

Takeovers and Bidders' Return Determinants on Announcement Dates

Vander Cassyen Benoit
University of Mons

Brédart Xavier
University of Mons

Finet Alain
University of Mons

The goal of this article is to determine the impact of takeover announcements on bidders' return. Also, we analyze the influence of eleven independent variables on bidders' return on the day of the takeover announcement. These variables are sorted in four categories related to: the characteristics of the deal, the bidder's governance, the bidder itself and the market. Our results do not show any statistically significant abnormal rank on the announcement day (methodologically, the rank is used as a proxy of the return). However, we identify five variables as having a significant influence on bidders' stock value on the announcement date. These variables are the type of diversification, the hostility of the offer, the duality of the functions of CEO and chairman of the board of directors, the Return On Equity (ROE) and the bidder's debt to equity ratio.

INTRODUCTION

Financial theory traditionally considers the share price as the main target of takeover transactions since shareholders are after all the actual owners of the company. Martynova and Renneboog (2008) synthesized the conclusions of 65 studies related to the impact of takeover transactions on stock market value of both bidders and targets. According to these studies, made upon the five waves of takeovers that have occurred since the end of the 19th century, it appears that takeovers generally seem to create profitability, but the profits largely benefit the shareholders of the target company. On the other hand, the observed changes in value for the shareholders of the initiator company are not statistically significant and are close to zero. Sometimes slightly positive, sometimes slightly negative, these changes in value seem to vary according to the individual features of each operation and to the length of the period taken under consideration around the announcement date.

The goal of this article, based on a sample of 61 takeover operations announced between 2005 and 2007, is to contribute to the debate, first by highlighting the observed value variation for the bidders on the day of the takeover announcements. Second, we use a linear regression to understand the factors influencing bidders' stock return. In order to limit the influence of external factors, our study focuses on the date of the announcement. In our explanatory model, we use eleven independent variables sorted in four categories: those related to the deal characteristics, to the bidder's governance, to the other bidder's characteristics and to the market. The variables related to the deal, are the method of payment, the takeover premium, the diversification strategy, the possible hostile character of the bid and the relative size of the target company. The governance variables are the ratio of non executive directors and the possible concurrent holding of the functions of both CEO and chairman of the board of directors. The variables specific to the bidder are the ROE, the Debt/Shareholder equity ratio and the logarithm of the amount of assets to take into account the influence of the company's size. Finally the variable associated with the market is the yield of the market index on the takeover announcement date.

The second part of this article presents a review of the literature for each variable of our model and states working hypotheses for the sign of the relation between each variable and the purchaser's return. The third part of the paper concerns our sample and methodology. The fourth part displays the results of our event study and our model. In this section, we also confirm or disprove our working hypotheses. The fifth part reviews our main conclusions and the limits of this study.

THEORETICAL INTRODUCTION TO THE WORKING HYPOTHESES

Deal Characteristics

Method of payment

The studies led on the American market unanimously agree on the fact that cash offers are associated with higher returns for the bidders than offers realized with shares or than mixed (with both cash and shares) offers (Travlos, 1987; Fishman, 1989; Berkovitch and Narayanan, 1990; Peterson and Peterson, 1991; Loughran and Vijh, 1997; Linn and Switzer, 2001). The reason for this difference in profitability emphasized by Fishman is that bidders tend to use cash offers when they possess private information about the target showing that important returns can be achieved by merging companies. In this case, bidders tend to use a large part of cash in their offer in order to quickly complete the deal and to avoid any other predators to bid for the target company. However, studies led on the European market show that offers made with shares have a positive and sometimes significant effect on bidders' return. Arguments of more theoretical origin also go in the same direction. Indeed, agency and free cash flow theories suggest that the announcement of cash offers could be a signal that the bidding company has excess cash flow compared to its needs to finance internal projects and that the management could invest that money in value-destructive projects. In conclusion, because of the lack of consensus between empirical studies and theoretical arguments, we choose to test the following two hypotheses.

Hypothesis 1A: "Cash offers have a positive influence on bidders' stock return on the announcement date"

Hypothesis 1B: “Cash offers have a negative influence on bidders’ stock return on the announcement date”

In our study, we consider offers made with cash in opposition with mixed offers and those with an exchange of shares only.

