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Cross-listing of Indian Companies' Shares in Developed Markets: Motives & Theories

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Abstract: *Integration of the financial markets and technology advancements in equities trading may provide corporations the chance to profit from listing their shares on a foreign exchange. Every year, a sizable number of companies continue to cross-list. In this article, reasons for cross-listing shares of developing market companies on developed stock exchanges are examined, and the literature on these motivations and theories is reviewed. Market segmentation, liquidity, investor recognition, information disclosure, legal bonding, proximity preference, and business strategy theories are among the theoretical studies summarized in the literature review. The review also discusses the testable implications and empirical support for each of the cross-listing theories mentioned above. These theories often complement one another by addressing various aspects of the complicated cross-listing behavior. However, ongoing market changes, such as substantial legislative and technical adjustments to the way capital markets function, present fresh concerns about why corporations cross-list and necessitate more study.*

Key Words: *Cross listing, ADR, GDR.*

1. INTRODUCTION:

Over the past few decades, the Indian economy has seen significant change. The economy has changed from being tightly controlled with total government interference to being liberalized. Before the early 1990s, administered interest rates, quantitative ceilings, captive markets for government securities, excessive dependence on central bank funding, fixed exchange rates, and current and capital account restrictions characterized the Indian financial markets. But after 1991, the economy began to taste three letters: LPG, which in fact sparked the opening of the Indian economy. Since July 1991, India's economic reforms have boosted stability, sped up development, and strengthened the economy. The money market, the market for government securities, and the foreign currency market have all seen a dramatic shift over the period.

The listing of a company's shares on more than one stock market is known as a cross listing, or "secondary listing." A corporation often begins with an initial or primary listing on one exchange before moving on to list in another country or in many other countries. By going public in another country, the firm can access financing that it would not normally be able to in its own country.

A dual listed structure is a set of agreements between two listed entities that allow them to function as one economic entity while maintaining their individual legal identities. The shareholders gain from the combined profits of the firms even if the shares of one company are not convertible into the other.

Companies established in India can only use the American Depository Receipts (**"ADR"**) and Global Depository Receipts (**"GDR"**) systems in order to access the equity capital markets of other jurisdictions. More businesses have cross-listed their shares on the main international stock markets during the past 20 years, particularly those from developing market nations. What does a cross listing mean? The act of listing a company's common shares on an exchange other than its primary and original stock exchange is known as cross-listing. Businesses all around the globe are seeking for new strategies to expand and strengthen their competitive advantage as the global economy grows increasingly intertwined. Companies may improve their competitiveness in a variety of ways. Raising capital on a foreign stock exchange is one option for a firm to expand.

For instance, an Indian listed firm may trade its shares on markets in the United Kingdom, the United States, and many other countries to generate money. I paid particular attention to the situation in India in order to comprehend the effects of cross-listing.

Since the Indian stock market resumed in 1990, cross-listing of Indian firms has increased and turned into a source of foreign capital inflows through overseas stock exchanges. Indian economic investment started with the experience of cross-border listing of Indian firms in 1980, in addition to foreign direct replenishment.

The study of Indian firms' cross-border listing is evolving into a new area of academic inquiry as more and more Indian companies list on the global stock market. According to the beneficial effect hypothesis, some studies have looked into the positive effects of cross-listed Indian companies; however, it is unclear whether cross-listing is advantageous for developing markets and whether investment strategies can be derived from the positive effect phenomenon between dual-listed shares. Indian businesses have prospered during the past 20 years. India is the biggest democracy in the world and one of the fastest-growing developing economies. Even though India has a sizable economy and population, there are very few sponsored ADRs listed on U.S. exchanges.

