

# Equity Ownership Choices in Acquisitions: On what matters: A Pitch

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## **1. Introduction**

One month ago (Sept/2014), my PhD supervisor encouraged me to consider submitting my work to present at the symposium, following the new “Pitching Research” framework developed by Professor Robert Faff, who will be chairing the symposium that to be held at La Trobe University. Consequently, I am writing this pitch letter to express my research topic based in the merger and acquisition discipline following the template developed by Faff (2014).

When I have taken a look at the “Pitching Research” by Faff (2014), I was very excited about what his paper has attempted to provide to research students/early career researchers. Indeed, for a PhD student, especially who are doing “three-essays thesis”, deciding on whether a potentially new research project is worth starting is very challenge. By following the template proposed by Faff (2014), I can easily outline my research proposal in a meaningful and relevant way. Particularly, the Cocktail Glass approach helps me definitely focus on the narrow literature, and then draft a basic research question of the project. Also, his “3-2-1” method enables me to imagine the framework of an academic proposal, from outlining the idea, data availability, and tools to undertake the project, to answering the key research questions, such as “how and why it is important”, thereby allowing the researcher to explain the basic contribution of the project to the theoretical and practical literature. Last, but not least, the use of “Mickey Mouse diagram” allows me to depict the novelty in my proposal.

The remainder of this letter is organized as follows. Section 2 gives a brief introduction on my pitch (Preliminaries). Section 3 outlines three core aspects of the empirical research project: Idea; Data; and Tools, while Section 4 responses to two questions – what’s new? and so what?. Contribution and other considerations are discussed in Section 5 and Section 6. Section 7 concludes.

## **2. Preliminaries**

The completed pitch is reported in Figure 2 and relates to the topic of mergers and acquisitions in which the working title is “Equity Ownership Choices in Acquisitions: On What Matters” (Item (A)). The title gives a key motivation for building a full framework of potential factors which impact on

equity ownership choices in acquisitions. The title is explained in the item (B) with the basic research question is “What explains the equity ownership decision in acquisitions?”. In terms of pitch item (C), there are two key papers: Ouimet (2013) and Liao (2014). These papers are published in the A-star-ranked journals, one in the Review of Financial Studies (Top 4 finance journals) and one in the Journal of Corporate Finance. As such, the notion of quality “foundational” papers is satisfied. On the basis of conditions that serve as heuristics for “currency” and quality proposed by Faff (2014), the notion of key “foundational” papers is satisfied. In terms of pitch item (D), the motivation is expressed as follows:

There is scarce empirical evidence on the benefits of targeting different levels of ownership resulting from takeovers, and no prior study is found focusing on the emerging markets. The study of Ouimet (2013) has focused predominantly on examining the trade-offs between minority (if less than 50% is acquired) and majority acquisitions (greater than 50%) in the U.S market, and found that minority acquisitions are primarily motivated by the benefits of target managerial incentives, relieving financial constraints at the target firm, and providing an opportunity for the acquirer to gather more information before taking a majority stake. Full-control acquisitions, on the other hand, are driven by the ability to achieve acquisition synergies and benefits accruing to the acquiring firm’s management. In a related aspect, Liao (2014) examines various theories explain motivations for minority block acquisitions (the acquirer purchases more than 5% and less than 50% of the target’s shares) using a global dataset, and finds evidence that is consistent with the financing motives. Accordingly, financially constrained firms are more likely to be targets of block acquisitions and experience larger announcement returns compared to non-constrained firms. Also, target firms are more likely to be in industries with high research and development (R&D) expenses. The key motivation for this project is that, while some prior research in the finance literature has attempted to explain motivations for minority and majority ownership, our knowledge of why and how acquirers decide among different levels of ownership is still limited. In other words, little is known about the trade-offs among minority, majority, and full acquisitions. We do not know what the drivers are for bidders to seek, say full-control (100% is acquired) ownership, over minority and majority ownership in the target firms, and it is unclear why acquirers choose a specified type of equity ownership over others. Also, the literature still has not shown what the determinants of shareholder value creation outcomes associated with these acquisition types and whether or not there is shareholder value creation for both acquirers and targets in relation to these takeover outcomes.

