NBER WORKING PAPER SERIES

CHARACTERISTICS OF HOSTILE AND FRIENDLY TAKEOVER TARGETS

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Working Paper No. 2295

NATIONAL BUREAU OF ECONOMIC RESEARCH
1050 Massachusetts Avenue
Cambridge, MA 02138
June 1987

Support from the Seaver Institute is gratefully acknowledged. We thank Oliver Hart, Michael Jensen, Kevin M. Murphy, Edward Rice, and Lawrence Summers for helpful comments and the National Bureau of Economic Research for financial support. The research reported here is part of the NBER's research program in Financial Markets and Monetary Economics. Any opinions expressed are those of the authors and not those of the National Bureau of Economic Research.

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ABSTRACT

Compared to an average Fortune 500 firm, a target of a hostile takeover is smaller, older, has a lower Tobin's Q, invests less of its income, and is growing more slowly. The low Q seems to be an industry-specific rather than a firm-specific effect. In addition, a hostile target is less likely to be run by a member of the founding family, and has lower officer ownership, than the average firm. In contrast, a target of a friendly acquisitions is smaller and younger than an average Fortune 500 firm, and has comparable Tobin's Qs and most other financial characteristics. Friendly targets are more likely to be run by a member of the founding family, and have higher officer ownership, than the average firm. The decision of a CEO with a large stake and/or with a relationship to a founder to retire often precipitates a friendly acquisition.

These results suggest that the motive for a takeover often determines its mood. Thus disciplinary takeovers are more often hostile, and synergistic ones are more often friendly.

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Economic analysis has identified two broad classes of takeovers. The first is what we call disciplinary takeovers, the purpose of which seems to be to correct non-value-maximizing (NVM) practices of managers of the target firms. Such practices might include excessive growth and diversification, lavish consumption of perquisites, overpayment to employees and suppliers, or debt-avoidance to secure a quiet life. Disciplinary takeovers thus address the problem of what Williamson (1965) has called discretionary behavior by managers, and Jensen (1986) has christened "free cash flows." Because disciplinary takeovers are designed to replace or change the policies of managers who do not maximize shareholder value, the actual merger of the two firms is not really essential. The takeover is only the most effective way to change control and with it the target's operating strategy.

The second class of takeovers can be loosely called synergistic, since the motivating force behind them is the possibility of benefits from combining the businesses of two firms. Synergy gains can come from increases in market power, from offsetting profits of one firm with tax loss carryforwards of the other, from combining R & D labs or marketing networks, or from simply eliminating functions that are common to the two firms. The combination of the two businesses is thus essential for realizing the gains in synergistic takeovers.

It is important to note from the start that the gains in synergistic takeovers could well be gains for the managers as much as for shareholders. For example, when managers launch diversification programs, they may be creating no value for shareholders, but only satisfying their own preferences for growth. The point nonetheless remains that the acquiror is seeking a combination of the operations or cash flows of the two firms and not an improvement of the target. This would not be the case in disciplinary takeovers.

This paper attempts to verify the conjecture that disciplinary takeovers are more often hostile, and synergistic takeovers are more often friendly. We assemble evidence showing that targets of hostile and friendly bids have ownership and asset characteristics that one would expect of the targets of disciplinary and synergistic takeovers, respectively. We interpret this evidence as showing that, at least to some extent, the motive for a takeover determines its mood.

The claim that hostility and friendliness typically reflect two different takeover motives is by no means clearcut. Some diversification-motivated takeovers undoubtedly run into resistance from managers of target firms, who are unhappy either with expected changes in operations or with the compensation they get for giving up control. Similarly, some takeovers launched in order to change the target's operating strategy proceed with the consent of target managers who obtain lucrative enough rewards to give up control peacefully, or else simply want to retire. These grey areas suggest the possibility that the variation in the monetary incentives of managers across target firms can completely account for mood differences from acquisition to acquisition. Walkling and Long (1984) appear to take this view. In contrast, we show that there are numerous characteristics, in addition to measures of financial incentives of their managers, that differ across hostile and friendly targets. Moreover, these are the differences one would expect to find between targets of disciplinary and of synergistic takeovers.

The analysis of this paper is based on the sample of all publicly traded Fortune 500 firms as of 1980. Of the 454 firms in the sample, 82 have been acquired by third parties or went through a management buyout (MBO) in the period 1981-1985. Based on an examination of the Wall Street Journal Index, 40 of those appear to have started hostile and 42 friendly. We call an acquisition hostile if the initial bid for the target (which need not be a bid from the eventual acquiror) was neither negotiated with its board prior to being made nor accepted by the board as made. Thus initial rejection by the target's board is taken as evidence of the bidder's hostility, as is active management resistance to the bid, escape to a white knight, or a management buyout in response to unsolicited pressure. We sort acquisitions on the basis of the initial mood because we are interested in the source of the takeover gains that sparked the bidding in the first place. Targets that are not classified as hostile are called friendly.

The remaining sections of the paper examine ownership and financial characteristics of our Fortune 500 sample. Section 2 focuses on the ownership characteristics of friendly and hostile targets. Friendly targets appear to have much higher board ownership than either hostile targets or the rest of the sample, and in particular much higher ownership by the top officers. Compared to an average firm in the sample, a friendly target is much more likely, and a hostile target much less likely, to be run by a founder or a member of the founder's family. Furthermore, the probability of an acquisition, and particularly of a friendly acquisition, rises with management ownership. In fact, intentional exit of the founding family or of a CEO with a very large stake is a frequent impetus for a friendly acquisition in our sample. Although the results on ownership identify some clear differences between hostile and friendly targets, they do not suggest a clear link between the motive for a takeover and its mood.

Section 3 examines the asset and performance characteristics of the sample. The results suggest that targets of friendly acquisitions have comparable Tobin's Qs to those of non-targets, but that hostile targets have lower Qs. Hostile targets not only have low Qs within their industries but are concentrated in low Q industries. Friendly targets are younger and faster growing than hostile targets and are basically indistinguishable from the sample as a whole in terms of performance variables.

These results are the basic evidence consistent with our conjecture that synergistic takeovers are more likely to be friendly and disciplinary takeovers are more likely to be hostile. Hostile targets appear to be poorly performing firms, as we would expect of candidates for disciplinary takeovers. In contrast, it seems less likely that match-specific attractions of synergistic targets would be easily captured by basic performance measures.

