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Emerging Markets Queries in Finance and Business

Similarities between the acquirer and the target company in successful takeover bid offers

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Abstract

In order to narrow the high competition between firms that operates in the same industry, mergers and acquisitions (M&As) transactions are frequently encountered in Romania. In many M&As can be found some similarities between the acquirer and the target company. The study analyze how a successful takeover bid offer is influenced by similarities regarding the age, the geographical position, the industry or ownership between the acquirer and the target company. The results point out that some variables have an important influence on the successful takeover bid, while others are not significant in the acquirer's point of view.

Keywords: mergers and acquisition, takeover bid, similarities

1. Introduction

Mergers and acquisitions are one of the key strategies used by corporation to diversify or consolidate their business. In many cases, companies are looking to acquire firms in the same industry in order to minimize the competition and so to gain new market share. But a question remains. Are they willing to buy any company or they are looking after some specific characteristics?

The purpose of every M&A is to expand and to maximize the profits. In case of a takeover, the acquirer can benefits from the assets and know-how of a target firm in order to develop a stronger and competitive business. In this case, it would be preferable for the investor to buy a firm that has the same characteristics in order to

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assure a potential synergy and similarity of management practices. In the literature we find the terms similarity or compatibility to describe the possibility of synergy between firms with comparable features (Shelton, 1988; Greenwood et al., 1994).

The aim of this study is to analyze if success in a takeover bid in the Romanian capital market depend on the compatibilities between the acquirer and the target firm. There are studies in the literature that pointed out that some matching features between companies can be significant for a successful M&A, but, to our knowledge, none of them had this as the main purpose (Bena and Li, 2012; Ragozzino and Reuer, 2011; Dragota et al., 2013). Moreover, not many studies have been conducted on emerging markets economies which are nowadays some of the most profitable business places.

Further study is structured as follows. In Section 2 are presented the main findings of other studies in the field. Section 3 presents the database and methodology. Section 4 presents the main empirical results and section 5 contains the conclusions.

2. Literature review

In the literature, there are many studies that analyze the factors that lead a company to buy another one. The reasons can be the value of the future synergy, the size of the private benefits of control or simply companies try to gain market share by acquiring the competition (Barclay and Holderness, 1989; Dyck and Zingales, 2004). We believe that it is easier to accomplish all this if the acquired company has the same characteristic as the buyer or complete the buyer needs to develop its activities. From this point of view and according to the literature we tested hypotheses to explain the takeover bid success between the acquirer and the target company in order to analyze the similarities.

We know that companies are voluntary combining their skills and expertise to develop new products and technologies because this is the way to survive in a rapidly changing market economy nowadays (Grimpe and Hussinger, 2008; Higgins and Rodriguez, 2006). But when this is not possible the stronger company will buy the weak in a takeover process to assure a higher market share.

Acquirers are always attracted to invest in targets that act in the same industry. The more related the technologies are between companies that engage in a M&A, the more likely is that, in the end, the transaction will be successful (Ahuja and Katila, 2001). In this way the post M&A gains can rise from a joint effort of the production capacity and know-how. The most valuable targets for an acquirer are those with related R&D activities that can complete or develop their own activities (Bena and Li, 2012). So, the industry similarity or the technological proximity, as it is defined in the literature, can be a key factor in explaining the success of a takeover bid (Lehto and Lehtoranta, 2006; Singh and Zollo, 2004). Considering these elements the first hypothesis tested in this study are:

H1: The fact that the acquirer and the target company are in the same industry increase the chance of a successful takeover bid.

As we previous said, the companies are looking to increase their market share. This is always related to a specific city, state or region. If a company want to have a stronger position on the market it must start doing so in the nearby region. This is the reason why many M&A transaction happen in the same area. Moreover, a successful M&A depends on the right information about the parties. If they are in the geographical proximity there is a high chance that the correct information aboutthe firm's physical assets, leverage, the value of the total sales and profit is transmitted prior to the M&A decision (Ragozzino and Reuer, 2011; Cassiman et al., 2005). Also the closeness can facilitate the transmission of some soft information that in many cases are decisive for the success of a takeover (Uysal, et al., 2008; Kand and Kim, 2008). According to these findings in the literature we formed our second hypothesis:

H2: The geographical similarity between the buyer and the seller in a takeover bid offer increase the chance of success of the transaction.