### **3. IDioT**

Based on the “IDioTs” guide, I outline three core aspects of the empirical research project. First, in terms of research idea (Item (E)), this project extends and adds to the existing literature by reexamining the potential impact of motivations regarding management incentives, cost-related

benefits, and corporate governance on the equity ownership decisions in takeovers, thereby building a full framework of potential factors influencing equity ownership choices in acquisitions across emerging markets.

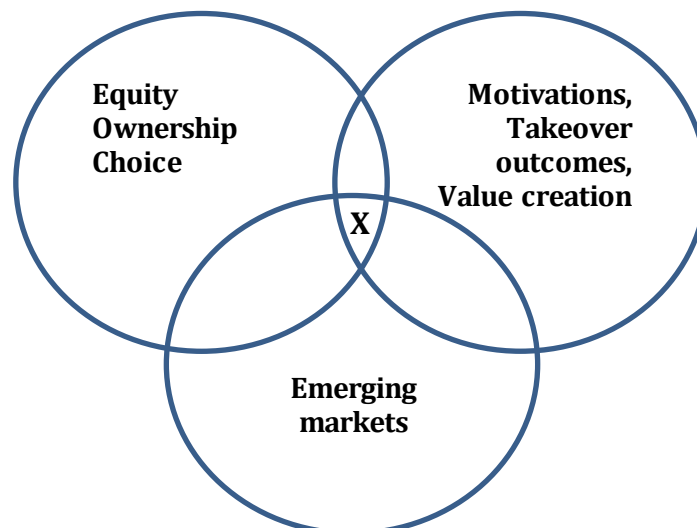
Based on the idea, I then introduce sample, data sources and sample selection. Item (F) of the completed pitch template address many dimensions of the data. (1) identifies the emerging markets as the chosen setting; individual firms as the unit of cross-sectional analysis; sampling interval: daily (stock price performance around the takeover announcement) and annual (using accounting results). Type of data, on the other hand, includes the events (takeover announcements), firm-level characteristics, and country-level characteristics. (2) suggests a cross-sectional dataset in the sample data design with a sample period of 2000-2013 that saw substantial growth in acquisition activities across emerging markets. (3) In terms of data sources, deal-related data comes from the Thomson Reuters SDC database. Also, collecting target firm-level data located in emerging countries is a bit difficult, thereby this project employs a combination of sources: Thomson Reuters Worldscope, Mint Global (the Bureau Van Dijk), Datastream, FactSet Ownership, and the World Bank database. (4) The data collection is mostly automatic.

Item (G) of the completed pitch template comments on the anticipated tools. In order to solve the research questions, the paper employs three econometric methods, namely multinomial logistic regression, event study analysis, and cross-sectional multivariate regression. In terms of econometric software, Stata is identified.

#### **4. What's new? So what?**

Item (H) in the completed pitch states that the idea is novel by examining existing hypotheses to explain what motives behind the bidders' ownership decision and shareholder value creation following a specified ownership choice. The pitch also shows that the data and tools are standard. As mentioned by Faff (2014), the idea can be claimed to be the "driver", while data/tools are strong passengers. I also employed a "Mickey Mouse" approach (Figure 1) as proposed by Faff (2014) as a meaningful way to identify novelty in my research and to represent something new to the relevant literature.

**Figure 1: Mickey Mouse Applied to my Pitch**



Item (I) in the completed pitch assumes that the project has posed a novel research question, and then what a researcher needs to respond why is it important to know the answer? And how will major decisions/behaviour/activity be influenced by the outcome of this research. Deciding on an appropriate ownership level is important. Indeed, a correctly planned ownership level can result in significant economic benefits through post-acquisition integration and asset synergy. An incorrect ownership level may lead to a mismatch between resource commitment and risk, inefficient integration of the target firm, and less-than-desired rent appropriation. By examining various potential factors, this project is expected to outline what matters equity ownership decision in acquisitions across emerging markets. Managers of bidders and target firms should be aware of how the management incentives, cost-related benefits, and corporate governance attributes influence ownership decisions and the announcement period gains.

### **5. Contribution**

An assessment of the contribution of the proposal/paper (Item (J)) is one of the central parts of the review process. A quality proposal/paper should contribute to the existing substantive and methodological understandings of the area, and try to generalise beyond the specific research study being reported through helping to develop, or to test, the theoretical/conceptual framework put forward. It should also have a strong contribution to policy or practice. This project employs a full, majority, and minority ownership trichotomy which can yield an enhanced understanding of motivations for equity ownership decisions, takeover outcomes, and the value creation resulting from selecting these post-acquisition ownership levels. Another contribution is that I focus on emerging-based takeovers. Compared to the U.S and European markets, however, there has been far less research conducted; hence we know very little about equity ownership choices in takeovers across emerging markets. The scarcity of studies on the emerging markets demands more academic research on the topic.