Here is the list of Indian ADR trading in US Markets

Company	Market	Industry
Azure Power Global Limited	NASDAQ	Utility
Dr. Reddy's Laboratories	NYSE	Pharma. & Biotech.
Eros Media World PLC	NYSE	Entertainment
HDFC Bank	NYSE	Banks
ICICI Bank	NYSE	Banks
Infosys	NYSE	Software & Computer Svc
Mahanagar Telephone Nigam	OTC	Fixed Line Telecom.
MakeMyTrip Limited	NASDAQ	Travel & Leisure
SIFY Technologies	NASDAQ	Software &Computer Svc
Tata Motors	NYSE	Industrial Engineer.
Wipro	NYSE	Software &Computer Svc
WNS Holdings	NYSE	Support Services
Yatra Online, Inc.	NASDAQ	Travel & Leisure

2. LITERATURE REVIEW:

Three primary concerns are emphasized in the literature on international cross-listings. First, a number of studies have looked at the excess returns, liquidity, and risk implications of a cross-border stock listing. In their investigation of Canadian stocks that list in the US, Foerster and Karolyi (1993) discovered a positive pre-listing abnormal return but a negative 100-day post-listing abnormal return. In general, the equities' liquidity rises as their betas fall. In addition, liquidity is found to rise for a sample of UK stocks that cross-list at the NYSE by Werner and Kleidon (1996). The authors discover no connection between stock risk and anything. The risk and cost of capital of 94 dual-listed Canadian stocks in the US are compared to a benchmark sample of 655 non-US-listed Canadian stocks by Jorion and Schwartz (1986). They discover that compared to benchmark firms, cross-listed companies have a lower cost of capital but a higher susceptibility to market risk in the US. More recently, Doukas and Switzer (2000) discover a noticeably favourable stock market response to the news of 79 Canadian companies listing in the USA between 1977 and 1997. This is in line with the theory that businesses operating in lightly segmented markets see a decline in their risk premium as a result of international listings. Karolyi (1998) draws this conclusion after reviewing a large number of research on cross-listings: the data points to a favourable short-term stock price reaction to the listing, an improvement in liquidity, and a noticeably lower cost of equity capital. The data on longer-term stock price performance after listing is contradictory.

Second, both the features of corporations that cross-list their stock at a foreign exchange and the reasons for doing so have been well researched. According to Saudagaran (1988), who looked at a sample of 223 companies that obtained dual listings in Canada, Europe, Japan, or the US, major businesses with a significant proportion of sales abroad are more likely to list overseas. Similar findings were made by Pagano et al. (2002), who discovered that firms that list overseas are typically rather large and spend a lot on R&D. Firms are comparatively unlikely to list at foreign exchanges with tougher disclosure laws than the domestic market, according to Biddle and Saudagaran's (1989) analysis. After reviewing current data, Karolyi (1998) draws the conclusion that the biggest barrier to international listings is the strict

disclosure requirements. On the other side, Fuerst (1998) contends that businesses may utilize a cross-listing at a market with stringent guidelines for signaling quality.

3. WHY CROSS LISTING?

- Dual listing is an easy option as it can help avoid capital gains tax and other complex tax issues while offering the benefits of scale and merger synergies without the need for a disposal or transfer of shares.
- Another advantage from the company's perspective is an increased profile and global presence, which can be valuable when expanding brands or operations into other markets or overseas.
- From the standpoint of the shareholders, a secondary listing may provide investment diversification, higher share liquidity, and possibly decreased investment risk due to the shares' exposure to two or more markets rather than just one.
- The market heavily relies on investor sentiment, therefore having a domestic firm listed on the NYSE or NASDAQ would increase the organization's prominence and demand a higher valuation for domestic businesses.
- Local businesses will have access to foreign money that may be utilized to finance international projects.

4. MOTIVES & THEORIES TO CROSS-LIST:

- **Traditional motives to cross-list**
  Early ideas of cross-listing emphasized the use of cross-listing to reduce market fragmentation and increase stock liquidity. In ideal markets, businesses would not care about the choice of where to list their market shares. In actuality, stock market value and liquidity in the segmented market may not be ideal when a national financial market is divided from international financial markets owing to investment obstacles.