The takeover premium

The takeover premium is defined as being the extras amount that purchasers will have to pay to the shareholders of the target company in order to convince them to sell their shares. According to Gaughan (2002), this amount is partly influenced by the assessments made by the seller of the return that will result from the merger. Since a takeover transaction is considered as a costly investment, a high premium should have a negative impact on the future profitability of the company. Also, Lang, Slutz and Walking (1989) assert that the premium is determined by agency factors which can be apprehended through Jensen’s free cash flow theory (1986). According to that theory, the managers having at their disposal free cash flows are more likely to carry out purchases enhancing their discretionary area and their entrenchment - at the expense of the company’s profitability. Moreover, Gondhalekar, Sant and Ferris (2003) found a negative relationship between the premium paid and the bidder’s return which suggests that the premium paid for the purchase of the target is an agency cost borne by the shareholders of the initiator company. In conclusion, we expect a negative relation between the amount of the premium (in percentages) and the profitability of the purchaser at the time of the announcement.

Hypothesis 2: “The takeover premium paid to the shareholders of the target company has a negative effect on the bidder’s stock return at the time of the announcement”

In this study, we calculate the takeover premium as the excess of the bid’s value in percentages compared with the latest closing value preceding the announce.

Nature of the diversification

This variable analyzes how the nature of the diversification (concentric vs. conglomeral) influences the profitability of the purchaser on the announcement date. According to Lubatkin (1983), concentric takeovers generate a higher profitability than conglomeral takeovers because of the complementarity of the companies’ activities which generates synergies in terms of production, financing, marketing or competences. At the opposite, conglomeral diversifications generally only allow financial synergies due to a higher indebtedness capacity, a more efficient internal capital market, and to imperfectly correlated cash flows. Besides, this type of diversification also implies costs linked to the information asymmetry between the different departments of the company and to the lack of knowledge of the activity sector of the target company. Finally, according to Morck, Shleifer and Vishny (1990) non-linked diversifications are more likely to be driven by personal motivations of the managers, at the expense of the shareholders. Indeed, non-linked diversifications actually imply a lower risk for the manager’s job (Amihud and Lev, 1981); they favor the manager’s entrenchment (Shleifer and Vishny, 1989) or augment the manager’s salary by increasing the size of the company (Kroll, Simmons and Wright, 1990). In conclusion, even though the theory seems unambiguous on the fact that linked acquisitions provide higher returns than non-linked ones, empirical studies did not

confirm this statement categorically. Nevertheless, we follow Flanagan's advice and state the hypothesis that stock market investors prefer linked acquisitions rather than non-linked ones.

Hypothesis 3: "Concentric acquisitions provide higher profitability than conglomeral acquisitions"

In our study, we use the SIC Codes classification (Standard Industry Classification) to define the concentric or conglomeral character of the diversification. We consider a diversification as concentric if the first two digits are similar for the main activity of the companies. The purpose of this step is to use an objective criterion and to avoid arbitrary judgment about the interpretation of the type of diversification. Moreover, for this variable, we do not consider target companies active in several sectors without a predominant role of one of them.

Hostile vs. friendly bids

Several empirical studies highlight the higher cost of hostile takeover bids for the initiator company. According to Franks, Harris and Titman (1991), Servaes (1991) and Goergen and Renneboog (2004), hostile bids lower bidding companies' value by three to five percent. This reduction in value could be due to market anticipation that the target will use defense mechanisms that will oblige the buyer to offer a higher premium. Thus, the potential resistance of the target company could cause a reduction in the gains of the initiator company (Yen 1987). At the opposite, friendly offers benefit from the cooperation of the target company's management, which will contribute to reduce the information asymmetry between the two firms. The managers of the initiator company can therefore more easily assess the potential synergies and determine feasible plans. Also, this kind of offer is less uncertain and should therefore be better considered by investors. However, unlike the previous studies, the recent works of Baghat (2005), conducted on a sample of 1018 takeovers that happened between 1962 and 2001, show a positive return associated with announcements of hostile bids and a negative return associated with announcements of friendly offers. The author explains these results by the fact that hostile offers are related with significant future cash flows and with strong managerial skills of the purchaser. Moreover, Baghat also considers hostile bids as punishments aimed at penalizing inefficient management. Because of the contradiction between these different studies, we test the following two hypotheses.

