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Monika Tarsalewska

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Buyouts under the threat of preemption

Monika Tarsalewska*

University of Exeter Business School

Rennes Drive, Exeter EX4 4ST, United Kingdom

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Abstract

This paper analyses the effects of preemption fears on the buyout efficiency when firms combine non-synergistic operational activities and have asymmetric access to financing. Bidders with preemption fears are more likely to acquire target firms at an earlier development stage. However, if uncertainty is high, an acquirer may opt to wait and buy the target firm at a later stage as assets in place. The fear of preemption affects the efficient exercise of each offer differently. While the timing of a hostile takeover under threat of preemption converges to an efficient global optimiser threshold, negotiated mergers are exercised inefficiently too early. Premiums to the target firm are higher when the firm is acquired at an earlier stage, and when the bidder fears being preempted.

Keywords: Buyouts, Real Options, Fear of Preemption

JEL Classification: G34, G13, G32

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