Section 4 presents probits of the effects of firm characteristics on the probability of its hostile or friendly acquisition. The results confirm that a firm with a low market value relative to the amount of fixed assets it holds is more likely to become a hostile target than the average firm. This appears to be accounted for by an industry effect, and not by a particularly low valuation within an industry. Controlling for size, top officer ownership and Q, we find that the presence of the founding family reduces the likelihood of hostile bids, but does not raise that of friendly bids. Large management stakes, on the other hand, do more to encourage friendly acquisitions than to discourage hostile ones.

Section 5 takes a separate look at management buyouts. These deala deserve special attention becauae they cannot be motivated by synergistic gains. We define hostile MBOs as deals done in response to a third party bid or 13-D filing with an expression of intent to seek control. Friendly MBOs then are transactions in which such pressure is not apparent. Because our sample of MBOs is quite small, accurate statistical inference is impossible and all we do is eyeball the data. Except for the fact that leveraged buyouts are, on average, much smaller transactions, differences between friendly and hostile MBOs largely mimic the differences between friendly and hostile acquisitions more generally. The external pressure that prompts defensive MBOs seems likely to be an attempt to discipline the management. Friendly MBOs, however, seem more likely to be done for tax reasons or possibly to buy undervalued shares.

We interpret this study as furnishing some evidence consistent with the view that hostile and friendly targets are very different types of companies. While targets of friendly bids appear to be a wide range of firms in many industries, hostile targets are usually older, slowly growing firms that are valued much below the replacement cost of their tangible assets. Friendly acquisitions could be motivated by corporate diversification, synergies, and, as our results suggest, life cycle decisions of a founder or a manager with a dominant stake. Bidders in hostile transactions may be more interested in shutting down, selling off, or redepreciating the physical capital of the target, than they are in continuing business as usual. In addition to possible heterogeneity of financial incentives, resistance to takeovers may be related to the unwillingness of target management to accept the particular changes sought by the bidder, and often lead it to seek a white knight or an

MBO. In short, the evidence is consistent with our notion that the source of gains from a takeover can determine its mood.

2. Ownership Structure and Acquisitions.

In this Section, we present ownership characteristics of 1980 Fortune 500 firms that were acquired in the subsequent five years. Recent empirical research (Demsetz and Lehn, 1985, Morck, Shleifer and Vishny, 1986) has documented the incidence of substantial managerial ownership of large industrial corporations. These studies have not, however, focused on the ownership structure of acquisition targets, which is the task of this section. Evidence on ownership enables us to see whether managers of non-targets, hostile targets, and friendly targets have different financial interests in an acquisition.

The relationship between management ownership and the takeover mood has been previously examined by Walkling and Long (1984), who found managers' personal wealth changes from a successful acquisition to be negatively related to the decision to resist. In our analysis, we also consider the impact of management ownership on the probability of an acquisition, be it hostile or friendly, as well as the influence of the presence of a founding family and of the chairman of the board's age on the probability of either a hostile or a friendly acquisition. In this way, we hope to obtain a more complete picture of the function of managers' financial incentives in takeovers.

Throughout this analysis, we try to avoid sample selection problems and to this end begin with all publicly traded 1980 Fortune 500 firms (Walkling and Long might have had some sample selection problems since they report implausibly high initial stakes of acquirors -- 11 and 27 percent for contested and uncontested offers, respectively). Also, since we are interested in differences between firms, we try to get away from cyclical variation and compare all firms as of 1980. In the case of ownership, data come from the 1980 Corporate Data Exchange directory, which contains data on ownership positions of board members as well as large outside shareholders. We do not have data on executive compensation, or on the ownership positions taking the form of options; many studies (e.g., Murphy, 1985) indicate that executive wealth changes from stock ownership are large relative to those from other sources.

The first measure of ownership we use is the combined percentage stake of the board of directors. Because of the nature of CDE reporting, the stakes are added up over only those board members whose positions exceed .2%. This may lead to some problems for the largest firms, where even the tiniest percentage ownership positions are worth millions of dollars.

To the extent that the board makes the decision as to whether to resist an offer, the board's stake may be the appropriate measure of financial incentives. In addition to this measure, we divide the board ownership into that of the top two officers and that of the rest of the board. The first captures the interest of the top officers whose concern for the outcome of a bid might go well beyond their personal capital gain, and the second captures the interest of important decision-makers who might care little about the outcome of a bid except for their personal financial gain. These two measures complement the board's stake in that they reflect the pecuniary gain of the two constituencies on the board with possibly different attitudes to the acquisition.

Other personal characteristics of the management team might influence their attitude to being acquired independent of their ownership stake. First, top officers who are founders or members of the founding family might play a special role in the company, either because they command the loyalty of shareholders and employees, or because their attachment to the company is more than just financial. For this reason, it seemed useful to ask which fraction of friendly and hostile takeover targets were run by a member of the founding family. This is of particular interest in the context of executive succession, since sale of the company might be a natural means for a founder's retirement. For a similar reason, we are interested in the age of the chairman, since his retirement plans might influence his attitude toward the sale of his company.

Recall that an acquisition is called hostile if it was not negotiated prior to the initial bid, was not accepted by the board from the start, or was contested by the target management in any way. This category thus includes acquisitions by white knights. It also includes management buyouts that were precipitated by a bid or a 13-D filing expressing the intent to acquire control, since such pressure is clearly hostile (Shleifer and Vishny, 1986). Our calling a target hostile whenever there is any evidence of the board's rejection of the initial offer may misclassify as hostile some situations in which the board is only attempting to obtain a higher bid. Because there are only three transactions in our sample where resistance was limited simply to a rejection of the first offer, we proceed using this classification. Also, our classification records a transaction as friendly either if there is no evidence of resistance from the target management to the first prospective acquiror or if the management implemented an MBO and we have no evidence of a hostile threat. Again, the classification is far from perfect given that target management may have been coerced into going along in the face of imminent defeat.

Although Section 5 presents some evidence to the effect that it is appropriate to include hostile and friendly MBOs into the general samples of hostile and friendly transactions, we try to be cautious and present many of the results both including and excluding MBOs from the samples of targets. Unless specifically noted, our discussion will concern the results for the case where management buyouts are included.

Table 1A presents the means and medians of various ownership variables for different groups of companies, and Table 1B gives t-statistics for tests of the differences of means between these groups. In the whole sample, the board of directors owns on average 10.9% of the company; 6.3% is the average stake of the top two officers and 4.5% is the average stake of the rest of the board. Not surprisingly, ownership positions are skewed to the right: the medians for the above three measures are 3.54%, .61% and 1.09% respectively. One way to describe the magnitude of these stakes is that the average value of the top officers' position is $40.5 million and the median is $2.26 million. Almost a quarter of the companies in the sample are run by members of the founding families, and the average chairman of the board is a youthful 58 years old.

