operations, diversification, exploration findings, joint ventures and operations were carefully checked for information regarding joint venture activity. Each announcement normally offers at least a paragraph of information.

The use of alternative market indices was examined, but had a minimal impact since abnormal returns were calculated on a daily basis (Brown and Warner, 1985; Strong, 1992).

Whilst it was simple to identify if a project was undertaken as a joint venture, in many cases it was not clear whether it was a new joint venture or a partnership which was already established. For this reason the sample was not split between joint venture formations and investments by existing joint ventures.

The results of the market adjusted returns method (assuming β of 1 and a α of zero for all companies) were compared with the results of several other models including the market model using a beta calculated by making trade-to-trade adjustments. This method was not reported due to the large amount of data which is lost due to the limited observations available to estimate alphas and betas. There was no significant difference between the results of the various models except in cases where alphas and betas were estimated from very few observations. Abnormal returns and significance tests calculated using the market model, a trade-to-trade adjusted market model and a trade-to-trade adjusted index model are available from the authors upon request.

Analysis was also undertaken for a longer event window, from 3 days prior, to 3 days after, the day of the project announcement. No significant abnormal returns were observed for any day other than the day of the joint venture announcement.

Project size is calculated using only each partner's commitment and not the size of the whole project.

The correlation matrix is available from the authors upon request.

This significance was not repeated using a Mann–Whitney U independent samples test.