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The Impact of Pre Delisting Crisis on the Stock Price of Chinese Stocks

--The Case of "Bilibili"

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Abstract: Against the backdrop of the introduction of the US Foreign Company Accountability Act, the threat of trade tensions between the US and China to the fate of corporations has once again been exposed. The US increased regulatory scrutiny of Chinese stocks and then signing of an agreement between Chinese and US regulators regarding audit and regulatory cooperation. Although the risk of Chinese stocks being delisted has decreased in the short term, in the medium to long term, the risk of delisting and the pressure brought by trade frictions between China and the United States still exist for the company. This paper uses the event study method to analyze the degree of abnormality in the share price volatility of Bilibili, when the first pre-delisting list is announced and the company itself is on the list, reflecting the magnitude of the pre-delisting event's impact on Chinese stocks. The findings demonstrate that not only do the listed companies have abnormal fluctuations in stock prices, but the entire Chinese concept stock market has short-term negative impacts when the pre-delisting list is announced. Finally, based on the research results and previous literature, this article will provide relevant suggestions from the perspectives of the country, government, and enterprises.

Keywords: pre-delisting, China concept stocks, Bilibili

1. Introduction

China Concept Stocks are businesses that listing on overseas capital markets, but the legal company entity, the actual management and control rights remain within China

The Foreign Company Accountability Act (hereinafter referred to as the "FCAA") was voted by the US Congress to impose additional disclosure requirements on foreign companies listed in the US. By failing to comply with the Public Company Accounting Oversight Board's (PCAOB) rules for three years in a row, the bill mandates foreign issuers to ban trading in the US. And in December 2021, the Securities and Exchange Commission (hereafter referred to as the "SEC") revised the bill.The act permits the SEC to delist a foreign-listed firm from the Exchange if it doesn't submit the reports that the PCAOB requires for three consecutive years.

According to the disclosure documents on the SEC's official website, as shown in Table 1,40 companies were listed on the pre-delisting list from March to April 2022. In May, the number of

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companies reached a record high of 107. And as of July 30, 2022, there were 158 Chinese companies listed on the list. It also includes Alibaba, Aiqiyi, Baidu and other benchmarking enterprises.

Table 1: Provides statistics on the number of Chinese businesses with US locations that will be pre-delisting in 2022.

Time	List of pre-delisted companies
March	11
April	29
May	107
June	5
July	6

Compiled from disclosure filings on the SEC website.

1.1. Significance of the Research

The tension in trade and economic relations between the US and China is the primary cause of pre-delisting events. Few studies have been done on the effects of a single US-China friction event, although numerous scholars have studied the effects of economic and trade friction between the US and China on Chinese equities. The topic matter of such research has been enriched by the study of pre-delisting events, and it has also given theoretical support to cope with the associated risks.

According to the Act's requirements, the majority of corporations will need to be passively delisted from the US stock market by 2024. This crisis, which started in 2022, has not yet over. More direction is required in terms of how to approach pre-delisting events, how to respond to national governments and companies, and what can be done to support the long-term growth of Chinese equities during these two years.

1.2. Innovative Elements in the Article

The pre-delisting event is systematically examined in this essay. A lot has been written about the trade tensions between China and the US recently, both domestically and internationally, but most of the pre-delisting events are covered in the news and little specific analysis is provided. The painful aspect of the pre-delisting event is that once things go south and a company's pre-delisting turns into a confirmed delisting, the result is a delisting from the US stock market. Trade friction between the US and China has always existed, and it has an impact on the share price and development of Chinese stocks. The thesis begins with sketches out the pre-delisting event's larger backdrop, quantifies the event's impact, and closes with views from the standpoint of the country, government, and businesses.

2. Literature Review and Theoretical Basis

2.1. Literature Review

Chinese and foreign academics have long been interested in the topic of Chinese companies. The purpose of this section is to provide a reference for the pre-delisting event and lay the groundwork for the formulation of strategies. It does this by reviewing the literature of previous scholars to identify the macro background and fundamental contradiction of pre-delisting events.

2.1.1. Effective Disclosure

The background of the pre-licensing event is the introduction of the Act, and the core contradiction of the Act is the incomplete disclosure of information. Burton G.Malkiel, Eugene F.Fam put forward the "efficient market hypothesis" in their works [1], that is, the information is completely open in the fully efficient market. S. J. Grossman and J. E. Stiglitz argued that there is no complete information market [2]. Once the perfect hypothesis of the capital market is broken, the traditional view will be overturned, and the price cannot fully reflect all the relevant information. The most fundamental reason is that information is very expensive and rare. There is a direct contradiction between requiring companies to disclose information, market dissemination of information, public psychology and the reasons for market formation. Therefore, the article finally proposes that social welfare and other issues should be optimized to achieve the optimal allocation of the whole society.

