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Large shareholders and value creation through corporate acquisitions in Europe. The identity of the controlling shareholder matters

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ABSTRACT

We investigate whether and how major shareholders influence M&A wealth effects for listed acquirers in Europe. To that end, we examine 342 intra-European takeovers of listed target firms announced between 1997 and 2007. We find that family-controlled acquiring firms *on average* engage in deals with substantially larger value creation, particularly in Continental Europe. However, this positive family effect disappears in industry-diversifying acquisitions, consistent with the idea that those family-controlled firms may also pursue corporate diversification through M&As in order to diversify the family wealth. Moreover, family owners across Europe cannot curb low-value acquisitions driven by managerial overconfidence. We relate this finding to the strong connections of family owners with management in family-controlled firms. Next, large institutional shareholders all over Europe are associated with the lowest-value deals, but they are able to limit the negative effects of managerial overconfidence. As to the division of M&A gains, we find that regardless of their identity, large acquirer shareholders tend to put their firm in a weaker negotiation position. Lastly, we find no robust support for the idea that major owners are less likely to pursue private benefits through M&As in countries with stronger investor protection.

Introduction

As of the mid-1990s, the merger and acquisition (M&A) market has become more internationally oriented, with a growing stake of European takeovers in the total number and total deal value of worldwide M&As (e.g., Huyghebaert & Luypaert, 2010; Martynova & Renneboog, 2011; Moeller & Schlingemann, 2004). Despite this increased weight of Europe, research on the value creation in European acquisitions remains limited to date. A number of studies have shown that stock market investors in European acquiring firms on average react positively to the announcement of a takeover, even when the takeover target is a publicly listed firm (e.g., Craninckx & Huyghebaert, 2011; Martynova & Renneboog, 2011). In this article, we posit that those positive M&A announcement effects could be related to the concentrated ownership structure that publicly traded companies in Europe tend to have (Faccio & Lang, 2002; La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 1999). We therefore wish to examine whether and how large acquirer shareholders influence M&A wealth effects in takeovers by listed acquirers in Europe.

The central argument in our study is that major owners in European acquiring firms may provoke a larger focus on firm-value maximization, given their wealth at stake. As a result, acquiring firms with a large shareholder may initiate deals with a bigger synergy potential, which can be captured by the deal's *total M&A gains*. Besides, large owners may restrain the firm's management from paying a (too) large premium in order to acquire target control. As the fraction of total M&A gains obtained by acquirer shareholders clearly captures a different, but complementary aspect of M&A wealth effects, we additionally examine the deal's *relative M&A gains*. Arguably, acquirer shareholders can gain (more) from a takeover when two conditions are satisfied: first, the deal creates value (captured by *total M&A gains*), and second, the acquiring company does not bid (too) aggressively for target control (captured by the acquirer's *relative M&A gains*). Besides, through a better monitoring and disciplining of firm management (Burkart, Gromb, & Panunzi, 1997; Shleifer & Vishny, 1986; Thomsen & Pedersen, 2000), large shareholders may impede managers from engaging in takeovers that do not add value for acquirer shareholders. Some studies have tried to test these ideas in a U.S. context. Gaspar, Massa, and Matos (2005) and Chen, Harford, and Kai (2007) provided evidence that long-term and independent institutional blockholders can effectively prevent the management of U.S. acquiring firms from initiating value-destroying acquisitions. Martin (1996) showed that higher institutional blockholdings also decrease the probability of using

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stock to pay for takeovers. Overall, the empirical evidence based on U.S. data thus suggests that large shareholders can influence M&A outcomes through an efficient monitoring and disciplining of firm management.

For Europe, no study to date has yet addressed the questions as to *whether* and *how* large acquirer shareholders influence M&A wealth effects. The evidence based on U.S. data does not necessarily allow us to conclude much about the impact of dominant owners in European listed firms, though. We provide two notable reasons as to *why* the impact of large acquirer shareholders in Europe could be different from what we know from existing U.S.-based research. Those reasons also motivate our research design. First, the most prevalent type of concentrated ownership in European listed firms is family control (Faccio & Lang, 2002; La Porta et al., 1999), while the existing U.S. evidence primarily emphasizes the beneficial effects of large institutional investors. Evidence from U.S. data as to whether and how large family owners affect M&A outcomes is limited and inconclusive. On the one hand, a number of studies have shown that family-controlled firms perform better and are less diversified than other firms (Anderson & Reeb, 2003; Villalonga & Amit, 2006). However, in the context of acquisitions, Miller, Breton-Miller, and Lester (2010) pointed out that family firms initiate less deals and may use acquisitions to achieve corporate diversification, because family owners want to reduce firm risk and retain control of their firm for offspring. Such a strategy is not necessarily in the best interests of the firm and its minority investors, which could negatively impact the bidder's stock market value at the deal announcement date. If anything, these studies reveal that family owners are different from institutional owners. Moreover, family owners usually have a disproportionately large fraction of the family wealth invested in the firm, which provides them with appropriate incentives to discipline and monitor firm management. Nonetheless, and unlike institutional owners, family owners also tend to put family members in the management or in the board of their firm (Miller et al., 2010; Villalonga & Amit, 2009). Those control-preserving mechanisms of family owners might actually limit their ability to perform an independent monitoring role vis-à-vis firm management. To examine the impact of acquirer ownership structure on M&A wealth effects in Europe, we therefore explicitly distinguish between large family owners and major institutional investors.