From the viewpoint of ownership, friendly targets are very different both from the sample and from hostile targets. Boards of friendly targets own over 20% of the company, on average, which is statistically significantly higher than either the 10.9% average board ownership in the sample, or the 8.3% average of hostile targets. Hostile targets have on average lower board

TABLE 1A: Characteristics of Top Management By Acquisition Type

		Sample	Friendly	Hostile	Friendly Non-MBO	Hostile Non-MBO
Founding Family Present on Top Management Team = 1	Mean	.244	.405	.100	.412	.0938
	Median	0	0	0	0	0
Fractional Equity Ownership By The Board of Directors	Mean	.109	.208	.0829	.186	.0874
	Median	.0354	.135	.0418	.0894	.0382
Fractional Equity Ownership By Top Two Officers	Mean	.0635	.145	.0318	.139	.0364
	Median	.0061	.0176	.0049	.0139	.0044
Fractional Equity Ownership By The Rest of the Board	Mean	.0455	.0625	.0512	.0464	.0510
	Median	.0109	.0172	.0233	.0152	.0227
Age of Chmn.	Mean	58.4	58.7	57.1	58.5	55.3
	Median	59	57	58	57	57.5
Dollar Value of Top Officers' Stake (in millions)	Mean	40.05	83.75	9.22	60.79	11.23
	Median	2.26	6.02	.795	4.22	1.11

TABLE 1B: T-Statistics for Tests of Equality of Means of Top Management Variables by Acquisition Type

	Friendly vs. Sample	Hostile vs. Sample	Friendly Non-MBO vs. Sample	Hostile Non-MBO vs. Sample	Friendly vs. Hostile	Friendly Non-MBO vs. Hostile Non-MBO
Founding Family Present on Top Management Team = 1	2.55	-2.23	2.37	-2.06	3.33	3.12
Fractional Equity Ownership By The Board of Directors	4.42	-1.11	3.03	-.811	3.28	2.26
Fractional Equity Ownership By Top Two Officers	4.20	-1.56	3.45	-1.18	3.33	2.55
Fractional Equity Ownership By The Rest of the Board	1.27	.415	.0611	.358	.559	-.23
Age of Chmn.	.217	-1.13	.0481	-2.28	.742	1.34
Dollar Value of Top Officers' Stake (in millions)	1.55	-1.25	.667	-1.04	2.03	1.60

ownership than the whole sample, although this difference is not statistically significant. The higher board ownership of friendly targets comes from higher ownership of the top officers. In fact, stakes of outside board members do not seem to be much different from either those in hostile targets or in the whole sample. At the 15% confidence level, hostile targets seem to have lower top officer ownership than does an average firm. The difference in officer positions is even more dramatic if one looks at dollar values of the stake, where the average for a friendly target is twice that for the sample as a whole, and nine times that for a hostile target. All these results come through in the medians as well, although not as dramatically.

The incidence of the presence of a founder is also very high in friendly targets, showing up as an impressive 40%. This is statistically significantly higher than the 24% average for the sample as a whole and the 10% average for hostile targets. The incidence of the presence of a founder in hostile targets is low relative to the sample, with a t-statistic of -2.23. There does not seem to be any significant difference in the age of the chairman or in the outside board ownership between the whole sample and friendly and hostile targets. However, when MBOs are not classified as acquisitions, we find that the chairmen of hostile targets are slightly younger than the average chairman in the sample, perhaps suggesting that the younger managers are more likely to strike a favorable deal with a white knight or fight harder to remain independent, while the older managers more often rely on the MBO as a takeover defense.

Before interpreting these results, we should explicitly acknowledge that the means we compute are only intended to be suggestive, since in their calculation we do not control for important differences between firms. For example, firms with very small ownership are larger firms that are less likely to be acquired. Without a multivariate analysis, some of the correlations we describe might be spurious. We deal with these issues in Section 4, but meanwhile proceed as if the evidence was indicative of the causal relationship between ownership and takeovers.

One interpretation of the results presented so far is that management teams with strong financial incentives to accept a tender offer at a premium do not resist. This is supported by the fact that boards of friendly targets have higher stakes and boards of hostile targets have lower stakes than the sample average. Moreover, the entire difference is basically accounted for by differential ownership of the top officers. Since officers have more to lose as a result of an acquisition than do other board members, looking at top officers rather than whole boards may be more powerful in explaining the adopted resistance strategy.

An alternative interpretation of the findings on friendly offers is that management teams with very large ownership have close to a veto power over the outcome of the bid, and that therefore the only acquisitions with large management ownership we observe are friendly. This is corroborated by the fact that firms where founders are present are more likely to be the targets of friendly bids, since founders might have a stronger preference for control as well as a better ability to resist. The two interpretations are not, of course, incompatible. Companies might be targets of friendly offers both because managers have a large incentive to succumb and because if they chose not to, the offer could not succeed.

The latter view suggests that a number of would-be hostile offers end up as friendly offers because of the necessity to bribe entrenched managers. It does not, however, explain a higher incidence of total acquisitions among high ownership firms that we find in the data. Table 2A presents the numbers and probabilities of various types of acquisitions for firms with special ownership structures, and Table 2B provides some hypothesis tests. Table 2A shows that, whereas the probability of a non-MBO acquisition within five years is 14.5% in the sample, it is 19.7% if the officer stake exceeds 15%. If MBOs are included, the probability that a firm with over 15% officer ownership gets acquired exceeds that for a firm with under 15% ownership by 11%, with a t-statistic of 2.11. That large stakes invite bids suggests that the managers' incentive to sell is probably an operative factor in the observed pattern of takeover activity.

The reason why companies with very large officer ownership have a higher likelihood of being acquired is that they have a much higher likelihood of a friendly bid. The probability that a firm with at least 15% top officer ownership was acquired in a friendly non-MBO transaction is 15.2% versus 6.2% for firms with officer ownership below 15%. This difference between high and low ownership firms is significant at the 1% level (t=2.57). On the other hand, the probability of a non-MBO acquisition initiated in a hostile manner is 4.5% for high ownership firms versus 7.4% for firms with less than 15% top officer ownership, which is not statistically significant.

