Can Liquidity Shifts Explain the Lockup Expiration Effect in Stock Returns?

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Abstract

Several studies on the expiration of IPO lockups document a strong negative reaction even though the unlock event is devoid of any informational content. The empirical finding has remained a conundrum. In this paper, we find that changes in liquidity can account for the observed stock price reaction around lockup expiration. Specifically, firms which show improvement in liquidity subsequent to the unlock day experience positive abnormal returns in the post-expiration period, and vice versa. Another interesting finding is that liquidity changes strongly predict long-term abnormal returns as well as accounting performance in the post-lockup period. Our results remain robust to the use of alternate procedures to characterize changes in liquidity.

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