Why European Firms issue Convertible Debt?

Franck Bancel
(ESCP-EAP)
Email: bancel@escp-eap.net

Usha R. Mittoo
(University of Manitoba, Canada)
Email: umittoo@ms.umanitoba.ca.

ABSTRACT

Why convertible bonds are such a popular financing vehicle has been a puzzling phenomenon for financial researchers. In this paper, we examine the characteristics of convertible bonds listed on the European exchanges as well as survey managers of the issuer firms to gain some insights into this issue. Our preliminary analysis shows some interesting findings. Our evidence suggests that while a majority of firms issue convertibles as a "delayed equity", they also value convertibles for their ability to provide a signal about the future prospects of the firm. Most managers perceive that convertible bond is cheaper than straight debt and value the delayed impact of convertibles on earnings per share dilution relative to the equity alternative. Most managers report that issuing convertibles has significantly positive net benefits compared to the debt or equity alternatives. Overall, our evidence is consistent with theoretical models in asymmetric information framework such as Stein (1992), Mayers (1998), and Brennan and Kravs (1987).