These results suggest the possibility that the ownership structure of some firms makes them especially attractive targets of friendly takeovers. For example, if a top officer with a large equity stake wants to retire and simultaneously take some of his wealth out of the firm, he would probably prefer selling out at a premium to a diversification-minded acquiror to the

TABLE 2A: Acquisition Activity by Ownership Category

	Total Number of Firms	Number of Friendly	Number of Hostile	Number of Friendly Non-MBO	Number of Hostile Non-MBO	Probability of Non-MBO Acquisition	Probability of Hostile Non-MBO
Founding Family Present	111	17	4	14	3	.153	.027
Founding Family Absent	343	25	36	20	29	.143	.085
Top Officers' Stake Greater Than 15 Percent	66	15	3	10	3	.197	.045
Entire Sample	454	42	40	34	32	.145	.070

TABLE 2B: Differences Between Acquisition Probabilities For Various Ownership Categories. T-Statistics for Tests of Equality of Acquisition Probabilities in Parentheses

			All Acquisitions	Non-MBO Acquisitions
Probability of Hostile Acquisition Founder = 1	-	Probability of Hostile Acquisition Founder = 0	-.0690 (-2.23)	-.0575 (-2.06)
Probability of Friendly Acquisition Founder = 1	-	Probability of Friendly Acquisition Founder = 0	.0803 (2.55)	.0678 (2.37)
Probability of Any Acquisition Founder = 1	-	Probability of Any Acquisition Founder = 0	.0114 (.270)	.0103 (.27)
Probability of Hostile Acquisition OFF > .15	-	Probability of Hostile Acquisition OFF ≤ .15	-.0499 (-1.32)	-.0293 (-.858)
Probability of Friendly Acquisition OFF > .15	-	Probability of Friendly Acquisition OFF ≤ .15	.1577 (4.16)	.0896 (2.57)
Probability of Any Acquisition OFF > .15	-	Probability of Any Acquisition OFF ≤ .15	.1078 (2.11)	.0604 (1.29)

option of selling his shares on the open market. Life-cycle decisions of the officers might provide a stimulus for friendly bids.

Further evidence on this point comes from the results on founders. Table 2A shows that the probability of any acquisition of a firm run by the founding family is not much different from that of an average company in the sample. The likelihood of a friendly bid, however, is much higher for founders' firms, and that of a hostile bid is much lower. For the entire sample, the probability of a hostile non-MBO acquisition is 7.0% and the probability of a friendly non-MBO acquisition is 7.5%. For firms run by founding families, in contrast, the likelihood of a friendly bid is 12.6% and that of a hostile bid is 2.7%. The probability of a friendly bid is statistically significantly higher for firms with founding families than for firms without ($t=2.37$), and the probability of a hostile bid is significantly lower ($t=-2.06$). If founders can effectively deter hostile bids, and end up selling their firms when they intend to leave the business, such results might be expected.

A final piece of statistical evidence that corroborates the top management exit story concerns the age of the chairman. While the average chairman in our sample is 58.4 years old, and the average chairman of a firm with a founding family at the helm is 59.7, the average chairman in firms that are run by the founding family <u>and</u> are sold to a friendly acquiror is 62.6 years old. These findings are consistent with the notion that founders selling off their firms before retirement should on average be older.

An examination of the stories of individual companies confirms the statistical evidence. A common story (e.g., ABC, Beckman Instruments, Clark Oil, and others) is an elderly founder wishing to sell the business before he retires. In fact, of the fourteen founder firms that were acquired by another party in a friendly transaction, one was the case of bankruptcy, one of need to get money to pay inheritance taxes, one of a super-manager merging into a larger firm to get a bigger job, and the rest of founders or of their families wishing to get out.

If an important part of friendly acquisitions is just a personal life-cycle decision of top management, then it is natural to ask how can high takeover premia be paid in such transactions. One possibility is mismanagement under the founder's reign; e.g., insufficient risk-taking, insufficient expansion in order to maintain high fractional equity ownership, or just poor decision-making. In this case, the founder's exit is accompanied by a disciplinary takeover. An alternative possibility is that the takeover is synergistic, but that the desire of managers to run their own show often precludes such combinations. The founder's wish to get out provides the impetus for realizing the already available gains. Some evidence shedding light on these two possibilities is presented in Section 3.

3. Financial Characteristics of the Targets.

The financial motivation of target management is unlikely to be the only factor entering into the decision to oppose a tender offer. Some acquisitions might be done for reasons that management particularly dislikes, such as its own replacement or the liquidation of the firm. In this section, we pursue such possible heterogeneity of acquisition targets.

The starting point of our analysis is Tobin's Q. As the ratio of the market value of the firm to the replacement cost of its <u>tangible</u> assets, Tobin's Q can be viewed as measuring the intangible assets of the firm.

These may include future growth opportunities, monopoly power, quality of management, goodwill, rents appropriated away from unions, etc. Since we are looking at the measured Q, this interpretation can be problematic. The replacement cost of assets could be overstated, for example, if the firm bought its assets a long time ago and their value depreciated significantly due to technological progress, foreign competition, or other changes. In these cases, the inflation-adjusted historical cost is a poor guide to the true replacement cost, but a very low Q is probably still a reliable indicator of a declining firm.

Alternatively, Q might just capture the mispricing by the stock market of the firm's physical assets in their current use. If, however, a low Q genuinely measures the low valuation of tangible assets in their current use, it may pay to sell off assets when Q is low because those assets have a higher value in another firm or sector. Even when the firm's capital is highly firm- or sector-specific, it may pay to just abandon the unprofitable capacity or insist on a reduction in union wages that were set under more profitable conditions.

A related measure of profitability relative to the value of physical assets is the deviation of a firm's Q from the average Q of its 3-digit SIC code industry. The market might attach low value to assets of the whole industry, and it could attach an even lower value to the assets of a particular firm within that industry. If it does the latter, then we must look at the firm's idiosyncratic characteristics, such as its management, as a source of potential acquisition gains.

Tobin's Q can shed light on the hypothesis that hostile acquisitions are essentially purchases of old physical assets that can be redeployed more profitably either from an efficiency or tax viewpoint. If a low Q reflects low valuation of physical assets relative to their potential, then acquiring this firm might be a cost-effective way to buy and redeploy its physical capital. In the same vein, we look at the age of the firm, which might give us an idea of the age of its capital. Apart from serving as an indicator of a declining firm, the age of the capital stock is a proxy for the potential for a step up in the basis from which this capital can be redepreciated. From the tax viewpoint, acquiring older assets is more advantageous; Shleifer and Vishny (1986) show how such tax considerations can be important in MBOs.

Since Tobin's Q might be mismeasured, we are also interested in other potential measures of the firm's performance. In particular, we look at a 10-year growth rate of the firm's labor force, GL. If Q and GL are simultaneously low, we feel more confident in attributing low valuation to past or current troubles rather than to mismeasurement or market mispricing.