More study on information disclosure has also been done by domestic scholars. The purpose of information disclosure is to address the information asymmetry that exists between investors and publicly traded companies, enabling investors to gain a more complete understanding of the company's performance and prospects, preventing unwarranted losses, and protecting small and medium-sized investors [3]. Disclosure of key audit matters can have a positive impact on audit quality, in particular, matters of different natures have varying degrees of influence on enhancing audit quality, disclosure of critical audit problems can therefore have a favorable impact on audit quality [4]. Thus, it is clear that increasing the disclosure of information about Chinese equities will help the securities market function more effectively. Due to several instances of financial fraud, the SEC is aware of the flaws in Chinese corporations' disclosure procedures. The Act requires more information disclosure by Chinese companies to close the information gap for small and medium-sized investors and make investment more logical from the perspective of safeguarding the interests of small and medium-sized investors. Investors have historically been at a disadvantage due to incomplete disclosure of company information. The Act compulsorily requires Chinese companies to disclose more information, which can narrow the information gap between small and medium investors and make investment more rational.

2.1.2. The Chinese Stock Market Crisis

By comparing the various listing requirements in the Chinese and US stock markets and looking at operating data from US-listed businesses, Xiao find that many companies go public in the US when they can't meet the Chinese stock market requirements [5]. Companies that lack comprehensive strength are also more susceptible to sniping by shorting companies. According to Chen , financial fraud, weak internal control and governance systems of companies, dissimilar disclosure information systems in China and the US, and a lack of knowledge of the global capital market are the main causes of Chinese stocks being repeatedly targeted by shorting agencies in the market [6].

2.1.3. Implications of the FCAA

The promulgation of the Act had a great impact on the Chinese stock market. Shen et al. contend that the Act's implementation is not accidental and that three factors—short-, medium-, and long-term overlapping [7]. The short-term factor is the fraud of Luckin Coffee, which leads to a crisis of confidence in the information disclosure of Chinese concept stocks. This has also become the focus of Sino-US consultation and US regulatory enforcement. The medium-term factor is the need to distract internal tensions by timing the growth of the New Crown Pneumonia pandemic in the US with the approach of the US election. The Act contains numerous political clauses that are directed against China. The separation of the US and China in the financial industry is a long-term factor. According to Liang, The promulgation of the Act, will be bad for domestic technology and finance

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[8]. The sustained decrease in US shares of Chinese companies would, to some extent, convey pessimism to Hong Kong and A-shares due to the transmission effect between the US, Hong Kong, and A-share markets. Because of the SEC's adherence to the case-by-case principle, which can target the suppression of Chinese concept stocks, making it difficult for them to raise capital and putting them at risk of being delisted and shorted. This would prevent Chinese high-tech companies from accessing the market to raise money and take part in the latest wave of industrial and technological change. According to Huang Long, the additional disclosure requirements in the Act will undoubtedly make it more difficult and expensive for US-listed companies to disclose information, which will deter Chinese companies from going public in the US and accelerate the current downward trend in their share prices [9].

2.2. Foundational Theories

To further strengthen the academic theoretical foundation of the thesis, the second section of the theoretical foundation introduces the theories of information asymmetry and economic regulation, analyzes the underlying contradictions of the pre-delisting incident, the reasons for the contradictions, and provides the theoretical basis for recommendations

2.2.1. Information Asymmetry Theory

Joseph Stiglitz, George Akerlof, and Michael Spence, three American economists, were the ones who initially put up the notion of information asymmetry. According to the theory of information asymmetry, there are differences between the two parties in a trading relationship in terms of their access to and knowledge of pertinent information. Those who have access to more relevant information are typically in a better position than those who lack it, and those who lack it are frequently on the weaker side.

