

How Persistent Is The Impact of Market Timing on Capital Structure?

Abstract

This paper examines the capital structure implications of market timing. I isolate timing attempts in a single major financing event, the initial public offering, by identifying market timers as firms that go public in a hot issue market. I find that hot-market IPO firms issue substantially more equity than cold-market firms. The difference represents a genuine timing effect, as it cannot be explained by firm-level characteristics. Market timing depresses the leverage ratio substantially in the very short-run. However, the timing effect on leverage quickly reverses. Immediately after going public, hot-market firms start increasing their leverage ratios by issuing more debt and less equity relative to cold-market firms. This active reversal policy is strongly visible for two years. At the end of the second year following the IPO, the market timing impact on leverage completely vanishes. The results contrast with recent findings that suggest high persistence of market timing effects on capital structure.