In two effective papers, Michael Jensen (1986a, 1986b) has proposed a free cash flow theory of low stock market valuation of targets of hostile takeovers. On his theory, because some firms waste shareholders' wealth on unprofitable investments and managerial perquisites, eliminating this waste can create shareholder value. An example of wasted free cash flows, proposed by Jensen and by Jacobs (1986), is exploration activity in the oil industry that did not slow down in the face of declining oil prices. Jensen suggests that interest and dividend payments alleviate the problem of free cash flow. In this regard, he points to the role of debt as a means to commit future corporate revenues to being paid out.

Strictly speaking Jensen's theory requires controlling for a variety of aspects of the firm's opportunity set to be properly tested. We nevertheless check what fraction of their earnings non-targets, hostile targets, and friendly targets allocate to dividends, interest payments and investment. The question is whether higher payouts and lower investment preclude hostile action.

Another important strand in the discussion of corporate acquisitions argues that capital market imperfections can deter otherwise feasible transactions. A firm with a large market value could be difficult to acquire, especially without the cooperation of its management, because financial markets might be unable to supply the credit necessary for the acquisition. This view attributes the lively hostile takeover activity of the 1980s at least in part to the appearance of junk bond financing. Looking at market values of acquired firms should thus enable us to appraise the extent to which capital market imperfections matter. Not surprisingly, all types of targets have fewer assets and lower market values than do firms that are not acquired, indicating that capital market imperfections might deter some corporate control transactions. Because market value is correlated both with Q and management ownership, we defer more discussion of this issue to the multivariate analysis section.

The means and medians of the variables of interest by the type of firm are presented in Table 3A, with the t-tests of differences of means in Table 3B. Recall that all the variables are measured at the beginning of 1980. The average Q of the sample is .848, which is the standard result of the low valuation of corporate assets by the stock market in 1980. The average Tobin's Q of a friendly target is .796, which is not significantly below the sample average. In contrast, the average Tobin's Q of a hostile target is only .524, which is significantly below .848 ($t=-2.84$). A similar pattern

TABLE 3A: 1980 Asset and Financial Characteristics of Sample and Acquired Firms

		Sample	Friendly	Hostile	Friendly Non-MBO	Hostile Non-MBO
Q	Mean	.848	.796	.524	.774	.545
	Median	.645	.617	.452	.624	.461
Q-Industry Q	Mean	0	.0163	-.113	-.0368	-.119
	Median	-.0304	-.0662	-.112	-.0794	-.115
Replacement Cost	Mean	2772.6	1372.0	1947.5	1534.6	2237.1
	Median	1055	747.7	791.4	843.1	960.6
Growth Rate of Labor Force	Mean	.0272	.0258	.0137	.0270	.0140
	Median	.0199	.0183	.00948	.0232	.00948
Year of Incorporation	Mean	1918.3	1924.6	1911.9	1924.6	1914.9
	Median	1920	1925	1913	1925	1916
Total Market Value	Mean	2092.6	969.8	1009.1	1028.4	1181.1
	Median	808.2	683.2	384.2	732.0	387.8
Investment/Income	Mean	.704	.651	.576	.687	.588
	Median	.640	.522	.579	.629	.609
Dividends/Income	Mean	.183	.158	.178	.162	.176
	Median	.175	.151	.176	.151	.172
Interest/Income	Mean	.193	.246	.219	.254	.232
	Median	.175	.261	.211	.269	.223
Value of Long-Term Debt/Total Market Value	Mean	.248	.285	.330	.269	.335
	Median	.208	.228	.267	.213	.299

TABLE 3B: T-Statistics For Tests of Equality of Means of Asset and Financial Variables by Acquisition Type

	Friendly vs. Sample	Hostile vs. Sample	Friendly Non-MBO vs. Sample	Hostile Non-MBO vs. Sample	Hostile vs. Friendly	Hostile Non-MBO vs. Friendly Non-MBO
Q	-.360	-2.84	-.464	-2.36	-2.66	-2.19
Q-Industry Q	.163	-1.43	-.337	-1.34	-1.72	-1.39
Replacement Cost	-1.13	-.840	-.914	-.485	.641	.656
Growth Rate of Labor Force	-.148	-1.54	-.0191	-1.37	-1.02	-.985
Year of Incorporation	1.97	-1.92	1.78	-.922	-2.78	-2.02
Total Mkt. Value	-1.19	-1.46	-1.04	-1.09	.0866	.285
Investment/Income	-.701	-1.86	-.204	-1.57	-.818	-.96
Dividends/Income	-1.26	-.318	-.938	-.354	.966	.624
Interest/Income	2.07	1.14	2.18	1.56	-.804	-.622
Value of Long-Term Debt/Total Mkt. Value	.864	2.45	.460	2.31	.646	.859

emerges in the medians.

Unfortunately, a variety of interpretations are consistent with this result. The first possibility is that hostile targets are mismanaged and therefore have low Tobin's Qs. The result of such mismanagement is the inefficient utilization of the fixed assets of the firm, and the resulting low valuation of these assets by the market. Removing such management might justify the takeover premium, although the managers would probably resist since they do not want to lose control or to have their incompetence revealed. Managers of friendly targets, in contrast, are safe, and do not need to worry about being removed.

Mismanagement can come in two forms. It can be a firm-specific or an industry-wide phenomenon. In the former case, what should matter for hostility is the extent by which the firm underperforms similar firms. To some extent, this difference is measured by Q - Industry Q. In fact, the mean of Q - Industry Q is positive for friendly targets and negative for hostile ones, with the difference significant at the 10% level (t=1.72). On the other hand, the differences are much smaller in the medians. To ascertain whether the industry or the firm effect is more important in predicting hostile activity, the next section presents some probits.

An alternative interpretation of extremely low Tobin Qs of hostile firms is that, while the assets are managed properly, they simply are not particularly valuable. For example, if hostile targets have invested a long time ago when their industry was growing, but now the fortunes of their industry have turned around, they will be stuck with a lot of capital. Under this scenario, hostile targets might be smokestacks ruined by technological progress and foreign competition.

Consistent with this view, hostile targets are older and slower growing than the average firm in the sample. The difference in year of incorporation between hostile targets and other firms is over six years, and is significant at the 6% level. The difference in the growth rates of the labor force is 1.4% (or almost twofold), which is significant at the 12% level. Friendly targets, in contrast, are younger than the average firm and are growing at roughly the same rate.