Another question is which investors are more likely to succeed in a takeover offer: domestic or foreign investors? After the transition to the market economy, Romania had an inflow of foreign capital, investors that where looking to expand their business in the Eastern Europe. Domestic investors also tried to find new opportunities on the same market and so, in many cases, the owner was the one to decide. From a previous study on the Romanian market we learned that domestic owners are not likely to easily give up their business to domestic investors (Dragota et al., 2013). Our third hypothesis is:

H3: The similarity between the acquirer and the target firm ownership can reduce the chance of a successful takeover

The age of a company is very important when it comes to M&A decision. An old company has a well defined market share, with loyal customers and this will always attract investors. Also, old companies have well implemented strategies and practices that worked over the years, but new firms are innovative and in this way can reduce the gap. In our point of view a transaction between two firms with different age, a new and an old firm, can complete each other's businesses. If the two companies have around the same age we expect that the probability of a successful transaction will decrease. For this reason, we have tested as our forth hypothesis:

H4: The age similarity can decrease the chance of a successful takeover bid

Another important thing is the prior M&A experience. If both the acquirer and the target company dealt with previous M&A transactions, they will capitalize its M&A-specific knowledge by involving in additional M&As (Amburgey and Miner, 1992). We believe that there is a less chance for a successful M&A transaction in case of firms with previous M&A experience as owners have the experience to wait for the right price to sell their business. In accordance to this, our last hypothesis will be:

H5: Prior M&A experience decreases the chance of a successful takeover bid.

In our empirical part of this study, we test all these hypotheses and also attempt to more explanations for why and how the similarities can influence the success of mergers and acquisitions transactions.

3. Database and methodology

The database contains all the transaction that took place on the BSE(Bucharest StockExchange)andRASDAQ(the Romanian equivalent for US NASDAQ)during the period 2000-2012. The sample include takeover bids where there acquirer aimed and obtain the control of the target company at the end of the transaction and takeover bids where the acquirer only aimed to obtain the control but did not succeeded in doing so. We have not taken into account transactions that not imply the possibility for the bidder to take effective control of the company.

The database of our study consists of 309 takeover bid offers. In each case both the acquirer and the target company were legal persons. Due to our previous hypothesis (age similarity, geographical similarity) we could not include in our database the cases where the acquirer was a natural person. In the end our database includes almost 49% of successful takeover bids, offers where the acquirer succeeded in gaining the controlling position at the end of the transaction.

As we described in the abstract section, the aim of this study is to analyze the similarities between the companies that engage in takeover bids and if these have an impact on the success of the transaction. In order to do that, we used a Probit model and we based on the assumption that the probability of an event to occur is linearly related to a set of explanatory variables. We considered that the coefficient estimated for the independent variables with this model will describe the change in the probability for the dependent variable. In Table 1 we present the variables used in the model to explain the probability of success of a takeover bid offer.

Table 1. Variables used in the model

Indicator	Explanation
AGESIM	Age similarity between the acquirer and the target company - The age of the young firm divided by the age of the old firm. The age was measured in years.

DINDSIM	Industry similarity - The target and the acquirer are in the same industry - dummy variable (1-if they are, 0-otherwise)
DOWNSIM	Ownership similarity – Both the acquirer and the owner of the target firm are domestic investors - dummy variable (1 - if is true, 0 – otherwise)
DGEOSIM[†]	Geographical similarity - The acquiring and target company are located in the same region – dummy variable (1 for the same regions, 0 for different regions)
DINDUSTCONC	Competition similarity – If the number of companies in a both the acquirer and target industry concentrates more than 10% of the registered firms at the national level – dummy variable (1- if is true, 0-otherwise)
DDIRCOMP	Direct competitors – If the acquirer and the target are located in the same region and act in the same industry – dummy variable (1- if is true, 0-otherwise)
PRIORMA	Prior M&A experience – We considered here the minimum between the number of prior takeover bid offers (succeeded or not) of the acquirer or the target.
SOTP	Stake owned before the takeover process – we considered that the more the acquirer owns the more familiar and interested is in acquiring the target.

In Table 2 we presented the descriptive statistics of the explanatory variables used in the model. For each one we have analyzed the mean, median, standard deviation and the maximum and minimum value.

Table 2. Dependent variables

	Mean	Median	St.Dev.	Max	Min
AGESIM	0,49	0,45	0,26	1,00	0,05
GEOSIM	0,57	1,00	0,50	1,00	0,00
DOWNSIM	0,79	1,00	0,41	1,00	0,00
DINDSIM	0,41	0,00	0,49	1,00	0,00
DINDUSTCONC	0,33	0,00	0,47	1,00	0,00
PRIORMA	0,60	1,00	0,49	1,00	0,00
DDIRCOMP	0,24	0,00	0,43	3,00	0,00
SOTP	0,14	0,00	0,18	0,50	0,00

This table summarizes the characteristics of the variable used to analyze the probability of a successful takeover bid. These variables charactherize the target company or the industry this one. The sample consists of all the takeover bids on the Romanian capital market between 2000 and 2012.

