Do telecom carrier takeovers create value? Longitudinal analysis of U.S. telecom carrier takeovers from 1996 to 2005

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\begin{abstract}
Takeovers by telecommunications carriers have surged during between 1996 and 2005, stimulated by the Telecommunications Act of 1996. In this study, we hypothesize and test the short-term and long-term performance of telecommunications carrier mergers and acquisitions (M&As) between 1996 and 2005 according to three main categories (strategic types, bidder characteristics, and payment methods). For short-term performance, this study investigates abnormal market returns of bidding firms after M&A announcements and our study shows that telecommunications carrier M&A announcements do result in a significant increase in shareholder wealth in the short run. However, from a long-term perspective, which has been investigated in terms of the survival rate and the operating performance after M&As, the telcos experience a statistically significant decrease of up to 10%. The results also show that though strategic type, bidder characteristics, and payment method play an important role in the value creation of M&As in the short term, only the bidder size matters in the success of M&As over a long period of time.
\end{abstract}

1. Introduction
Mergers and acquisitions (M&As) are an important vehicle for firms to achieve sustainability in the future (Majumdar, Yaylacegi, & Moussawi, 2012), and the primary motivation of firms to enter M&As has changed in pace with ever-changing business environments. Telcos also have pursued M&As to obtain resources such as labor, knowledge, and capital for providing a host of different service lines — long-distance, local, wireless, and cable (Singh, 2014).

In the telecom industry, the most recent merger wave is sparked by convergence. Indeed, telcos are well acquainted with convergence since their industry has already experienced voice and data convergence, fixed and mobile convergence (FMC), and telecommunications and broadcasting convergence (TBC). Most recently, they face heterogeneous inter-industry convergence\textsuperscript{1} (HIC). In this convergence era, through the types of convergence-oriented takeovers, telcos can quickly integrate different communications, capture a developed customer base, consolidate smaller niches, and accelerate the implementation of new technologies with combined resources (Evens & Donders, 2016; Singh, 2014). In particular, the deregulation that followed the Telecommunications Act of 1996 further unleashed these market forces, increasing M&As not only within but also outside the industry.

The focus of M&A studies has been the impact takeovers have on shareholder wealth. Since shareholder wealth creation within
the acquiring firm varies among each individual M&A, many studies have hypothesized and tested antecedents of M&A performance. Unfortunately, however, there have been a limited number of studies that investigates the wealth creation of telecom M&As and characteristics specific to telcos remain uncharted. In addition, most of the studies focus more on the short-term wealth effect of M&As, and lack deep investigation of the long-term wealth effect of M&A deals by telecom carriers and the affecting factors of M&A deals' success in the telecommunication industry. Thus, this study first examines whether shareholders' wealth is created by telecommunication takeovers, both in the short-run and long-run perspectives. This work also explores the empirical evidence of any performance variations depending on the types of M&A strategy pursued by the acquirer; the characteristics of the acquirer; and the payment methods chosen.

Note that after the Telecommunications Act of 1996, telecommunications firms, which had not previously experienced multi-market contact, began trying to diversify their businesses into other markets. This paper focuses on the effect of the new regulation, and hence we use only 10-year takeover data after the Telecommunications Act of 1996.

This paper is composed as follows. Relevant studies on the wealth effect of M&As by telecommunications carriers and the factors affecting the wealth effect of M&As are discussed in Section 2. Research hypotheses are developed based on literature review. Methodology is explained in Section 3, and results of this study are presented in Section 4. In Section 5, conclusions are drawn.

2. Literature review

2.1. Wealth creation of M&As by telecom carriers

Regarding the short-term wealth effect of M&As in the telecommunications industry, previous studies have drawn several mixed results. For example, Wilcox, Chang, and Grover (2001) analyzed 88 M&As in the U.S. telecommunications industry and found significant abnormal bidder returns at the time of takeover announcements. Trillas (2002) analyzed data from 12 large telecom acquisitions in Europe and found that the acquirer's market return in those cases was not significant. The paper concluded that the data demonstrated the paradox that acquiring a company in the telecommunications industry did not necessarily provide added value to the shareholders of the bidding company. However, the paper failed to further investigate the variation of shareholder wealth creation with respect to the specific characteristics of each individual M&A. On the other hand, Rhéaume and Bhabra (2008) found that takeovers of companies within the same sector of industry, where the acquisition strategy was intended to achieve synergistic gains, resulted in positive wealth change for the acquiring firm's shareholders.

As for the long-term wealth effect of M&As in the telecommunications industry, previous studies were limited with mainly negative results. Through the analysis on M&As carried out during the 1990–1993 period in the telecommunications industry, Ferris and Park (2002) concluded that bidding firms have worse performance compared to their size and industry-matched control firms 5 years after M&A deal conduction. Liu, Chen, and Pai (2007) showed the same negative results focusing on M&As by telecommunications firms in Taiwan, supporting the low efficiency hypothesis.

Though studies mentioned above have offered some empirical evidence for the wealth effect of M&As in the telecommunications industry, there are few studies that take both short-term and long-term performance of M&As by telecommunications carriers into consideration. To fill the literature gap, this study includes not only the short-term but also the long-term wealth effect into the scope of research. Considering the incentives provided by the Telecommunications Act of 1996 during the period 1996–2005, it is hypothesized that M&As in the U.S. telecommunications market will have a positive impact on the bidding company's stock returns. On the other hand, based on the mainly negative results drawn by studies regarding the long-term performance of M&As in the telecommunications industry, it is hypothesized that M&As by telecommunications carriers will have a negative impact on bidding firms' wealth effects in the long run.

Hypothesis 1a. M&As in the U.S. telecommunications market will have a positive impact on the bidding company's short-term stock returns.

Hypothesis 1b. M&As in the U.S. telecommunications market will have a negative impact on the bidding company's long-term wealth effect.

2.2. Factors affecting wealth creation of M&As

Wealth creation of M&As can be affected by several firm-specific and deal-specific factors. This study explores how the strategic types of M&As, bidder characteristics, and payment methods influence the wealth creation of M&As in the telecom industry.

M&As can be classified into three types (regarding the production stages of an industry): horizontal, vertical, and conglomerate (Chon, Choi, Barnett, Danowski, & Joo, 2003). To draw more insights particularly for the telecom industry, this study adds the convergence-type of M&A (further categorized into three types: FMC, TBC, and HIC M&A) to the scheme of strategic types, since the convergence-type of M&A is an emerging trend in the telecommunications industry and takes up a meaningful portion of the total M&As among U.S. telecommunications firms. To sum up, here we apply a telecom-specific categorization scheme with six strategic types of M&As (i.e., horizontal, vertical, FMC, TBC, HIC, and conglomerate2) and investigate how they influence the wealth creation of M&As by U.S. telecom carriers. Thus, we hypothesize that the wealth effect of takeovers in the U.S. telecommunications market will be

2 Note that this study defines horizontal M&As as the integration between same industries (e.g., a mobile carrier’s acquisition of another mobile carrier). Vertical M&As are defined as the integration across the value chain entities and are closely related to core businesses (e.g., a telco’s acquisition of a software provider, portal, and device makers).
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