Although this view suggests why firms with a lot of old fixed capital would have low Qs, it does not explain why these firms are attractive candidates for hostile acquisitions. One explanation is the free cash flow theory. If low Q industries are in decline, managers may be too slow to close down or sell-off plants, abort investment, and trim down operations. There ia some evidence that hostile targets are investing a smaller fraction of earnings than the average firm in the sample (t=-1.86).

If managers' dedication to the aurvival of organizations, stressed by Donaldson and Lorsch (1983), keeps them from shrinking their operations sufficiently fast, then acquirors can increase value by speeding up the decline of the target company. Our numbers on growth of the labor force, incorporation year, investment, and Q are all consistent with the version of the free cash flow theory that stresses management's tendency to disinvest too slowly.

Another reason why old tangible assets could attract acquirors has to do with taxes. An important feature of the (old) US tax code is the General Utilities doctrine, according to which if a firm's assets are sold in a liquidation, then capital gains taxes can be avoided at the corporate level. After such an acquisition, the target's assets can be redepreciated, presumably using the accelerated schedules of the 1980's. The step-up in basis could have been an important tax motivation for acquiring old capital. In addition of course, there are tax gains in acquisitions due to leverage. While these apply equally to firms without too much fixed capital, it may be more costly for such firms to obtain debt financing. If managers oppose a loss of control to an acquiror, they can lever up and step up the basis by doing an MBO or finding a white knight. These in fact have been common responses to hostile pressure.

One final explanation for hostile offers that is consistent with our findings is underpricing by the market. If the stock market does not value some firms properly, an acquiror who understands their intrinsic value may be able to buy assets more cheaply on the stock market than on the new or used capital goods market. Managers reluctant to give up assets at below their intrinsic worth would resist such acquisitions. One problem with this explanation of hostile bids is that it says nothing as to why older, slower growing companies with mostly tangible assets are the only ones undervalued on the stock market. Moreover, since once a company is in play the corporate control market becomes very competitive and a lot of information is revealed, there definitely are limitations on the ability of acquirors to profit in this way.

In summary, hostile targets appear to have sharply distinguishable asset characteristics. Relative to the market value of the firm, they appear to have a lot of old tangible capital. They are growing slowly and have a lot of debt. While this suggests that hostile acquisitions might be related to the desire to purchase these fixed assets, there are a variety of explanations consistent with this general story. In particular, incompetent management, asset redeployment, free cash flow, taxes and underpricing of the firm's assets by the market could all invite takeover bids. At the same time, we think that the evidence is supportive of the notion that hostile takeovers are motivated by the need of disciplinary action against the target management.

The analysis of this section said virtually nothing about the targets of friendly bids. Except for the fact that they are on average smaller and six years younger than the rest of the sample (t-statistics of -1.13 and -1.97 respectively), friendly targets are very similar to the average firm in the sample. Most notably, their Q is not statistically or substantively different from that of the average firm in the sample, and is significantly higher than Q of an average hostile target (t=2.66). In a sense, this is consistent with the view that friendly targets are just regular firms, and their acquisition derives from some idiosyncratic circumstances such as a life cycle decision of a top officer with a large stake, or a match-specific synergy (e.g., the desire of the acquiring management to enter a particular new business). One interesting feature of friendly targets is that they appear to have higher interest payouts and lower dividend payouts than an average firm in the sample, perhaps indicating that they are starved for capital. Their total outside payouts are very similar to those of an average firm.

The results of this section provide the basic evidence in support of the notion that disciplinary takeovers are more often hostile, while synergistic takeovers are more often friendly. The evidence indicates that hostile targets are older, poorly performing firms, possibly with a lot of old plants or equipment that should be abandoned or more profitably deployed elsewhere.

This is exactly what one would expect of targets of disciplinary takeovers. In contrast, financial characteristics of friendly targets do not appear to be very different from those of an average firm in the sample. If what attracts acquirors to such targets are match-specific synergies (as well as the target manager's interest in selling), we would not expect to see any real differences in the basic financial variables. In short, the results suggest that the motive for a takeover might well determine its mood. Treating hostile and friendly acquisitions as reflecting the same underlying fundamentals might be very misleading indeed.

4. Probits.

The previous section has offered evidence suggesting that the motives for hostile and friendly acquisitions might be different. In this section, we perform some further statistical tests of what makes a firm the target of a friendly takeover and what makes a firm the target of a hostile takeover. This is different from asking what makes the mood of a takeover of an already selected target hostile or friendly, since the latter question presumes that characteristics that make firms targets in the first place are the same across moods. If hostile and friendly takeovers typically reflect different motives, it is misleading to think of a firm becoming a general target. Rather, separate considerations are appropriate for predicting which firms are subject to hostile (i.e., disciplinary) takeovers and which are subject to friendly (i.e., synergistic) ones.

Accordingly, this section presents probits estimated on the whole sample of 1980 Fortune 500 firms, that separately predict hostile and friendly acquisitions. The models are either prob(hostile vs anything else) -

f(characteristics), or prob(friendly vs anything else) = g(characteristics). In short, we separately compare hostile and friendly targets to the rest of the Fortune 500 sample.

We do a multivariate analysis because many of the company characteristics we look at are correlated with each other. For example, the growth rate of the firm's labor force is so closely correlated with Q that it becomes dominated by Q in the regressions. While we have run several additional probits to identify the separate sources of influence of firm characteristics on the probability of a friendly acquisition and the probability of a hostile acquisition, the results presented below reflect our main findings.

Table 4A presents the four probits estimating the likelihood that a Fortune 500 firm goes through a successful friendly acquisition. Mimicking our earlier finding that friendly targets are just like the sample as a whole, the probits do not reveal particularly strong correlations. Specifically, the probability of a friendly acquisition is not clearly related to the log of the firm's market value, the presence of a founder, or Tobin's Q. That high market value does not deter friendly acquisitions is inconsistent with the preliminary indications from Table 3A. This could be because size is negatively correlated with officer ownership which is, in turn, positively related to friendly bids. In this case, the finding in Table 3A is spurious. Given that friendly bids are often made by large, cash-rich companies and sometimes for stock, it is not entirely surprising that capital market constraints are not particularly binding.

