

White Collar Crime and Stock Return: Empirical Study from Announcement Effect

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Abstract: Despite, the move by the government on integrity pledge, a white-collar crime continues to prevail across corporations and organizations in Malaysia. Globally, such a crime remains a serious issue which has undermined the performance of organizations. A share price event study was conducted on a group of public listed companies in Malaysia to examine the announcement effect of white-collar crime on stock return. Stretching from 1996-2010, the study covers both the Asian financial crisis in 1997/98 and the sub-prime mortgage crisis in 2008/09. The results indicate the existence of significant negative abnormal share price reaction on 10 trading days subsequent to the day of announcement. This suggests that the stock market in Malaysia is inefficient. It also implies that the market possesses the power to discipline unethical behavior amongst companies when shareholders drive down the stocks' value by disposing their stocks following the announcement.

Key words: Share price, event study, white-collar crime, unethical behavior, Malaysia

INTRODUCTION

The collapse of large-established organizations globally has motivated researchers to investigate the relationship between corporate governance and share prices. In fact, the string of corporate scandals occurred since the Asian financial crisis in 1997/1998 was due largely to weak corporate governance practices. A closer examination of some of the corporate governance cases reveals that it was a form of corporate crime.

Corporate crime also refers to "white-collar crime" and the term has been defined differently by criminologists at different times. White-collar crime was first popularized in 1939 by Sutherland (1949), who was both a criminologist and a socialist. Edwin argued that a crime is normally committed by a person of respectability and high social status in the course of a person's employment. On the other hand, Edelhertz (1970) another criminologist suggested that a white-collar crime is "an illegal act or series of illegal acts committed by non-physical means and by concealment or guile, to obtain money or property, to avoid the payment or loss of money or property or to obtain business or personal advantage". Given Edelhertz's wider definition of the term, it was used interchangeably with other terms such as "economic crime", "corporate crime", "business crime", "financial crime" and/or "commercial crime". In short, crimes committed against business organization are nothing new (Bressler, 2009) but the cost of crime is

significant and costly. For instance, several high-profile cases of fraud include the Madoff investment scandal (US\$50 billion) and the Stanford investment scandal (US\$20 billion) while Enron and Worldcom financial scandals remain one of the greatest scandals ever recorded in the history of corporate crime.

According to the Global Financial Integrity (GFI), illicit financial flows for the years 2000-2008 from developing countries record an average of US\$1.26 trillion outflow annually. The main sources of the illicit money are due to irregularity practices such as corruption, kickbacks, tax evasion and theft of cash. Notably, Malaysia is ranked fifth among all developing countries in the world in terms of the largest cumulative illicit outflows during 2000-2008, recording a total of US\$291 billion. In fact, among the developing countries in Asia, Malaysia is ranked second after China (US\$2.18 trillion).

As a result of corporate crime, companies like Sime Darby Berhad, Alliance Financial Group Berhad and Kenmark Industrial Co. (M) Berhad have experienced a nose dive in their share prices following the announcement of suspected fraud and abuse of authority. Kenmark, in particular has wiped out of some Ringgit Malaysia (RM) 100 million in market value over merely a week's time. In the case of Sime Darby, the company recorded a loss of RM2 billion in its energy and utilities division in the financial year ended June 30, 2010. Subsequently, the effect of the press announcement of white-collar crime requires serious attention due to the