Small and medium shareholders are particularly vulnerable to infringement of their interests in stock markets where information asymmetries are common. When one of the two partie s- firms or investors - is often at a disadvantage, imbalances can develop, the market may turn disorderly, and eventually an economic crisis may occur [10]. Governments frequently enact financial regulations to safeguard investors' interests, reduce the vulnerability of financial markets, and stop them from moving in the direction of irreversibility. The US side believes that there is low transparency of information disclosure in Chinese companies because prior financial frauds in Chinese stocks also exploited the information asymmetry between the Chinese and US markets, which caused no small amount of turmoil in the US stock indices. The US market and investors have weakened trust in Chinese companies. To prevent the stock market volatility caused by incomplete information disclosure, the U.S. SEC strengthened the supervision of foreign companies ' information disclosure and issued the Act.

2.2.2. Economic Regulation Theory

Stigler was the first to put forth the theory of economic regulation, which Posner and Peltzman later added to. This theory is called, the purpose of the government's financial supervision is not to improve the efficiency of economic operation and protect the interests of investors in the securities market. It is a kind of supply and demand. The ultimate goal is to realize the profits of the interest groups behind it [11-13]. According to Stigler, the examination of financial regulation should be based on market supply and demand, and the interests of both parties should be taken into account before determining if regulation is necessary and how much regulation should be implemented [11]. Bernstein declared his utter opposition to regulators who seek to protect the public interest in 1995. He argued that since regulatory authorities would be completely controlled by industrial capital,

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they would be unable to carry out their duties effectively and that financial regulation should be appropriately deregulated. Foreign companies were deterred from going public in the US by the implementation of the FCAA, which also hurt US investors who made investments in foreign firms and weakened confidence among foreign investors in US capital markets.

3. The Impact of the Pre-Delisting Crisis on the Stock Price of Bilibili

3.1. Business Profile

Bilibili was established on December 30, 2016, in Shanghai, China. It is currently a video platform and cultural community for young Chinese people. Information technology, computer hardware and software, network technology development, etc. are all included in the company's business area. The primary business activities of the company are split between live streaming, advertising, e-commerce, comics, etc.

Bilibili was successfully listed, raising US$483 million, on the NASDAQ in the United States on March 28, 2018. The transaction code is BILI, which is associated with the Internet industry in the tertiary sector. As of March 17,2021, US stocks closed, and BILI had increased to US$111.35. This means that Bilibili 's stock price has risen more than ten times, this also makes everyone full of expectations for the return of Bilibili to the Hong Kong market. On March 29,2021, it was listed in Hong Kong for the second time. At the time of the first financial report, the U.S. shares of Station B rose by nearly 5 %. However, after the opening, they were dragged down by many factors and finally closed down by 6.83 %. The attitude of mainstream institutions towards Bilibili is in contrast to the trend in share prices, with JP Morgan setting a higher target price for Bilibili and Goldman Sachs keeping its Buy recommendation on the company with a target price of HK$1,205. The future business model of Bilibili is very promising.

3.2. The Stock Price of Bilibili

3.2.1. Research Approaches

The case study, event study, and literature analysis methodologies are all used in this paper.

We select the Chinese company Bilibili, which is on the sixth batch of pre-delisted companies announced by the SEC, as a case study in this paper to examine its share price when the two events occurred, when it was not on the pre-delisting list and when it was on the pre-delisting list and when it was on the pre-delisting list, at the same time. By synthesizing pertinent domestic and international literature and sorting out the core contradictions behind the pre-delisting are examined using the event study method based on the literature. To investigate the dynamic impact route of events on the target variables, continuous observations over a chosen window period can be made using the event study approach, which looks at trends in the target variables before and after a series of events of the same type [14].

An event I is set as: the first batch of pre-delist announcement list on March 8,2022; event II is set as: Bilibili boarded the pre-delist on May 4,2022.

3.2.2. Sources of Data

The NASDAQ China Golden Dragon Index was chosen as a sample of market indices, with the daily NASDAQ China Golden Dragon Index market returns from May 10, 2021, to May 5, 2022, and BILI was chosen as a sample of individual stocks for the study. The data are from CSMAR database.

3.2.3. The Confirmation of the Estimation Period and Event Window Period

There is no objective criterion for the selection of the estimation window, and too short a window may lead to bias in the estimation of the model parameters, while too long a window may lead to structural changes. For the estimation model built with daily returns, the estimation window is typically in the range of 100-300 days [15]. In this paper, the event day of Event I and Event II is the event base day, defined as the 0th trading day (t=0). The event estimation window is determined to be 210 to 45 trading days before the event date. The date of Event I is from 2021.5.10 to 2021.12.31, and the date of Event II is from 2021.7.6 to 2022.3.1, which is marked as t = [-210, -45] for both.