### **6. Other considerations?**

The final item in the completed pitch template is Item (K), looking for any relevant suggestions offered in the template. Regarding the question of whether collaboration is needed/desirable?, the answer is yes, meaning that this project needs some research assistants to collect, organize, and analyze data. In terms of planned conference/symposium, I expect to submit the proposal for presentation at an internal seminar and at doctoral symposiums (say the 2015 FMCGC) to receive external feedback. The final entries in item (K) relate to the "risk assessment" exercise. (i) "insignificant result" risk can be low – equity ownership choices in acquisitions are expected to be related to certain motivations; (ii) "competitor" risk is medium/high as the ownership choice-related research is relevant in the current theoretical and practical literature; and (iii) risk of "obsolescence" is low – since the ownership decision plays a very important role for managers of

acquiring firms, target firms, and investing communities. There is also another potential challenge relating to data availability for emerging market-based firms.

## 7. Conclusion

This letter outlines my basic pitch for a proposed research project on equity ownership choices in acquisitions across emerging markets. By following the template proposed by Faff (2014), I can outline my research proposal in an expressive manner. Indeed, the most important thing that I realized after writing up the pitch paper is how useful and important it is to organize my ideas, though it is not easy for me to combine all of understanding and research idea in an easy-to-read style. As a result, I highly hope to receive feedback regarding the quality of research proposal and structure of pitch paper.

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**Figure 2: Pitching a New Research Topic - “3-2-1” Pitching Template - Completed Pitch on “Mergers and Acquisitions in Emerging markets” Topic**

Pitcher's Name	MAN DANG	Date Completed	17/10/2014
(A) Working Title	“Equity ownership choices in acquisitions: On what matters”		
(B) Basic Research Question	What explains the equity ownership decision in acquisitions?		
(C) Key papers	<p>- Ouimet, P. 2013. What Motivates Minority Acquisitions? The Trade-Offs between a Partial Equity Stake and Complete Integration. <i>The Review of Financial Studies</i> 26: 1021-47.</p> <p>- Liao, R.C. 2014. What drives corporate minority acquisitions around the world? The case for financial constraints. <i>Journal of Corporate Finance</i>, 26: 78-95.</p>		
(D) Motivation/Puzzle	<p>Prior studies in the finance literature have attempted to explain motivations for minority (if less than 50% is acquired) and majority (more than 50% is acquired) acquisitions in terms of management incentives, financial constraints, and agency-related motivations. Nevertheless, our knowledge of why and how acquirers decide across the different levels of ownership is still limited. Little is known about the trade-offs among minority, majority, and full ownership acquisitions. We do not know what the drivers for bidders to seek, say full-control (100% is acquired), over minority and majority ownership; and it is unclear what determines ownership outcomes in takeovers. Also, the literature still has not shown what the determinants of shareholder value creation outcomes are, and whether or not there is shareholder value creation for both acquirers and targets in association with these takeover outcomes. Additional motivation relates to the emerging markets perspective. This means that these markets could be financing options and availability, which may increasingly impact on the ability to undertake full acquisitions compared to other types of acquisitions.</p>		
<b>THREE</b>			
(E) Idea?	<p>This study extends and adds to the existing literature by reexamining the potential impact of motivations regarding management incentives, lower cost-related benefits, and corporate governance on the equity ownership decisions in takeovers after controlling for other firm-level and transaction-related characteristics. Particularly, I hypothesize some correlations that are identified in prior studies:</p> <ul style="list-style-type: none"> <li>- Whether or not bidders select full-control acquisitions due to benefits regarding expected large efficiency gains [Maksimovic and Phillips (2001); Ouimet (2013)], agency-motivated acquisitions [Lang et al. (1991); Ouimet (2013)], increased market power [Fee and Thomas (2004); Shahrur (2005)].</li> <li>- Whether or not bidders select partial acquisitions (minority or majority ownership) due to benefits in terms of unchanged incentives in control [Allen and Phillips (2000); Fee et al. (2006)], increased monitoring and discipline [Akhigbe et al. (2007); Mantecon et al. (2012)], target financing needs and financial constraints [Fee et al. (2006), Liao (2014)], uncertain gains from a full takeover [Higgins (2006)], inefficient internal capital markets from a full takeover [Rajan et al. (2000)], risk sharing, reduction of opportunistic behaviors, and fostering of knowledge exchange among partners [McConnell and Nantell (1985); Johnson and Houston (2000); Oxley and Wada (2009)].</li> <li>- What are the determinants of shareholder value creation and whether or not there is shareholder value creation for both acquirers and targets in relation to these takeover outcomes?</li> </ul>		
(F) Data?	<p>(1). <b>Setting:</b> Emerging markets (no prior study is significantly found regarding the equity ownership choices in takeovers across emerging markets); <b>Unit of analysis:</b> firms; <b>Sampling Interval:</b> Daily (stock price performance around the takeover announcement), Annual (Accounting results); <b>Type of data/sample size:</b> Events (takeover announcements), Firm-level characteristics, and Country-level characteristics.</p> <p>(2). <b>Sample data design:</b> Cross-sectional dataset; <b>Sample period:</b> 2000-2013.</p> <p>(3). <b>Data source:</b> Thomson Reuters SDC (deals). Also, collecting target firm-level data located in emerging countries is difficult, thereby this project employs a combination of sources: Thomson Reuters Worldscope, Mint Global (the Bureau Van Dijk), Datastream, FactSet Ownership, and the World Bank database.</p> <p>(4). <b>Data collection:</b> mostly automatic.</p>		
(G) Tools?	<p>- <b>Econometric methods:</b> Multinomial logistic regression, Event study analysis, and Cross-sectional multivariate regression.</p> <p>- <b>Software:</b> Stata.</p>		
<b>TWO</b>			
(H) What's New?	The idea is novel by examining existing hypotheses to explain what motives are behind the bidders' ownership decision and the shareholder value		