Hypothesis 4A: "There is a positive relation between hostile offers and bidders' stock return on the announcement date"

Hypothesis 4B: "There is a negative relation between hostile offers and bidders' stock return on the announcement date"

Purchaser's liquidity / Bid's value

To complete a takeover, the bidding company can use two major methods of payment: cash or the exchange of shares. In the case of payment with an exchange of shares, the importance of the purchaser's cash compared with the total amount of the bid will be limited. Nevertheless, this cash is necessary to finance the integration costs of the two companies. The purchaser's cash should be regarded as a warranty for a good integration and have a positive effect on the investors. If the purchaser whose cash capacities are lower than the amount of the bid chooses to

make a purchase with cash, he will be forced to use indebtedness or to launch an appeal for an increase in capital. In both cases, the transactions will be regarded as negative by the markets. On the one hand, an increase in the purchaser's indebtedness will increase its leverage, but it will also increase the financial pressure on the company and decrease its solvability. On the other hand, according to Myers and Majluf (1984), a capital increase will lead to a lower return for the purchaser because it sends the signal of an overestimation of his share. Therefore, we can conclude that the greater the amount of the company's cash with respect to the amount of the bid, the less the company will have to resort to indebtedness or to the capital market, and the more likely investors will react positively. However, according to numerous authors (Jensen and Meckling, 1976; Blanchard, Lopez de Silanes and Shleifer, 1994; Hartford, 1999; Bates, 2005; Richardson, 2006), the abundance of cash could influence managers to invest in unproductive projects damaging the company's profitability. In conclusion, because of the contradiction between the different arguments, we choose to test the following two hypotheses.

Hypothesis 5A: "There is a positive relation between the bidder's relative amount of cash compared with the bid value and its stock return on the announcement date"

Hypothesis 5B: "There is a negative relation between the bidder's relative amount of cash compared with the bid value and its stock return on the announcement date"

Bidder's Governance

Duality of the functions of CEO and Chairman of the board of directors

The supporters of the separation of the duties of CEO and chairman of the board of directors argue that having the same person for these two functions has the effect of weakening the internal managerial culture within the company by making the assessment of the CEO's performance by the board of directors difficult (Jensen, 1993). According to Fama and Jensen (1983), the separation of deciding and controlling functions is necessary to lower the agency costs and the risks of entrenchment of the manager. This comment is also confirmed by the studies of Finet and Labelle (2004), which show that in a period of bad results for the company, the duality of the functions of CEO and chairman of the board increases the probability that the CEO keeps his post. Also, still according to supporters of a separation of the roles, such a separation could ensure an enhancement of the company's performance: Rechner and Dalton (1991) show, on a sample of 141 companies having a fixed managerial structure between 1978 and 1983, that companies whose functions of CEO and Chairman of the board are separated achieve higher performances. Pi and Timme (1993) also reach this conclusion considering a similar sample over the period 1987-1993. However, Boyd (1995) and Finkelstein and D'Aveni (1994) claim that companies with an overlap in the functions of CEO and chairman of the board of directors are not less efficient. The argument proposed by these authors is that the goals of the managers and those of the board of directors are not necessarily divergent. Moreover, the plurality of these functions enhanced the flexibility of the firm and can be benefic, especially in case of crisis. Since the former studies show contradictory results, we decided to test the following two hypotheses.

Hypothesis 6A: "There is a positive relation between the duality of the functions of CEO and chairman of the board of directors and the bidder's return on the announcement date"

Hypothesis 6B: “There is a negative relation between the duality of the functions of CEO and chairman of the board of directors and the bidder’s return on the announcement date”

Percentage of executive directors

The presence of non executive directors (so non-subordinated to the CEO’s authority) on the board improves the monitoring of the decisions made by the managers and therefore reduces the agency costs. Indeed, it can be thought that, if the directors are not internal to the company, they will have fewer qualms to denounce the possible opportunistic behaviors of the managers because of the absence of implicit agreements. Thus, in the case of the acquisition of a company, the presence of non executive directors will constitute a warranty for the investors that the takeover decision is rational and that the acquisition is not aimed to pursue the manager’s interests. Moreover, the appointment of external directors should also allow the company to benefit from additional expertise. Therefore, the presence of external directors will have a positive effect on the company’s profitability. In conclusion, an increase of the percentage of directors belonging to the executive committee of the company augments the probability of managers’ entrenchment and lowers the profitability of the bidder.

