

## FIN 423 M&A Strategy

### Successful & unsuccessful mergers & tender offers

- Sharks
- White Knights
- winners
- losers

### Dodd (JFE, 1980): Successful & Unsuccessful Mergers

151 targets, 126 bidders

NYSE, 1970-77

Announcement effects (2-day):

	<u>Bidders</u>	<u>Targets</u>
Successful	-1.09%	13.41%
N,t-stat	(60,-3.0)	(71,23.8)
Unsuccessful	-1.24%	12.73%
N,t-stat	(66,-2.6)	(80,19.1)

## Dodd (JFE, 1980): Successful & Unsuccessful Mergers

Total abnormal returns, 10 days before  
offer announcement through 10 days after  
outcome:

	<u>Bidders</u>	<u>Targets</u>
<b>Successful</b>	-7.22%	33.96%
N,t-stat	(60,-2.5)	(71,7.7)
<b>Unsuccessful</b>	-5.50%	3.68%
N,t-stat	(66,-2.1)	(80,1.0)

## Analysis of Bidder Returns

### (1) Bidders pay too much?

- Roll's "hubris" hypothesis
  - egos of CEOs get involved and they pursue NPV<0 takeovers just to show they can win

### (2) Mergers are more often financed with equity -- Is this a reaction to the financing decision?

- cross-sectional studies trying to explain merger premiums typically focus on target firm returns

## Analysis of Bidder Returns

**(3) Is the decision to merge a signal about the quality of internal investment opportunities?**

- **reaction to Kodak-Sterling announcement (2-day effect = -12.5% for Kodak, +10% for Sterling) was too big to be explained by a wealth transfer from Kodak to Sterling**
  - **loss to Kodak = \$2 billion**
  - **gain to Sterling = \$500 million**
- **did the market interpret this as adverse information about Kodak's other business lines?**

## Analysis of Bidder Returns

**(4) Dodd's evidence says that successful bidders lose about 7%, but unsuccessful bidders lose about 5.5%**

- **warning: Asquith(JFE, 1983) doesn't find losses for successful bidders, but finds similar losses for unsuccessful bidders**
- **it seems that there are substantial costs of not succeeding in a merger if you are the bidder**
  - **reflects on competence of management?**

## Who Cancels Unsuccessful Mergers?

(5) Dodd segments his sample of unsuccessful mergers by what the WSJ says were the reasons for cancellation

- bidders should cancel if, when they get access to inside info about the target, they learn negative things (NPV<0 deal)
- targets should cancel if, when they learn more about the terms of the deal, they learn it will not be a good deal for their shareholders
  - or management -- agency problem!

## Dodd (JFE, 1980, Table 8): Who Cancels Unsuccessful Mergers?

Announcement effects (2-day):

	<u>Bidders</u>	<u>Targets</u>
Target Cancels	0.86%	-5.57%
N	(19)	(26)
Bidder Cancels*	1.38%	-9.75%
N	(47)	(54)

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\*or it is uncertain who canceled

## Dodd (JFE, 1980, Table 8): Who Cancels Unsuccessful Mergers?

Total abnormal returns, 10 days before offer announcement through 10 days after outcome:

	<u>Bidders</u>	<u>Targets</u>
Target Cancels	-3.12%	10.95%
N	(19)	(26)
Bidder Cancels*	-6.47%	0.18%
N	(47)	(54)

\*or it is uncertain who canceled

## Dodd (JFE, 1980, Table 8): Who Cancels Unsuccessful Mergers?

Announcement effects line up with the identity of the cancelor

- i.e., the one who has second thoughts is rewarded, at the margin

The overall effect is best for both targets and bidders if the target pulls out

- better for bidders than if the bid is successful (-7%), or if the bidder pulls out (-6.5%)
- is it relatively good news that the bidder was apparently trying to strike a hard bargain?