[†]We considered the acquirer and the target firm in the same region if they are located in the same NUTS 2 region. The NUTS classification (Nomenclature of territorial units for statistics) is a hierarchical system for dividing up the economic territory of the EU. This was made for the purpose of the collection, development and harmonisation of EU regional statistics, socio-economic analyses of the regions (NUTS 1: major socio-economic regions, NUTS 2: basic regions for the application of regional policies, NUTS 3: small regions for specific diagnoses). In Romania there are 8 NUTS 2 regions.

4. Results

In this section we have tested the hypotheses proposed in section 2. We used a Probit model where the dependent variable takes value 1 if the acquirer succeeded in owning, at the end of the transaction more than 50% of the target share, and 0 if he has not succeeded. We refered only to takeover bid offers that happened on the Romanian capital between 2000 and 2012. The results of the model are presented in Table 3.

Table 3. The model estimated results

Variable	(1)	(2)
AGESIM	-0.95***	
	(-3.10)	
GEOSIM		0.37*
		(1.68)
DOWNSIM		-0.57**
		(-2.45)
DINDSIM	0.67***	1.05***
	(4.29)	(4.23)
DINDUSTCONC	0.33**	0.27*
	(2.09)	(1.73)
PRIORMA	-0.72***	-0.71***
	(-4.56)	(-4.48)
DDIRCOMP		-0.64**
		(-2.04)
SOTP	0.95**	1.21***
	(2.28)	(2.91)
Intercept	0.41*	0.15
	(1.79)	(0.64)
Mcfadden R-squared	12.55%	12.85%
Probability (LR stat)	2.33*E(-10)	1.46*E(-9)

To estimate the probability of a successful takeover bit we used the probit regression model. The regression uses 309 observations of takeover bids on the Romanian capital market between 2000 and 2012. We consider a takeover bid successful if there is a change in the target's controlling ownership. We did not consider in the same regression the variables correlated at a higher level than 0.3. T-statistics are in parentheses. The symbols *, **, *** represent significance levels of 10%, 5% and 1%.

The results are conclusive with the hypotheses presented in section 2. The age similarity decreases the chance of a successful takeover bid. If two companies with similar age engage in a takeover bid there is a little chance that the transaction will succeed. On the Romanian market, this is due to the fact that investors want to diversify their strategies. If he owns a relatively new firm he is looking for an old company than can offer him stability and if he owns an old firm, he will like to acquire a new innovative firm with great develop opportunities.

The geographic similarity can increase the chance of a takeover. Being in the same region, the acquirer is more likely to have the information if the target company offers the opportunity of a future synergy. The same is the case of a target company that acts in the same industry as the acquirer. The buyer knows how the business well and he can easily judge if the target offers him the chance to develop and grow in the future. According to our results, there is an increasing chance of a change in the control of the firm if the companies are acting in high competition industries. The only way to survive in this business environmental is to develop fast and M&A transaction is the best way to achieve this.

Other results suggest that if the acquirer and the target are in the same location and industry or have the domestic ownership the chance of a successful takeover bid decreases. We consider that the ownership of a company will not accept to be acquired by the competition, maybe due to the self-pride or unless a high price is offered. If the acquirer already owns some of the target's equity shares this will increase the probability that the takeover will succeed.

Prior M&A experience is important and significant in this model. On the Romanian capital market the companies with M&A experience usually not succeed in takeovers. For example, if the target company has prior offers the owners know that there is a permanent interest in their business and will try to obtain as much as they can in case they decide to sell the company. This can mean a lot of takeover offer rejections.

5. Conclusions

This study analysis if there is any influence between the takeover bid offer and the similarities recorded among the acquirer and the target company. We found out that if the companies involved are similar, in terms of geographical location, ownership characteristics or industry sector, there is a higher probability for a takeover bid to be successful. Contrary, if the age is similar there is less chance to have a change in control at the end of the transaction.

We also found that the prior M&A experience is significant in explaining the probability of success. If the involved parties have encounter previous takeover bids, the chances of successful takeover decreases.

Future research can be conducted on other similarities. We think that firm size and structure or accounting and financial data about the acquirer and the target could also be significant in explaining the success in a takeover process.

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