Hypothesis 7: “The percentage of executive directors on the board of directors has a negative effect on the bidder’s return”

Bidder’s Characteristics

Return on equity (ROE)

This indicator measures the ability of the company to generate profit for its shareholders. It can be instinctively thought that the higher the ROE is, the more efficiently the shareholder’s equities are used and the higher the stock return of the company will be. Therefore, on the announcement date, a high ROE should constitute a proof of the competence of the management in place and encourage investors to trust the different plans launched by these managers. Thus, we state the hypothesis that the bidder’s ROE has a positive influence on its stock market value on the day of the takeover announcement.

Hypothesis 8: “Bidder’s ROE positively influence the company’s profitability on the announcement date”

Debts / shareholder’s equities

The acquisition of a company represents an important financial constraint for the purchaser and this constraint grows with the relative size of the target (Ahujja and Katila, 2001). Also, the bidder’s indebtedness before the takeover announcement increases this financial constraint and might influence the future profitability of the merged entity. Therefore, the higher the Debts/Shareholder’s equities ratio is, the riskier the deal will be. Thus, because of the financial constraint that the purchaser’s indebtedness constitutes, we state the hypothesis that the bidder’s Debts/Shareholder’s equities ratio negatively influences his stock value.

Hypothesis 9: “The indebtedness of the bidder has a negative influence on his stock value on the announcement date”

The logarithm of the total amount of assets - the size of the company

This variable is used to take into account the size of the bidder which is apprehended by the total asset value of the company. Because of their higher media exposure, big companies are often more closely monitored by financial analysts. This market supervision limits the opportunistic behaviors of the managers and influences them to act towards a maximization of shareholders value. Moreover, big companies are able to integrate other companies at a lower cost and without necessarily having to make considerable organizational changes. However, it can also be thought that, in the case of small companies, the potential to increase the profitability per share will be higher. Nevertheless, since the risk of this type of operation is also higher, the investors' response will depend on their risk aversion. Given these opposed views, we test the following two hypotheses.

Hypothesis 10A: "The bidder's size has a positive influence on its stock value on the announcement date"

Hypothesis 10B: "The bidder's size has a negative influence on its stock value on the announcement date"

Market Variable

Return of stock market index on the announcement date

The use of this variable is aimed to take into account the general level of investors' confidence on the day of the announcement. Indeed, it can be thought that, during a good period for stock markets, investors tend to be more optimistic and therefore to react more favorably to takeover announces. On the contrary, during a period of market drop, investors might appear more pessimistic towards takeover transactions. The indicators used in our study are the Dow Industrials for the companies quoted on the NYSE and the NASDAQ composite for the companies quoted on the NASDAQ.

Because of the supposed influence of the stock market index return on the trust level of investors, we state the hypothesis that the bidder's profitability is positively linked to the profitability of the market index on the day of the announcement.

Hypothesis 11: "The return of the market index has a positive influence on the bidder's stock value on the announcement date"

SAMPLING AND METHODOLOGY

Sample

The sample of this study includes 61 takeovers announced between 2005 and 2007 by companies quoted on the NASDAQ or on the NYSE. The spreading out per market of these 61 bids is: 10 on the NASDAQ and 51 on the NYSE. Note that target companies were all quoted firms. For the selection of our sample, we adopted several rules.

- Firstly, we rejected announces made on non quoted companies and those announced by a consortium of companies.
- Secondly, we also rejected the announcements made by companies quoted on American markets other than the NASDAQ and the NYSE.

- Thirdly, in the case of successive offers announced by the same company, only the first bid was taken into account.
- Fourthly, the companies that announced several purchases during the period of analysis were not removed from the sample, and each announcement was analyzed separately.

Methodology

The rank test

For this study, we used the rank test which is a non parametric test derived from the event study methodology. The use of this test is justified by the presence in the sample of bidding companies quoted on two markets (NASDAQ and NYSE) with different structures. Also, Campbell and Wasley (1993) showed the limits of parametric tests to conduct event studies on markets such as the NASDAQ because of a high volatility which tend to distort the results and to overestimate the effects of these events. In practice, the methodology of this test first sorts the observed profitability on a period of 140 days before the announcement of the takeover to 20 days after the announce. After that, the 161 observations of returns are sorted in ascending order and numbered from 1 to 161. Then, these dates are sorted again in chronological order. Finally, for each company, we consider the ranks related to the period of event (between 20 days before the announcement and 20 days after), in order to detect the possible effects of forecasting or delay. For each day of the period of event, we then calculate the average of the observed ranks on our whole sample. Then, we determine an abnormal rank for each day of the period of event by subtracting 80.5, corresponding to the average or a normal rank, from the observed average rank. So we are able to determine for each day of the period of event, a standard deviation and a “t” stat.

