

The Impact of Different Financial Variables on the Privatization of the Kuwaiti Stock Market

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Abstract

The main goal of this research is to examine if there have been any notable changes in the trading actives of the Kuwait stock Exchange (KSE) after the privatization process that took place on the 25th of April 2016. The data that are used to test if there is any change in the Kuwait financial market performance are the daily indices for the period from the 15th of June 2014 till 21 of April 2016 (before privatization) and a similar period after the date of the privatization from the 24 of April 2016 till the 29 May 2019. The research outcomes indicate a lower variability of most of the variables that are associated with the privatization. However, that the observed switch in slope direction is not actually a product of privatization, but rather one of serial correlation. In addition, there is no evidence to show that privatization has, as of yet, affected the average closing price of assets listed on the Kuwait Stock Exchange.

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I. INTRODUCTION

Stock exchanges are currently facing a complicated and a competitive environment in the different markets. Some of the key forces behind these changes and developments are the ever growing use of more sophisticated technology and the evolution of financial regulations. In light of these changes to the market and environment and in order to strengthen their competitive powers, stock exchanges are moving towards the privatization.

Kuwait Stock Exchange (KSE) was founded in 1983 to organize and regulate public trading activities. Over its years of operation, KSE have witnessed various changes and improvements through introducing different investment tools such as the introduction of forward, futures and options markets. In addition, Kuwait Stock Exchange worked on facilitating the process of trading through

introducing and implementing an electronic trading system which then extended to include an online trading platform. In year 2010 the Kuwait Stock Market moved to be under the Capital Markets Authority (CMA) which took over the regulatory responsibilities.

Commencing from April 25th 2016, the KSE started to be operated by Boursa Kuwait Securities Company (BKSC). BKSC was established by the CMA commissioner's council in 2014 mainly to run KSE operations efficiently and effectively in line with international standards.

The market capitalization (MCAP) of KSE is around KD 26.6 billion as of May 2019 distributed over 16 sectors. The banking sector alone represents nearly half the MCAP of the market with around KD 14 billion for the same mentioned period. Telecommunication comes next with around KD 2.4

billion which is equivalent to around 9% of the total MCAP (May 2019).

This research is based on the index figures of the market daily operations for two periods. The first period is before the privatization date from the 15th of June 2014 till 21 of April 2016. The second period starts from the first date of privatization which is the from the 24 of April 2016 till the 29 May 2019.

The research main source of data and information are the Kuwait Stock Exchange, Boursa Kuwait Securities Company, and Zawya research reports.

II. LITERATURE REVIEW

During 1960's, Germany privatized its stock exchange and was one of the first to carry out this transformation (Esser, 1994). The promotion of the participation of investors and national exchanges renewal was a top priority of the privatization programs in many countries such as UK, Spain, Italy and France (Vickers and Yarrow, 1988; Dumez and Jeunemaitre, 1994; Chiri and Panetta, 1994).

As per Boutchkova and Megginson (2000), a significant increase in wealth is shown to be correlated with privatization and the financial market development. For example, in developed countries outside the US, the stock trading volume grew from USD 460 billion in 1983 to around USD 17 trillion in 1998.

Pagano, 1989; Subrahmanyam and Titman, 1999, suggest that privatization contributes to stock markets via improving diversification opportunities for investors. Academic and otherwise, a multitude of literature has examined effects of privatization. In particular, Megginson and Netter, 2001; Bortolotti et al., (2002) offer several papers that have documented major changes and developments in the financial performance of privatized institutions.

Privatization involving the floating of shares in both domestic and international exchanges is said to reduce informational barriers to foreign investment,

thereby boosting liquidity in the domestic market (Hargis and Ramanlal, 1998; Chiesa and Nicodano, 2003). Ryden, 1997; mentioned that since the privatization of the Stockholm Stock Exchange took place as of January 1993, the market witnessed a substantial growth in market values and trading volume.

The Organization for Economic Co-operation and Development report that “the privatization of exchanges globally was done through either a strategic sale or a self-listing (The Organization for Economic Co-operation and Development “OECD” 2014). The ownership of an exchange by the companies listed on it is extremely rare and in the MENA region, only the Palestinian stock exchange is predominantly owned by one of the largest companies listed on it. This is due to some circumstances particularly related to the Palestinian economy, the fact that the exchange was never owned by the government.

A research paper prepared by Atyeh, et. al. (2017) examined the performance of the Kuwait Stock Market (KSE) after privatization. The results indicate that privatization is associated with lower variability for the majority of variables, but that the observed switch in slope direction is not actually a result of privatization, but rather one of serial correlation. In addition, there is no indication to show that privatization has, as of yet, affected the average closing price of assets listed on the Kuwait Stock Exchange.

Despite the importance of these issues, there is no enough empirical research focuses on the impact of privatization on the development of the financial markets and especially in the Arab world in general and Kuwait in particular.