When friendly MBOs are included among acquired firms, there is some evidence that large officer ownership promotes friendly acquisitions. This

TABLE 4A: Probit Regressions of Friendly Acquisition Dummies on Ownership and Financial Variables

	Dependent Variable			
	Friendly Acquisition = 1	Friendly Acquisition = 1	Friendly Non-MBO Acquisition = 1	Friendly Non-MBO Acquisition = 1
Intercept	-1.33 (-1.81)	-1.29 (-1.70)	-1.57 (-1.86)	-1.60 (-1.90)
Log of Total Market Value	-.0583 (-.490)	-.0632 (-.561)	-.0195 (-.150)	-.0213 (-.170)
Founding Family Present = 1	-.130 (-.339)	-.129 (-.337)	-.155 (-.361)	-.162 (-.373)
Proportion of Equity Owned by Top Officers	1.54 (1.60)	1.51 (1.48)	1.18 (1.09)	1.20 (1.09)
Q	.00289 (.0103)		-.0574 (-.187)	
Q-Industry Q		.0556 (.140)		-.102 (-.158)
Number of Firms in Regression	371	371	371	371

Note: t-statistics in parentheses

result gets weaker when MBOs are excluded, since, as we show in the next section, firms going through friendly MBOs often have dominant management ownership. We should also point out, however, that the ownership results are generally weaker in the probits than in the earlier tables, because we lose a substantial number of observations due to missing values for Q. We have Q for only 20 friendly targets and 31 hostile targets.

The result that as far as assets and performance go, friendly targets are just like other firms, is confirmed using both Q and Q - Industry Q. Neither Q nor Q - Industry Q mattered for predicting friendly acquisitions. These negative results are consistent with the notion that friendly takeovers are motivated by synergy.

The story is very different with hostile acquisitions, the probits for which are presented in Table 4B. For the sample including hostile MBOs, the likelihood of a hostile acquisition is negatively related to the log of value, negatively related to Q, and negatively related (at the 15% confidence level) to the presence of a founder. Surprisingly, the negative effect of officer ownership on the probability of a hostile acquisition is not statistically significant.

The result that, controlling for Q, high market value deters hostile acquisitions, seems likely to reflect capital market imperfections. It suggests that some firms are too large to be acquired through a hostile bid, even when fundamentals dictate that they should be. This result becomes substantially weaker when hostile MBOs are excluded from the sample of hostile targets, since these are very small firms. In fact, MBOs are probably the best case for the argument that poor capital markets limit large transactions. The results in Table 4B also confirm our earlier finding that

TABLE 4B: Probit Regressions of Hostile Acquisition Dummies on Ownership and Financial Variables

	Dependent Variable			
	Hostile Acquisition = 1	Hostile Acquisition = 1	Hostile Non-MBO Acquisition = 1	Hostile Non-MBO Acquisition = 1
Intercept	.506 (.864)	.511 (.882)	-.123 (-.195)	-.147 (-.231)
Log of Total Market Value	-.182 (-1.91)	-.269 (-3.11)	-.115 (-1.17)	-.188 (-2.03)
Founding Family Present = 1	-.751 (-1.56)	-.748 (-1.72)	-.606 (-1.28)	-.623 (-1.46)
Proportion of Equity Owned by Top Officers	-1.31 (-.816)	-1.29 (-.843)	-.878 (-.555)	-.843 (-.556)
Q	-.827 (-1.96)		-.722 (-1.66)	
Q-Industry Q		-.219 (-.492)		-.268 (-.557)
Number of Firms in Regression	371	371	371	371

Note: t-statistics in parentheses

hostile targets have low market valuations relative to tangible assets, and that the presence of a founder discourages hostile action, <u>holding officer stake and valuation constant</u>. This suggests that founders or their families fight hostile bids more effectively, either because they value control more or because they command shareholders' or directors' support.

One important question that we could not answer by simply comparing means is whether industry-specific or firm-specific components of Tobin's Q are attracting hostile activity. In our estimated probits, Tobin's Q has a significant negative effect on the likelihood of a hostile acquisition, whereas Q - Industry Q has an insignificant negative effect. The log likelihoods for the two equations are also quite different, with the Q equation higher by 3.37. Furthermore, when Q and Q - Industry Q are simultaneously included in the probit, Q remains significant while Q - Industry Q hardly has any additional effect on the probability of a hostile acqusition. It appears that industry-specific rather than firm specific problems attract hostile bids.

Viewed in the context of the mismanagement story, this finding says that hostile activity is stimulated by industry wide and not company specific mismanagement. For example, it would suggest that the whole oil industry fell into the exploration trap, and not so much that Gulf Oil was a particularly overzealous explorer. The finding that, in predicting hostile action, Q matters while Q - Industry Q does not, may indicate the existence of entire industries whose assets can be profitably redeployed either for efficiency or tax reasons. As further examples, many steel and textile firms might be in need of shutdowns and selloffs that do violence to the preferences of existing managers. Such managers are not necessarily just trying to shirk or save empires. They may just be opposed to changes that enrich shareholders at the expense of employees. The point is that hostile acquisitions can be a way to move large quantities of fixed capital into more profitable (and possibly also more productive) uses, as one would expect of disciplinary takeovers.

While the statistical evidence is fairly weak, it is consistent with our observation that the motive for friendly acquisitions is more likely to be synergistic whereas for hostile ones it is more likely to be disciplinary. Specifically, friendly acquisitions seem to be related to high officer ownership, which suggests that an important impetus for such acquisitions might be a life-cycle decision of a large shareholder. Furthermore, all other basic firm characteristics we have looked at appear to be irrelevant for predicting friendly acquisitions. We might expect this of synergistic or diversification-oriented takeovers. Hostile bids, in contrast, seem to be targeted at firms located in low Q industries. One interpretation of the low Q finding is that hostile acquisitions are a way to redeploy tangible assets in a more profitable way. Many of these redeployments can either be unacceptable to managers (e.g., liquidation, employee dismissals), or can be more painlessly replicated by a white knight or in an MBO (e.g., step-up in depreciable basis, increases in leverage). This, of course, is the story of the disciplinary motive for hostile takeovers.

5. Management Buyouts.

Management buyouts are important to think about since we know that the motive behind them cannot be synergistic. Whatever gains realized by MBO organizers must come either from a more profitable exploitation of the firm's own resources, including its managerial talent, or from the ability of organizers to buy the firm's assets for less than their intrinsic worth under the existing operating strategy.

Schipper and Smith (1986), Shleifer and Vishny (1986), and Kaplan (1987) discuss the sources of gains in management buyouts. All of these authors found that tax considerations, especially leveraging up and step up in the basis, could justify a large part of the takeover premium. Kaplan estimates that 80% of the takeover premium can come from the tax savings. Other important candidates for the source of gains include buying underpriced assets, improved incentives from higher management ownership and leverage, and the restructuring of declining companies along the lines sought by raiders.