Table 2 shows the event dates and estimation periods for events I and II:

Table 2: Lists the dates of occurrences and the estimation windows for events I and II.

Event	Event day	Estimation window
EventI	2022-3-8	[-210，-45]
EventII	2022-5-4	[-210，-45]

3.3. Research Methodology

In order to create market model equations for individual stock returns (R_{it}) and market returns (R_{mt}) on Bilibili share prices, this study uses the market model.

$$R_{it} = \alpha_i + \beta_i \times R_{mt} \quad (1)$$

The estimation window of events I and II is substituted into the regression analysis of parameter equation, and the results are shown in Figure 1 and Figure 2.

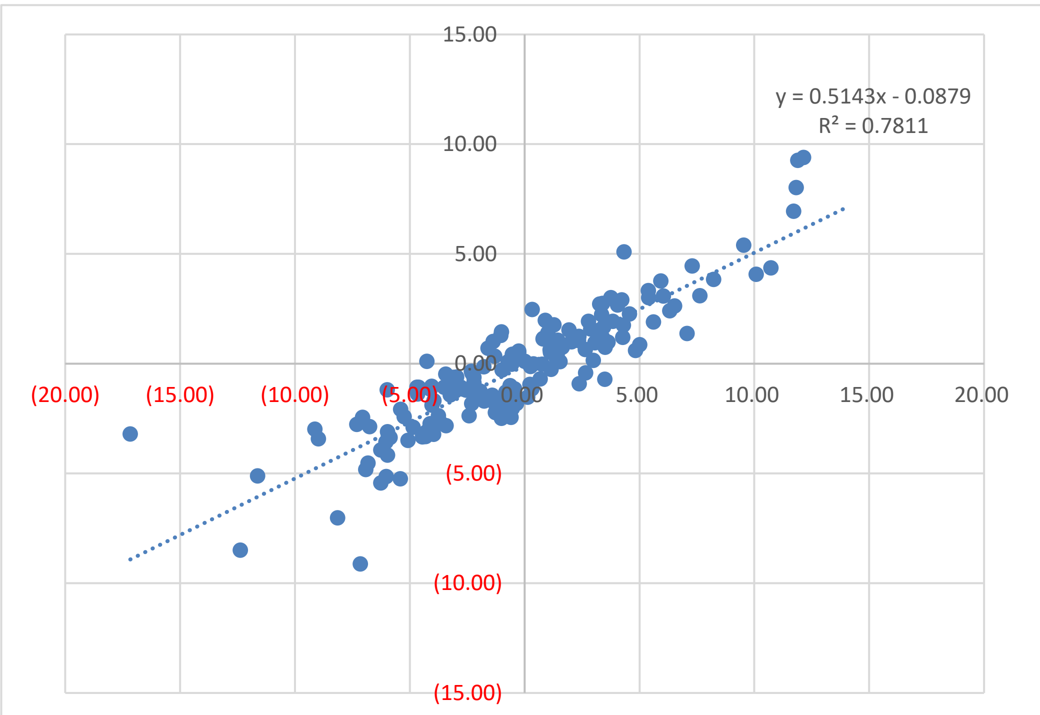

Figure 1: Shows the results of regressing actual returns against market returns over the anticipated Event I period.

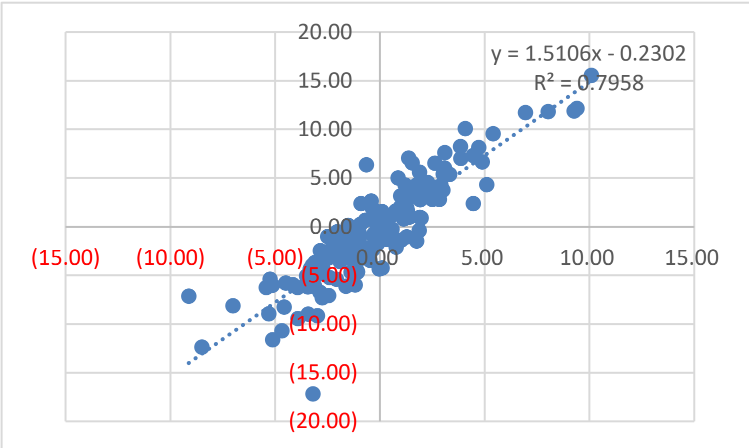

Figure 2: Shows the results of regressing real returns against market returns for the anticipated Event II period.