III. METHODOLOGY

The statistical tools used in this analysis are standard variance ratio tests (f-tests), and t-tests for comparing the various means between the three time segments. In addition a semi-log OLS regression is

ran on each of the four variables (Closing price, number of shares traded, value of deals and the number of deals, in which the independent variable is time.

IV. RESULTS AND DISCUSSION

The outputs below relate to a three-way comparison of four variables, in two time periods: one is before

the privatization of the KSE, while the other period is after the privatization. Table 1 compares the descriptive statistics, while table 2 compares the slope betas from several simple OLS regression in which time is the x variable.

Table 1: Mean and Variance Comparison

	Before		After	
	Mean	SD	Mean	SD
Closing Price	6281	715.61*	6241	621.98
No. of shares traded	174541847*	76146396*	152079666	160305148
Value of Deals	17182099	7914073*	17303915	13860619.85
No. of Deals	4038	1703	3823	2477.58

* Significantly different from the ‘after’ (post-privatization) period (minimum of 95% confidence)

There is a significant difference between the majority of variables, but this in itself is not particularly insightful. What is more telling is when the post-privatization period appears to universally distinguish itself from the other period, and as such, this is the point we focus this discussion on. The different mean returns in regards the closing price appears largely insipid, but the reduction in variance is noteworthy. Indeed, except for the ‘number of

deals’ variable, variance is lower for all variables in the after period. Analytically speaking, the near universal reduction in variance is probably indirectly responsible for many of the other observed differences. Focusing on the two remaining means, the ‘number of shares’ traded appears to be markedly lower in the after period. A similar observation stands in regards the ‘value of deals’ variable.

Table 2: OLS Slope Coefficient

$$\log(y) = \hat{\beta}_0 + \hat{\beta}_1 t$$

Y	Before	After
	<i>Beta-1</i>	<i>Beta-1</i>
Closing Price	-0.0008	0.00012
No. of shares traded	0.007	-0.0100
Value of Deals	0.0021	-0.0072
No. of Deals	0.0039	-0.007

Being a semi log model, the coefficients have a percentage based interpretation. For what it’s worth, with the exception of ‘closing price’ which is

weakly significant in the parallel set, all other relationships are highly significant. However, as there are no independent variables outside of time

itself, it's not so much a matter of significance per se, but rather one of analysing comparative trends and spotting pattern anomalies. And so that is what we focus our attention on. At first glance, the most compelling story told by the models is the near universal 'turn of sign' post-privatisation. The one exception is 'closing price'. And indeed, in terms of what one would expect from an OLS regression, closing price is the least well behaved out of all our variables, and accordingly, the one from which we can draw least in the way of a conclusion. Closing price to one side for now, this general reversal enables us to see that, if one were inspecting the first six months of privatization, these data alone would be highly misleading, as one may be tempted to conclude that privatization is associated with a dramatic reversal of trends. The parallel data period on the other hand serves as a control to favor the suggestion that what we are observing is more likely to be serial correlation ($\text{cov}(u_t, u_{tj}) \neq 0$) across time segments. In which case, the more legitimate comparison to focus on is between that of the parallel and the post-privatization periods. Therefore, based on confidence interval analysis, the other most notable observation emerges is that, all slopes are significantly different post-privatization. There appears to be an accelerated decline in regards the number of 'shares traded', and the actual 'value of deals'. Previously, a one-unit change in time was associated with a decline of 0.0025 percent, post-privatization it moved four-fold to 0.02 percent. The 'value of deals' trend shifted by a similar magnitude from, negative 0.02 to negative 0.07 percent. However, the 'number of deals' variable poses a different pattern. It undergoes moderation.

V. SUMMARY AND AVENUES FOR FUTURE RESEARCH

The firmest conclusion relates to characteristic variance. With the exception of the 'number of deals' variable, the evidence suggests that privatization is associated with lower variability. It's hard to rationalise why this may be. Actually, it's a

touch counterintuitive, as one would expect the withdrawal of public administration (and its implicit moral hazard inspired safety net) to perhaps be associated with more volatility not less. Indeed, that reasoning would still punctuate our long run expectation, and in turn, constitutes an avenue for future research.

For the time being, as we have taken the 'immediate period', and we attribute the tighter variance to indicative of investors having possibly adopted a 'test the water' sort of mentality towards the newly privatized KSE. The second most conclusive finding relates to what appears to be a dramatic reversal of trends in relation to all but one of the chosen variables. Viewed as just the immediate aftermath, the number of shares traded value of deals and the number of deals all switch to negative slopes after privatization, evidence does, however, suggest that this is a misleading turn; it is not a post-privatisation switch, but rather the segment of a wider pattern of serial correlation. And while it is noteworthy that the paralleled relationships display significantly different gradients, that in itself is ultimately a limited finding. One could consider an area for research to be to assess whether that is a transitory or persistent change. As is to be expected from an orthodox assessment of equity markets, closing price is a particularly slippery variable to deal with, and other than a significant fall variability, there is no evidence to show that privatisation has, as of yet, affected the average closing price of assets listed on the Kuwait Stock Exchange.

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