Hence, it is important to distinguish between two types of management buyouts. The first are the buyouts that respond to hostile pressure on the target's management. Such pressure can either take the form of an outside bid, or simply of an acquisition of a beachhead along with a 13-D filing to the effect that control might be sought. The fact that managers and their investment banker partners can win the bidding for the firm in such situations suggests that the gains from an acquisition can be realized by them as well as by outside bidders. If these gains come from tax savings or buying underpriced assets, this result is not surprising. But it also seems likely that after an MBO managers redeploy the target's assets in better uses. Managers may have been unwilling to implement these changes before being forced to make a defensive bid for the firm at a large premium.

Besides these hostile management buyouts, there are transactions initiated by the management without any apparent outside threat. We call them friendly MBOs. One of the motives for friendly MBOs may be the exit story we developed for friendly deals more generally. In this case, the MBO can be a way for a dominant CEO to pass the leadership to the next generation of managers without dissipating control. Another motive for friendly MBOs may just be to realize tax gains from leverage and stepping up the depreciable basis of the firm's assets. While another oft-cited motive for MBOs is to improve incentives through increased management ownership, this seems less plausible for our sample of friendly MBOs given that management ownership is already quite high.

A final motive for friendly MBOs that may be important, is for management to buy the share of the firm's assets they do not already own for less than its true value (either under the existing operating strategy or under a new one). Of course, this story requires that management have some ability to freeze out minority shareholders once it takes over, so that it can get shareholders to tender for less than the true value of their shares. Also, the story presumes that competitive bidding from third parties will not drive the profit from this strategy to zero. But both of these requirements seem likely to be met in many cases where managers have much better information than outsiders about the true value of the firm and management already owns a good deal of the stock (as in our sample of friendly MBOs).

Of the sixteen MBOs in our sample of 82 acquisitions, 8 are hostile in the sense described above and the other 8 are friendly. Table 5 presents ownership and financial characteristics of these MBOs. Comparing this table with Tables 1A and 3A, we see that hostile MBOs share many of the features of other hostile transactions. They have very low Qs, low growth rates, low investment, large amounts of debt, and relatively low board and officer

TABLE 5: Ownership and Financial Characteristics for Management Buyouts

	Sample	Friendly MBO	Hostile MBO
Founding Family Present Present On Top Management Team = 1	.244	.375	.125
Fractional Equity Ownership By Top Two Officers	.0636	.170	.0135
Fractional Equity Ownership By The Rest of the Board	.0454	.131	.0517
Age of Chmn.	58.4	59.8	62.5
Q	.848	.916	.436
Q-Industry Q	0	.318	-.0873
Replacement Cost	2772.6	450.3	740.5
Growth Rate of Labor Force	.0272	.0205	.0119
Year of Incorporation	1918.3	1924.3	1898.4
Total Market Value	2092.6	638.1	292.1
Investment/Income	.704	.456	.499
Dividends/Income	.183	.136	.185
Interest/Income	.193	.204	.135
Value of Long-Term Debt/Total Market Value	.248	.373	.310

ownership. The average year of incorporation for a hostile MBO target is a strikingly low 1898. These companies are much smaller than run of the mill hostile targets, and have lower incidence of a founder's presence. Our examination of particular instances of hostile MBOs confirms the observation that they are often acquisitions of old tangible assets, that can be subsequently redeployed more profitably or redepreciated. The picture of hostile MBOs that emerges is consistent with their being a defensive response to the threat of a disciplinary takeover.

Friendly MBOs are a very different type of transaction, and it is much less clear how they compare with other friendly deals. Friendly MBOs are management-initiated deals that are not foiled by higher third party bids. Not surprisingly, 37.5% of these firms are run by the founding family, and the average pre-MBO board stake is over 30%.

Given that officers in friendly MBOs often have virtually complete control of the company, their motives for the transaction may be suspect. Purchasing undervalued shares in the presence of coercion and disadvantaged competitive bidders seems like a distinct possibility. Consider two cases in our sample. One is an MBO of Metromedia at a 100% premium, which was followed by the sale of the parts of the company (previously dictatorially run by the same boss for 30 years) for more than double the acquisition price within 18 months. Another is the MBO of Beatrice foods, followed by the sale of several divisions that paid for the whole acquisition (Beatrice, however, did not have dominant insider ownership). There are other companies where management initiated an MBO when its voting control was already effectively absolute, such as Levi-Strauss and Questor.

In sum, while we do not have a clear idea of how friendly MBOs relate to other friendly acquisitions, our consolidation of hostile MBOs with other hostile acquisitions does not seem to do too much violence to the data. Firms going through MBOs in response to hostile threats resemble other hostile targets quite closely. In fact, we can use our knowledge of hostile MBOs to make inferences about hostile takeovers more generally.

6. Concluding Comments.

The notion developed in this paper is that the motive for a takeover can have a large influence on its mood. Disciplinary takeovers are more likely to be hostile, whereas synergistic takeovers are more likely to be friendly.

Compared to the universe of Fortune 500 firms, hostile targets are smaller, older, more slowly growing, have lower Tobin's Qs, more debt, and invest less of their income. The low Q seems to be an industry specific rather than a firm specific effect. In addition, hostile targets are less likely to be run by the founding family, and have lower officer ownership, than the average firm. Low Q, low market value, low growth and investment, and the absence of a founder are the characteristics of a firm that are most likely to make it the target of a hostile bid.

Compared to the universe of Fortune 500 firms, friendly targets are smaller and younger, but have comparable Tobin's Qs and growth rates. Friendly targets are more likely to be run by a member of the founding family, and have higher officer ownership, than the average firm. The decision of a CEO with a large stake and/or with a relationship to the founder to retire often precipitates a friendly acquisition. High officer ownership is the most important attribute in predicting friendly acquisitions.

We conclude that differences between synergistic and disciplinary takeovers, captured in part by differences in their moods, should be recognized in empirical work. Specifically, studies that fail to adequately distinguish acquisitions with different motives can be misleading. First, difficulties can arise when disciplinary and synergistic takeovers are analyzed together, presenting the researcher with a mix that may have few common characteristics. Our results suggest that, as a first cut, separating hostile and friendly takeovers can help deal with this problem. A second difficulty can occur when facts about one type of acquisition are used to draw inferences about another. An example of a good study that could be misread is Brown and Medoff's 1987 paper. The authors find that in a large sample of small Michigan companies, employment and wages rise after they are acquired. Since most of their sample seems to consist of friendly acquisitions of very small firms with high management ownership, one cannot conclude from their work that employment and wages do not fall on average after a firm is acquired in a disciplinary takeover. To get at the latter question, one would have to look at hostile targets. A key implication of our study for future work, therefore, is that results for friendly bids may have little to say about hostile bids, and vice versa.

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