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The price of corporate acquisition: determinants of cash takeover premia

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Abstract

A sample of cash-only acquisitions of Nasdaq targets during 1973–1999 is examined. It is found ... %) during the 197... ...e value reductio... ...rally will not pay high... ...d that over-invested ... ...nia while under... ...at agency rathe... ...a.

Notes

It might be that acquirers sell securities in the capital market in an effort to raise a ‘war chest’ that they would use in the future to make acquisitions. But in such cases, the capital and equity issuance effects would be captured immediately at the time of the new security issuance. They would not impact the determination of the premium to be paid for the acquisition.

The size of premia paid in a merger based on the free cash flow and market-to-book characteristics of the target is also examined. The impact that the target's level of over or under investment might have on the price that acquirers are willing to pay is examined. It is found that acquirers are more aggressive in their bidding for targets that are over-invested rather than under-invested. This suggests that acquirers are more interested in the cash flow of a target than its internal investment opportunities. The difference in the mean (median) premium paid for over-invested relative to under-invested targets is statistically significant at the 10% level.