	creation following a specified ownership choice. The idea can be claimed to be the “driver”, while data/tools are “strong” passengers. “Mickey Mouse” approach is employed to identify novelty in my research and to represent something new to the relevant literature.
(I) So What?	Deciding on an appropriate ownership level is important. Indeed, a correctly planned ownership level can result in significant economic benefits through post-acquisition integration and asset synergy. An incorrect ownership level may lead to a mismatch between resource commitment and risk, inefficient integration of the target firm, and less-than-desired rent expropriation. This project is expected to outline a full framework of potential factors influencing equity ownership decision in acquisitions across emerging markets. Managers of bidders and target firms should be aware of how the management incentives, lower cost-related benefits, and corporate governance influence ownership decisions and the announcement period gains.
<b>ONE</b>	
(J) Contribution?	<ul style="list-style-type: none"> <li>- This project employs a full, majority, and minority ownership trichotomy which can yield an enhanced understanding of motivations for equity ownership decisions, takeover outcomes, and the value creation resulting from selecting these ownership levels. Particularly, the choice between full, majority, and minority ownership will be explained by focusing deeply on benefits regarding management incentives, cost-related benefits, and corporate governance after controlling for other firm-level and transaction characteristics.</li> <li>- Another contribution is that the project focuses on emerging market-based takeovers. Compared to the U.S and European markets, however, there has been far less research conducted; hence we know very little about equity ownership choices in takeovers across emerging markets. The scarcity of studies on the emerging market demands more academic research on the topic.</li> </ul>
(K) Other Considerations	<ul style="list-style-type: none"> <li>- <b>Conference/Symposium:</b> submit the proposal for presentation at doctoral symposiums (say the 2015 FMCGC) to receive external feedback.</li> <li>- <b>Collaboration:</b> need some research assistants to collect, organize, and analyze data.</li> <li>- <b>Risk assessment:</b> <ul style="list-style-type: none"> <li>(i) “insignificant result” risk: low – equity ownership choices in acquisitions are expected to be related to certain motivations.</li> <li>(ii) “competitor” risk: medium/high as the ownership choice-related research is relevant in the current theoretical and practical literature.</li> <li>(iii) risk of “obsolescence”: low since the ownership decision plays a very important role for managers of acquiring firms, target firms, and investing communities.</li> </ul> </li> <li>- <b>Other potential challenges:</b> data availability for emerging market -based firms.</li> </ul>