## Bradley, Desai & Kim (JFE, 1988): Successful Tender Offers

236 successful tender offers  
NYSE or AMEX, 1963-84  
matched bidders & targets

Announcement effects (3-day, Tables 3&4):

	<u>Bidders</u>	<u>Targets</u>
Total Sample, 236	0.00%	21.6%
Single bidder, 163	0.65%	22.0%
Multiple bidders, 73	-1.45%	20.8%

## Bradley, Desai & Kim (JFE, 1988): Successful Tender Offers

Total wealth effects (5-days before first offer to  
5-days after last offer by winning bidder, Table  
2):

<u>Period</u>	<u>Bidders</u>	<u>Targets</u>	<u>Total*</u>
7/63-6/68	4.1%	18.9%	7.8%
7/68-12/80	1.3%	35.3%	7.1%
1/81-12/84	-2.9%	35.3%	8.0%
7/63-12/84	1.0%	31.8%	7.4%

\*pct change in combined value of target & bidder

## Bradley, Desai & Kim (JFE, 1988): Returns to White Knights

Total wealth effects to winning bidder (5-days before first offer to 5-days after last offer by winning bidder, Table 6):

<u>Period</u>	<u>Single Bidder</u>	<u>Multiple Bidders</u>	<u>Total</u>
7/63-6/68	4.6%*	1.6%	4.1%*
7/68-12/80	1.7%*	0.3%	1.3%
1/81-12/84	-1.1%	-5.1%*	-2.9%*
7/63-12/84	2.0%*	-1.3%	1.0%*

\* significant at .01 level

## Unsuccessful Tender Offers

Success of tender offer is much different

- target management has no veto power
  - must convince shareholders not to tender
- bidder management has a stronger commitment
  - hard, but not impossible, to cancel a tender offer before it expires
  - don't usually get access to inside info during hostile tender offer
  - would lose credibility with financing sources, investment bankers, arbitrageurs if frequently cancel deals

## Bradley, Desai & Kim (JFE, 1983): Unsuccessful Tender Offers

353 targets

- 241 successful, 112 unsuccessful
- 94 bidders who were unsuccessful

NYSE or AMEX stocks, 1983-80

Announcement effects (1 month) for  
initially unsuccessful offers (Table 3):

Total Sample, 112	35.6%
Subsequently taken over, 86	39.1%
Not subsequently taken over, 26	23.9%

## Bradley, Desai & Kim (JFE, 1983): Unsuccessful Tender Offers

Cumulative abnormal returns to target stock  
from month before announcement (-1) to  
month K (Table 4):

Event Period	<u>Total</u>	<u>Subsequently Taken Over</u>	<u>Not Taken Over</u>
-1,+1	40.2%	46.3%	20.2%
-1,+12	42.2%	56.9%	7.0%
-1,+24	40.9%	60.2%	1.9%
Cases	112	86	26

## **Bradley, Desai & Kim (JFE, 1983): Unsuccessful Tender Offers**

Cumulative abnormal returns to bidder stock from month before announcement (-20 days) to day K (Table 8):

<u>Event Period</u>	<u>Total</u>	Target Subsequently <u>Taken Over</u>	Target Not <u>Taken Over</u>
-20,+1	2.3%	1.9%	3.4%
-20,+140	-5.9%	-7.9%	0.7%
<b>Cases</b>	<b>94</b>	<b>67</b>	<b>27</b>

## **Successful & Unsuccessful Mergers & Tender Offers: Summary**

**(1) Market reacts negatively to bidder in mergers, not in tender offers**

- bidder defined as the company that is offering a premium for the other company's stock

**(2) At initial announcement of merger, it is hard to tell which deals will be successful**

- unsuccessful tender offers have lower announcement returns
- tender offers that are followed by other bids have higher announcement returns
- market can tell which are likely to succeed

## Successful & Unsuccessful Mergers & Tender Offers: Summary

(3) Targets that are not taken over within 5 years lose all of the tender offer premium

- bidders for those firms also lose value
  - reflects on competence of management?

(4) Multiple bidder auctions lead to higher target returns and negative bidder returns

- you don't want to be a "White Knight"
  - DuPont in Conoco takeover
  - Kodak in Sterling Drug takeover