Model

The model we used to make our linear regression is made up of eleven variables, of which four are binary.

FIGURE 1 EQUATION MODEL

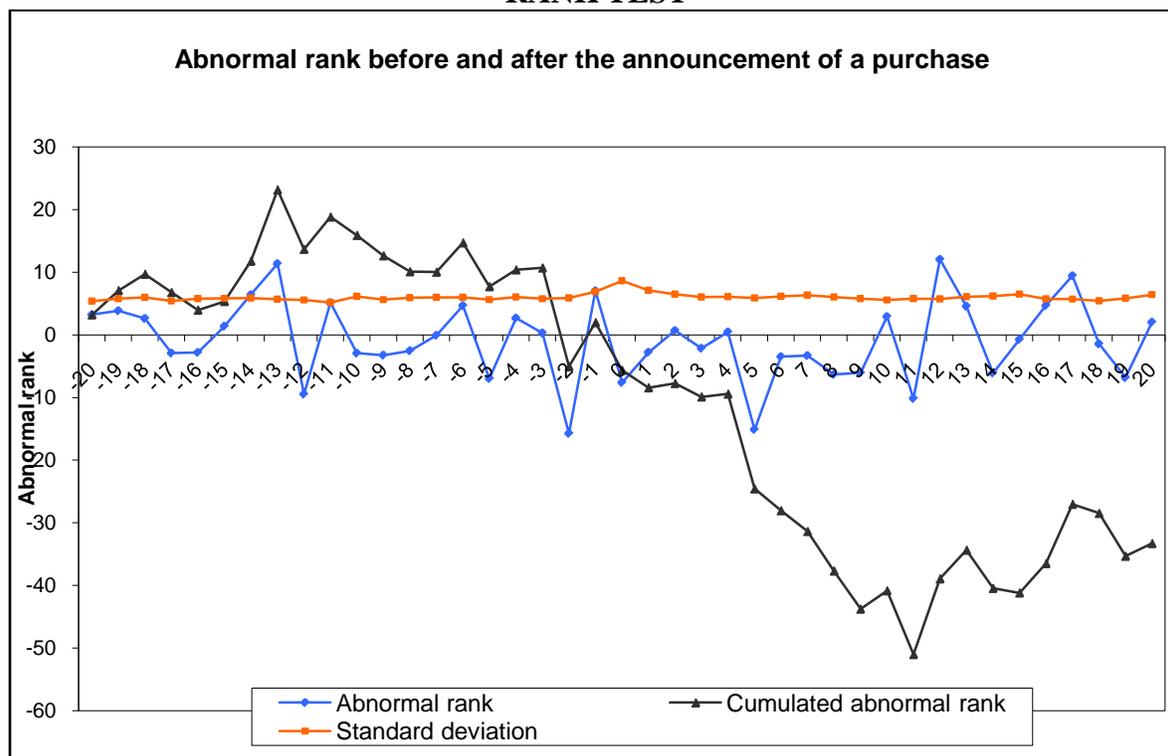
$$\text{RENTA} = \beta_0 + \beta_1 \text{METH} + \beta_2 \text{PREMIUM} + \beta_3 \text{DIVERS} + \beta_4 \text{HOST} + \beta_5 \text{LIQVAL} + \beta_6 \text{DUALITY} + \beta_7 \text{EXDIR} + \beta_8 \text{ROE} + \beta_9 \text{DEEQ} + \beta_{10} \text{LNTA} + \beta_{11} \text{INDICE}$$

RESULTS

Results of the Ranks Test

The analysis of the results of the rank test enables us to draw several conclusions. Firstly, we notice a negative abnormal rank but this rank is not statistically significant. These results are in line with empirical studies made on the subject. Secondly, the analysis of cumulated abnormal ranks enables us to highlight forecasting phenomena, two weeks before the announcement, tending to lower the purchaser's rate. Two significant abnormal ranks J_{-13} and J_{-2} support this hypothesis¹. Thirdly, the high observed standard deviation in J_0^2 shows a high volatility of the relative returns associated with the takeover announcement (this standard deviation is the most important one during the announcement period). Considering our data, we notice that, among our

