WESTERN HEMISPHERE DEPARTMENT

# Equity Financing and Exports: Evidence from IPO Approvals in China?

*by Robin Kaiji Gong, Yao Amber Li, Stephen Teng Sun, Shang-Jin Wei*

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Discussant: JaeBin Ahn (IMF)

# A Quick Summary of the Paper

- Investigate the role of finance in international trade
  - Focus on equity financing, as opposed to debt financing, by exploring IPOs in China
- Combines a novel methodological approach with a unique dataset
  - Exploiting the approval-based IPO system in China
  - IPO Examination Database (WIND-IPO) covering the universe of all IPO applications in China with hard and soft information
  - Including rejection cases with reasons for rejections, etc.

➔ After IPO, exports increase by ~ 40% in the subsequent 6 years, mainly via extensive margins, by promoting intangible investments and risk-taking

# Highly Relevant, with a Novel Approach

- An Important role of finance in international trade: The case of the economic impact of tariffs
  - Growth impact of declining imports; potential inflationary effects…
  - First line of defense: financing tariffs!
    - Only importers with stronger balance sheets can continue importing by paying for tariffs and limit the pass-through to consumers
    - Exporters with stronger balance sheets can help absorb and share the burden of tariffs
- A novel approach with a unique dataset overcomes typical identification challenges
  - Selecting ‘correct’ control groups: Near-misses
  - Further refined with information on reasons for rejections

# Comment 1: Caveats on Data

*What's left in variation across successful and unsuccessful IPO firms?*

- Threat: IPO rejections are correlated with unobserved firm characteristics
  - Productivity, technological advances, foreign market access, etc.
- Solution: exclude rejections citing revenue/profitability-related clauses

Clause 37(Main)/14(GEM)

- Factors that potentially affect future revenue/profitability
- Inferred based on financial statements in most cases
- May directly affect export performance (if rightly assessed)

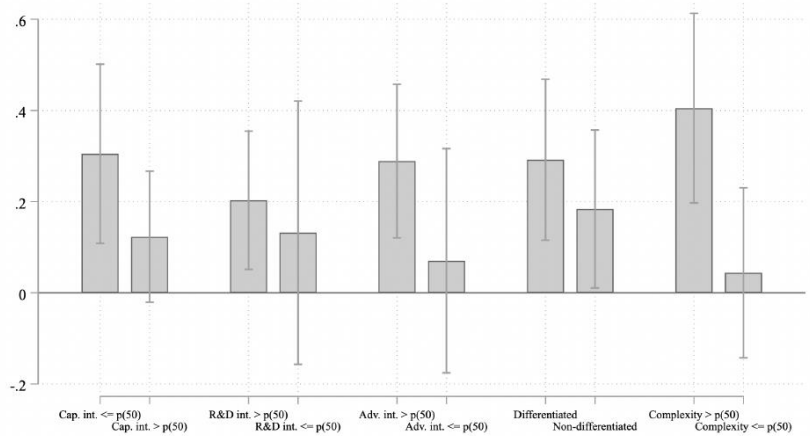
Other Clauses

- Commonly cited: independence, internal control, feasibility
- Subjective assessment and limited monitoring capacity
- Mainly domestic and not directly related to fundamentals

- Can political connections be hidden in 'Other Clauses'?
  - For example, the CCP membership status of the CEO or investors may facilitate access to debt financing, subsidies, and other benefits.

*Limited variation for firm heterogeneity analysis?*

Market expansion by product market characteristics




- Most of the firm-heterogeneity analyses show overlapping confidence intervals
  - Possibly reflecting side effects from an overly idealized empirical design

# Comment 2: Opening a Pandora's Box?

## Potential Channels: Summary of Empirical Evidence

1. IPOs are more than simply capital raising for exporters
   - Little effects on liquidity-constrained firms or capital intensive activities
2. IPOs provide *risk capital* for intangible investments and risk-taking activities
   - More pronounced market expansions in R&D and advertising intensive industries and markets with more differentiated and complex products
   - More pronounced market expansions in more volatile and less familiar markets
   - Positive effects on selling expenses and patenting per worker
3. Possibly non-financing channels
   - Information/reputational frictions: stronger effects on less experienced exporters
   - Corporate governance: positive effects on management expenses
   - Leave for future studies

- The evidence for potential channels is less convincing than the main finding (heterogeneity analyses)
- If all the findings are taken at face value, this should be a paper on IPOs and Innovation (or intangible investments)
  - Exporting is simply a byproduct
- The innovation / intangible investments literature may warrant a more in-depth examination
  - Any possibility that IPO firms used cash to buy patents? (e.g., Wei et al., 2023)

# Suggestion: Exploring the Trade Finance Aspect

- IPO exporters can use the raised cash to
  - Offer favorable financing terms to *existing* foreign importers
  - Extend trade credits to *new* foreign importers (e.g., unknown, riskier)

- Most IPO exporters are also likely to be importers
  - IPO improves a firm's creditworthiness as an importer, facilitating their imports
    - Foreign exporters are more willing to offer favorable financing terms (e.g., trade credits)
    - For example, export credit agencies provide support to exporters when importers are publicly listed or have credit ratings, etc.
  - New contacts through importing leads to new customers for exporting
    - This should be more pronounced in frontier markets (consistent with extensive margins findings)