Arrange the parametric equations to get Table 3:

Table 3: Equations for the parameter values that were produced by incorporating the estimating window into the market model equations for Events I and II.

Event	parametric equation	α	β
EventI	y = 0.5143x - 0.0879	- 0.0879	0.5143
EventII	y = 1.5106x - 0.2302	- 0.2302	1.5106

The α and β values of events I and II are substituted into the formula to obtain Table 4.

Table 4: How to get the parametric equation by substituting certain values for others in the equation.

Event	parametric equation
EventI	$R_{it}'=0.5143R_{mt}'- 0.0879$
EventII	$R_{it}'=1.5106R_{mt}'- 0.2302$

The daily market return rate of the Nasdaq Golden Dragon Index with window period t = [-210, -45] is substituted into the regression equation,the expected return rate Rit ' of BILI stocks of event I and event II can be obtained.

Table 5 displays the predicted rates of return for Event I, while Table 6 displays the anticipated rates of return for Event II.

Table 5: Event I anticipated returning.

Date	The events period	Expected yield(%)
2022.3.7	-1	-2.56
2022.3.8	0	-0.12
2022.3.9	1	3.23

Table 6: Expected Return for Event II(continue).

Date	The events period	Expected yield(%)
2022.5.2	-2	3.346
2022.5.3	-1	-0.471
2022.5.4	0	3.224
2022.5.5	1	-11.896
2022.5.6	2	-7.855

In the event window, the difference between the actual rate of return and the expected normal rate of return is the abnormal rate of return (hereinafter referred to as the "AR"). The cumulative abnormal return (hereinafter referred to as the "CAR") is obtained by accumulating the abnormal return rate. AR and cumulative abnormal return CAR can be used to test the impact of pre-delisting events on Bilibili stock price.

The abnormal rate of return calculated by the market model:

$$AR_{it} = R_{i,t} - R_{m,t} \tag{2}$$

The cumulative abnormal return calculated by the market model:

$$CAR_{it} = \sum_{t2}^{t1} AR_{it} \tag{3}$$

3.4. Model Outcomes

The event window period of event I is shown in Table 7:

Table 7: The cumulative returns and abnormal event I returns.

Date	The events period	AR（%）	CAR（%）
2022.3.7	-1	-5.45	-0.98
2022.3.8	0	-2.95	-3.93
2022.3.9	1	7.96	4.03

Figure 3 displays a trend graph based on the abnormal returns AR and CAR in Table 7:

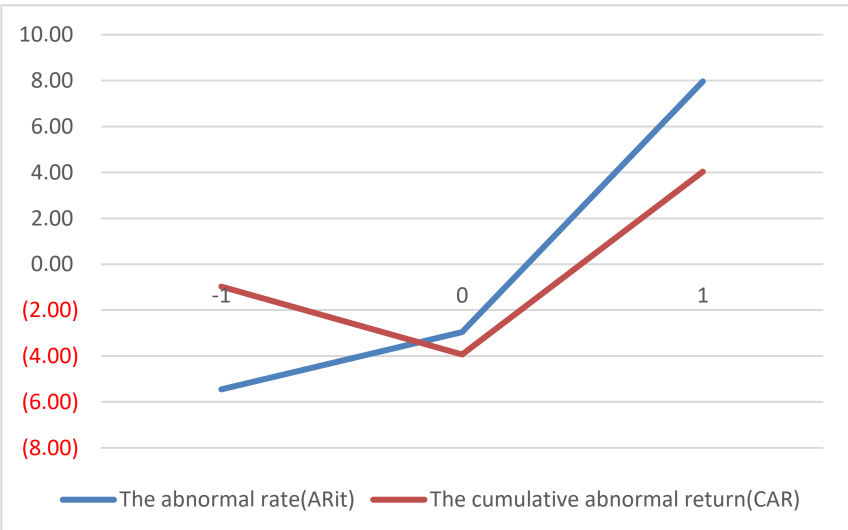

Figure 3: The share price volatility of BILI at the time of the initial pre-delisting list release.

Despite the fact that BILI did not at the initial pre-delisting list, it can be inferred that the announcement of the pre-delisting list was a significant blow to the majority of Chinese companies in the US based on the analysis of the results in Table 7 and Figure 3. The abnormal return increased from -5.45% the day before the event to -2.95% on the day of the event to 7.96% the day after the event date.

Table 8 displays the advantages acquired throughout the Event II event window:

Table 8: The cumulative and abnormal returns for Event II.