FIGURE 2
RANK TEST



61 companies, 18 show a rank between 1 and 5 on the announcement day (rank 1 being the one associated to the lowest return observed between J_{-140} and J_{+20}) and 10 companies show a rank between 156 and 161 (rank 161 being the rank associated with the highest return between J_{-140} and J_{+20}). Thus, 46% of the firms in our sample show extreme results on the announcement day, but these results tend to compensate for each other and the observed abnormal rank on the announcement day is not significant. This gives us a neutral opinion about the influence of takeover announcements on bidders' stock value.

Results of the Linear Regression³

It appears that our model is significant and reliable at the 1 percent threshold. On analyzing the t-stat, we notice that four variables are significant at the 5 percent threshold and one at 10 percent threshold. These variables are respectively: the type of diversification (linked vs. not linked), the possible hostile characteristic of the offer, the duality of the functions of CEO and chairman of the board of directors, the ROE and the ratio of debts to shareholder's equities.

TABLE 1
RESULTS OF THE MODEL

<u>Coefficients:</u>					
	Value	Std. Error	Beta	t	Proba
(Constant)	0,0655	0,1271	0,0000	0,5157	0,6108
METH	0,0089	0,0226	0,0715	0,3938	0,6972
PREM	0,0026	0,0560	0,0066	0,0466	0,9632
DIVERS	0,0744	0,0223	0,4775	3,3454	0,0027
HOST	0,0367	0,0162	0,2897	2,2675	0,0326
LN LIQVAL	-0,0083	0,0052	-0,3429	-1,5879	0,1254
EXDIR	-0,1132	0,0706	-0,2454	-1,6041	0,1218
DUALITY	0,0418	0,0182	0,3341	2,2933	0,0309
ROE	0,0686	0,0267	0,3675	2,5678	0,0169
DEEQ	-0,0055	0,0031	-0,3001	-1,7612	0,0909
INDICE	-1,3150	1,2894	-0,1509	-1,0199	0,3180
LNTA	-0,0052	0,0056	-0,1702	-0,9243	0,3645
<u>Summary of the model:</u>					
R ²	0,6553				
R ² Adjusted	0,4973				
<u>Analysis of the variance:</u>					
	ddl	Sum of squares	Mean square	F	P
Regression	11	0,0898	0,0082	4,1478	0,0017
Residual	24	0,0472	0,0020		
Residual	35	0,1371			

Interpretation of the results relative to the significant variables

A. Deal characteristics

• *Nature of the diversification (DIVERS)*

This variable is significant at the one percent threshold and shows the investors' preference for linked acquisitions by opposition to those that are not linked. This result is in line with the theoretical works of Lubatkin (1983) and demonstrates the importance of the industrial logic in takeover operations. Moreover, this preference of the financial markets for linked acquisitions can also be interpreted as a fear of takeovers with a conglomeral purpose that might be led by the CEO's own interests (Amihud and Lev, 1981; Shleifer and Vishny, 1989; Kroll, Simmons and Wright, 1990). Finally, this result allows us to reconcile theoretical and empirical studies on this topic; the different authors seem to be unanimous about the superiority of concentric bids but few empirical works had emphasized this so far.

• *Possible hostile nature of the bid (HOST)*

This variable indicates the market's preference for hostile bids by opposition to friendly ones. This result agrees with our hypothesis 4A stating the positive influence of hostile takeovers on bidders' stock value on the announcement date. On the one hand, the preference of financial markets for hostile bids indicates that investors are not especially worried about the risk of failure of a bid and the costs linked to the mechanism developed by the target. On the other hand, investors' preference for hostile bids might be associated with their disciplinary character for the target's management that has not been able to generate a sufficient performance to warrant the

company's independence. The bidder's management, seen as more efficient in the opinion of investors, should therefore allow to generate a higher profitability. Finally, hostile bids constitute a signal for investors showing a great confidence of the bidder which is convinced of the important return that will be generated by the deal. This confidence of the bidder can be related to the possession of private information.