- **Market segmentation theory**
  Cross-listing phenomena was initially discussed by Stapleton and Subrahmanyam in 1977. They contend that through cross-listing in a foreign market, a company based in a segmented market can get around segmentation constraints and, consequently, inefficiencies in asset pricing. Regulatory investment limits and taxes are only two examples of the market flaws that can lead to market segmentation. In the face of investment obstacles, a number of theoretical models predict equilibrium capital market prices. Taxes on foreign investors' asset holdings have been suggested as a potential explanation for both the underperformance of asset prices relative to expectations and the investor preference for local equities by Black (1974) and Stulz (1981).

- **Liquidity theory**
  One of the drawbacks of a market isolated from international financial markets that may be improved by cross-listing is poor stock market liquidity. Corporate management frequently claim increased stock liquidity as one of the primary reasons for cross-listing (Houston and Jones, 2002; Bancel and Mittoo, 2001, 2009). Cross-listing extends trading hours and boosts the number of investors who have a financial stake in the stock, which encourages trading competitiveness.
- **Information-based motives to cross-list**
  The traditional presumption of asset pricing is that markets are efficient, which means that all investors have free and quick access to information. In actuality, insufficient information causes considerable market friction that has an impact on business listing decisions, including cross-listing decisions, and financial market activity. Cross-listing can first eliminate information asymmetry and enhance the informational climate for stocks. Cross-listing is thought to raise investor awareness of the company among overseas investors, lower information costs for investors, and enhance investor protection, according to the investor recognition, information disclosure, and legal bonding theories. Furthermore, cross-listing patterns may reveal information flows. Particularly, proximity preference and business strategy theories contend that a firm's cross-listing conduct reflects both its worldwide corporate strategy and the familiarity preferences of investors.

- **Investor recognition theory**
  The condition of equal information availability is relaxed in Merton's (1987) model of capital market equilibrium, which also implies that investors are only aware of a portion of the securities. Expected profits in this situation are

influenced by both the costs of insufficient knowledge and market risk. Firm-specific risk is not valued under the Sharpe-Lintner capital asset pricing model since diversification can reduce it.

- **Information disclosure theory**
  In addition to the current disclosure in the home market, cross-listing is typically connected with complying with the obligatory disclosure requirements of the foreign host exchange. In turn, this increases information dissemination and lessens information asymmetry between company management and investors as well as between various investor groups. As a result, the firm's cost of capital is reduced due to the decrease in investor information expenses.

- **Legal bonding theory**
  The debate over whether the advantages of cross-listing result from the new legal framework that offers stronger investor protection was started by Stulz (1999) and Coffee (1999, 2002). In order to "bond" the company to better corporate governance practices, which restrict the ability of managers and controlling shareholders to take excessive private benefits, it is possible to cross-list on an exchange with stricter legal and disclosure requirements compared to those of the home market.

- **Proximity preference theory**
  According to the cross-listing theories stated above, businesses gain by cross-listing in foreign markets that differ from their home markets in terms of liquidity, investor base size, quality of information environment, and investor protection. However, these justifications don't seem to be able to account for the distribution of cross-listings that show a clear spatial grouping. Examples of cross-listing companies include those from Canada, Latin America, the UK, Ireland, and New Zealand in the USA.

5. CONCLUSION:

Over time, increased global integration has clearly lowered investment barriers, yet businesses still choose to cross-list in other countries. Different firms have various incentives, and it's possible that there are still others that haven't been covered in the literature. The geographic, political, and cultural divides between nations cannot be crossed by market integration. Given that nations will always have boundaries, it can only offer simple access to international markets.

The global equity trading environment has altered dramatically as a result of significant technological advancements, which have led to the transition of securities trading from the traditional trading floor to electronic trading. This has boosted accessibility to overseas markets for equities trading, promoted competition in the stock exchange sector, and permitted the introduction of new market and trading platform types.

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