Second, while stock market investors in the United States generally enjoy a strong legal protection of their rights, shareholder rights in Continental Europe are far less secured (Dyck & Zingales, 2004; La Porta et al., 1999). La Porta et al. (1999) showed that the protection of investor rights is even below the worldwide median in 11 of the 15 initial EU member states. In such an institutional context, large shareholders could easily use their stake in the firm to pursue private benefits of control, to the detriment of the firm's minority investors. We already pointed out that family-controlled firms may rely on acquisitions to realize a diversification of the family wealth. Along the same line, large institutional investors could abuse their power by consenting to non-value-maximizing acquisitions that allow them to attain other types of control rents. Hence, we also examine whether the M&A wealth effects of dominant owners are different in countries with weak versus stronger investor protection. Thereby, our study adds to the growing literature on principal–principal conflicts of interest in listed firms, whereas prior U.S.-based research has primarily focused on the principal–agent conflict of interest between acquirer shareholders and firm management. To the best of our knowledge, Holmen and Knopf (2004) is the only study that has analyzed this conflict in a European M&A context. Yet, they find no evidence that large shareholders with voting rights in bidders and targets of Swedish mergers expropriate minority investors through tunneling or corporate diversification.

Our results for a sample of 342 intra-European takeovers of listed target firms announced between January 1, 1997 and December 31, 2007 show that acquirer shareholders on average realize a small, positive abnormal return of 0.35% in the [−35,+1] event window surrounding deal announcement. The combined value effect to acquirer and target shareholders is a significant 2.52%. What is more, M&A wealth effects are affected by the ownership structure of the acquiring company. Family-controlled firms complete acquisitions with positive total gains of 4.75% on average, which is significantly larger than the combined M&A gains realized by widely held acquirers (2.34%) or by acquirers controlled by an institutional investor (−1.78%). Next, we show that total M&A gains are not split equally among acquirer and target shareholders, but we find no compelling evidence that the division of M&A gains is significantly affected by the identity of the acquirer's largest shareholder.

Our multivariate regression results confirm the positive impact of family control at the acquirer level on total M&A gains. This finding thus indicates that financial markets perceive the potential for synergies to be larger in acquisitions initiated by family-controlled firms, which could be explained by those firms' more long-term oriented and conservative investment strategies (e.g., Anderson & Reeb, 2003; Donckels & Fröhlich, 1991). Nevertheless, the results also reveal that family control can come at a cost: the positive family effect on total M&A gains disappears entirely once family firms adopt an industry-diversifying takeover strategy, implying that this diversification does not create any value for the firm's minority investors. We demonstrate that the results discussed earlier arise mainly for acquirers operating in Continental Europe, characterized by a weaker protection of investor rights. We further show that family owners across Europe do not curb the low-value acquisitions driven by managerial overconfidence, which can be related to the strong intrinsic bond of family owners with firm management in those firms. Next, we report a consistent negative association between large institutional shareholders at the acquirer level and total M&A gains. Extra analyses reveal that the latter outcome could be driven in part by institutional cross-holdings of target equity. Also, potentially up to 74% of large institutional blockholders in our dataset could be considered as 'grey', based upon the classification by Chen et al. (2007). Those investors may then consent to lower-value deals if doing so is beneficial for their current and future business relations (Chen et al., 2007; Duggal & Millar, 1999). Somewhat unexpectedly, we do not find that this negative institutional blockholder effect is weaker when acquirers operate in an environment with stronger protection of investors rights. On a more positive side, our results reveal that large institutional owners are able to alleviate the negative impact of managerial overconfidence on M&A wealth effects. Finally, we show that large family owners as well as large institutional owners tend to put their firm in a weaker negotiation position when it comes to dividing M&A value creation, as the fraction of total M&A gains realized by acquirer shareholders is significantly smaller for acquirers with such a dominant owner, ceteris paribus.

As the earlier results arise after including various proxies for acquirer size, managerial agency problems, managerial herding, or market-timing behavior, we conclude that those alternative rationales cannot explain our findings. Likewise, as our results are robust to including additional firm-level and country-level indicators of corporate governance, we conclude that they cannot be driven by alternative governance arguments either. Overall, our study thus points out that M&A wealth effects in intra-European acquisitions are hugely affected by the presence of a large acquirer shareholder, while its exact impact on total M&A gains depends upon whether this dominant owner is a family owner or a major institutional investor. Moreover, the external corporate governance regime proves far less effective in protecting minority investors than is typically assumed in the literature.