B. Corporate governance variable

- Duality of the functions of CEO and chairman of the board of directors (DUALITY)

In line with our hypothesis 6A, the linear regression shows a positive and statistically significant relation between the bidder's return and the duality of the functions of CEO and chairman of the board. In our opinion, the explanation of this result lies in the notion of optimal discretionary power. This notion aims at installing a managerial system that is both adaptable (in order to make possible flexible management) and strict enough to limit the opportunistic behaviors of a CEO. When a company enters into an acquisition process, some investors consider positively the concurrent holding of the positions of both CEO and chairman of the board since this situation generates a higher flexibility that is necessary for a good sequence of the takeover process. Thus, at the time of the takeover announcement, the separation of the positions of CEO and chairman of the board does not appear to investors as a key variable of the government system that could control the CEO opportunism. Instead, at the moment of the takeover announcement, markets prefer a duality of the functions since it makes the decision process easier and quicker. However, markets are not that indifferent to the bidder's governance. Indeed, with a t-stat of -1.6041, the EXDIR variable is not significant but tends to show a negative relation between the percentage of executive directors and the bidder's profitability. Therefore, investors tend to give more confidence to non executive directors which are considered as the guarantors of the industrial rightfulness of the transaction. In conclusion, because of increased organizational flexibility, markets consider positively the concurrent holding of the positions of both CEO and chairman of the board of directors' on the date of the takeover announcement. Nevertheless, the markets appreciate the presence of external directors in order to make sure that the purchase transaction is not intended to serve the CEO's personal objectives.

C. Variables concerning the bidder

- Return On Equity (ROE)

This variable is significant and shows a positive relation between the profitability of the funds invested in the company and the bidder's return at the time of the announcement. Therefore, it can be thought that investors use the previous profitability of the company (return of the invested shareholder's equities) to predict its future performance.

- Debts/ shareholder's equities ratio (DEEQ)

According to our hypothesis, this statistically significant variable indicates that there is a negative relation between the relative indebtedness of the bidder and its stock return at the time of the announcement. Thus, the previous indebtedness of the purchaser is seen as a handicap which, added to the numerous charges associated with the purchase deal, could be harmful to the transaction. In addition to the costs associated with the previous indebtedness of the purchaser, a high indebtedness ratio could cause problems for the company to find necessary funds to overcome the difficulties that could occur during the merging process.

CONCLUSION

The purpose of this study was, on the one hand, to determine the impact of a takeover announcement on the purchaser's share price and, on the other hand, to emphasize the factors influencing this profitability. Firstly, the results of the analysis of the abnormal ranks did not enable us to show a statistically significant abnormal return on the announcement day. Almost the half of the firms in our sample show extreme results (positive and negative) on the announcement day, but these results tend to compensate for each other and the observed abnormal rank on the announcement day is not significant. However, if we take a period from two weeks before the announcement till two weeks after it, we notice a significant decrease in the cumulative abnormal rank; which shows a decline of bidder's stock value. Next, using eleven independent variables, we investigated the explanatory factors of the bidder's stock return on the announcement date. After applying a linear regression to our model, we found five variables as having a statistically significant impact on bidders' stock value. Two of these variables are associated with the deal, one with the bidder's governance and two are linked to the previous bidder's performances. The first significant variable is the type of diversification that indicates the investors' propensity to give credibility to concentric bids and shows the investors' concern for the industrial logic of a merger. The second significant variable is related to the hostile nature of the bid which positively influences bidders' stock value on the announcement date. This observation could be linked to the trust signal sent by the purchaser or to the disciplinary nature of the hostile bids towards the target's management. The third significant variable is linked to the duality of the functions of both CEO and chairman of the board of the directors' that positively influences bidders' return. On the day of the takeover announcement, investors favorably perceive this concurrent holding of functions because it allows an increased flexibility. However, markets appreciate governance mechanisms - such as the presence of external directors - aimed at containing the opportunistic behaviors of the CEO. The fourth significant variable is the ROE which has a positive effect on the bidder's stock return on the announcement day. Investors therefore use the previous performances of the bidder to evaluate its ability to carry out a profitable merger. The fifth significant variable is the debts to shareholder's equity ratio which has a negative effect on the bidder's profitability. The previous indebtedness of the purchaser is therefore regarded as an embarrassment that could be harmful for the merger. The limits of our study mainly concern the methodology and the choice of variables. First, regarding the methodology, our event study uses the rank test in order to determine abnormal profitability. In some cases, increases in terms of ranks may be slight in proportion to the increases in term of profitability and the effect of the event can therefore be more or less undervalued. Moreover, the daily observed profitability does not take account of events that are external to the announcement. Finally, our results are peculiar to our sample. Indeed, as highlighted in our literature review, several studies on this topic show different and sometimes contradictory results.