Date	The events period	AR（%）	CAR（%）
2022.5.2	-2	-2.853	-2.853
2022.5.3	-1	-3.904	-6.757
2022.5.4	0	-0.317	-7.074
2022.5.5	1	1.218	-5.856
2022.5.6	2	4.831	-1.024

Figure 4 displays a trend chart based on Table 8's AR and CAR:

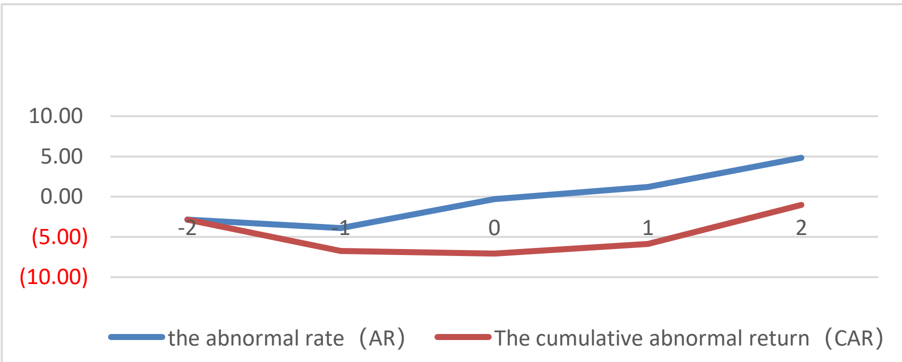

Figure 4: Bilibili share price volatility when Bilibili was on the pre-delisting list.

From the day before it was listed on the pre-delisting list to two days after the event date, Bilibili experienced a significant spike in abnormal return (AR) and a sharp abnormal share price movement, as shown by the findings in Figure 4. BILI disclosed a document on its official website on May 3, 2022, the day before the event date, stating that the company has applied to the Hong Kong Stock Exchange for the proposed conversion. After the application takes effect, Bilibili will be listed on the Hong Kong Stock Exchange and the US NASDAQ. The dual listing would have made it possible for the shares to be more liquid and for more international visibility, both of which would have been advantageous for the company's growth strategy. However it is not necessarily favorable for US investors. The dual listing will force the corporation to concentrate half of its attention on Hong Kong, and the company has the risk of exiting the US market. Therefore, it may lead to an increase in the turnover rate of stocks. As observed in the graph, the abnormal return peaked at 4.831% two days after the event day from a low of -3.904% just one day before the event day. The abnormal return is declining from -2 to -1 days following the event day. The data indicate that Event I had a non-trivial effect on the share price of BILI. Because market panic was growing and investor trust in the company was declining, the abnormal return on the second day of the event day was much higher than that on the first day of the event day.

4. Conclusion

For the return of capital to China and the long-term development of Chinese businesses, the research of risk response strategies for pre-delisting events is crucial. This article, which uses the degree to which pre-delisting events have an impact on Bilibili's share price as a case study, makes the following suggestions based on the prior literature from the perspectives of the nation, the regulatory agency, and the company:

(1) Actively collaborate with the US to create an auditing system that is compatible with both nations' regulatory frameworks. Concentrate on preventing the politicization of trade, which causes ethical enterprises to fall victim to politics, and on preserving the future growth of Chinese businesses. To regulate cross-border audits, the PCAOB has inked cooperation agreements with many nations and regions. China can refer to the way the United States cooperates with other countries and regions, focus on negotiating regulatory methods for sensitive information, and steadfastly opposes the outflow of sensitive data.

(2) Improve China's stock market system. The imperfect capital system and the high bar for domestic listing are significant causes of capital flight from China. To prepare for the return of Chinese companies to A shares and Hong Kong shares, China should therefore intensify efforts to improve the stock market system. Regulators control the regulatory scale, appropriately reduce the threshold of listing and increase the circulation of China's stock market shares, but also increase supervision after listing, to prevent financial fraud and inadequate information disclosure.

(3) Businesses decide on the development path in the stock market based on their requirements. Companies with severely depressed share prices that need to lower transaction costs and free cash flow depletion can opt to privatize and delist. When necessary, privatization and delisting should be done quickly because, in some cases, they are more in accordance with the company's essential objectives than listing and funding. Businesses that have enough cash flow but still want funding can decide to revert to a dual listing on A-shares or Hong Kong shares, which can boost the company's visibility and stock liquidity.

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