ENDNOTES

1. See table 1 in appendix
2. See table 1 in appendix
3. Reminder regarding the meaning of the variables:

METH: method of payment - binary variable: 1=cash - 0=share parts or mixed.
PREM: purchase premium in percentage relative to the purchaser's closing price the day before the announcement.
DIVERS: nature of the diversification - binary variable: 1= linked diversification - 0= non linked diversification.
HOST: hostile offer vs. friendly offer - binary variable: 1= hostile offer - 0= friendly offer.
LIQVAL: logarithm of (purchaser's liquid assets / total amount of the bid).
DUALITY: holding of CEO and chairman of the board of directors functions - binary variable: 1= concurrent holding - 0= separation of the functions.
EXDIR: percentage of executive directors on the board of directors.
ROE: return on equity.
DEEQ: total debts / shareholder's equities.
LNATA: logarithm of the total assets.
INDICE: yield of the market index on the announcement day.

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APPENDIX

**TABLE 2:
RESULTS OF THE RANKS TEST**

Day	Abnormal rank	Cumulative Abnormal rank	Standard deviation	Statistical t
-20	3.216672935	3.216672935	5.399634	0.595720581
-19	3.860132151	7.076805086	5.775438	0.668370488
-18	2.622740648	9.699545734	5.982354	0.438412837
-17	-2.916812312	6.782733422	5.420374	-0.538120155
-16	-2.811401665	3.971331757	5.809575	-0.483925519
-15	1.377886183	5.34921794	5.828378	0.236409869
-14	6.422649205	11.77186715	5.898841	1.088798492
-13	11.37998053	23.15184768	5.717722	1.990299694
-12	-9.476512318	13.67533536	5.571769	-1.700808553
-11	5.149543152	18.82487851	5.188672	0.992458717
-10	-2.928795823	15.89608269	6.158669	-0.475556388
-9	-3.252291616	12.64379107	5.619769	-0.578723323
-8	-2.542521183	10.10126989	5.964732	-0.426259061
-7	-0.076019704	10.02525019	6.013166	-0.012642209
-6	4.680327869	14.70557805	6.014986	0.778111155
-5	-6.987378597	7.718199457	5.627403	-1.24167012
-4	2.674391422	10.39259088	6.046991	0.442268125
-3	0.307799238	10.70039012	5.777892	0.053271889
-2	-15.76082756	-5.060437444	5.892112	-2.674902707
-1	7.0382993	1.977861857	6.925731	1.016253643
0	-7.620543056	-5.642681199	8.631419	-0.882884158
1	-2.784942073	-8.427623272	7.104158	-0.392015774
2	0.687473729	-7.740149542	6.508444	0.105627964
3	-2.147360309	-9.887509851	6.070654	-0.353727985
4	0.461151302	-9.426358549	6.087093	0.075758867
5	-15.13033266	-24.55669121	5.908754	-2.560664022
6	-3.485420676	-28.04211189	6.136021	-0.568026199
7	-3.314952471	-31.35706436	6.371943	-0.52024204
8	-6.319863867	-37.67692823	6.041099	-1.046144649
9	-6.078416407	-43.75534463	5.814367	-1.045413234
10	2.924577628	-40.830767	5.568413	0.52520824
11	-10.16978607	-51.00055307	5.788197	-1.756986736
12	12.07301092	-38.92754215	5.766019	2.093821026
13	4.577793265	-34.34974888	6.084202	0.752406511
14	-6.09784813	-40.44759701	6.217250	-0.980795089
15	-0.726020072	-41.17361708	6.488706	-0.1118898
16	4.686551921	-36.48706516	5.763424	0.813154162
17	9.456859362	-27.0302058	5.724576	1.651975654
18	-1.43683768	-28.46704348	5.448059	-0.263733876
19	-6.845980546	-35.31302403	5.831763	-1.17391273
20	2.024523795	-33.28850023	6.428717	0.314918781