

The Effect of Target Ownership Structure in the Wealth Gains in Owner-Manager Dominant Acquisitions: Evidence from Korean Cases

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Abstract

This paper examines how the distribution of target ownership is related to the wealth gains of target shareholders in “owner-manager” dominant acquisitions, in which a firm is managed by managers and directors nominated and closely directed by controlling shareholders. Using the Korean case of mergers and acquisitions during 1996-2007, we find that the agency problem exists between owner-managers and non-controlling shareholders. This finding is different from what we can observe in the US case, where the agency conflict between managers and shareholders is more crucial. In the meantime, the effect of the bidder’s top 30 *chaebol* membership on the wealth of target shareholders is inconclusive. In order to resolve the agency problem, the presence of institutional shareholding may be effective.

Keywords: mergers and acquisitions, ownership structure, governance structure, agency problem, managerial entrenchment, *chaebol*, owner manager

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The author also wishes to thank the KDI School of Public Policy and Management for their gracious research fund for this study.

INTRODUCTION

A distinguishable characteristic of publicly listed Asian companies is the dominance of “owner-managers,” in which a firm is managed by managers and directors nominated by controlling shareholders. Because controlling shareholders sometimes become managing directors or controlling shareholders closely direct professional managers through hierarchy or long-term relational bondage, in many cases, the interests of managers and controlling shareholders are tightly aligned. Therefore, owner-managers could have the incentive to maximize the benefits of controlling shareholders rather than those of other shareholders, including minority shareholders (La Porta, Lopez-de-Silanes, and Shleifer 1999; Johnson et al. 2000; Bae, Kang, and Kim 2002). In these circumstances, the imbalance of control power between owner-managers vs. (non-controlling) shareholders would be a central issue not only to the corporate governance study, but also to investors and securities legislation.¹⁾

Mergers and acquisitions can be used as excellent experiments to test the valuation effect of corporate governance structure (Stulz, Walking, and Song 1990; Sudarsanam, Holl, and Salami 1996; Moeller 2005). First, they require the active participation of all decision makers, namely, managers, directors, and shareholders. Managers negotiate the acquisition, directors endorse it and are sometimes involved in the negotiations, and shareholders have to either vote on it or decide whether to tender their shares. Second, the effect of the corporate governance structure on the value of the target, given appropriate control for other influences, is immediately observable in the takeover premium.

There are three issues presented in the study. First, this paper examines how the ownership of owner-managers in a target firm influences the wealth gain of target shareholders in acquisitions. Particularly, we address the hypotheses concerning the impact of agency conflict between owner-managers and non-controlling shareholders on the way the value is created and distributed:

1) In the paper, the owner-managers mean both managers and controlling shareholders who share aligned objectives.

Does the owner-managers' ownership of a target firm matter in determining acquisition premium? If so, do they utilize their divestiture-decisions to maximize the benefits of all shareholders including minority shareholders? Second, this paper explores whether wealth gains can be created for target shareholders when the bidder belongs to a top 30 *chaebol*²⁾ group. If the benefits from being a member of a *chaebol* group surpass its corresponding costs, positive wealth could be gained for target shareholders because the *chaebol* bidder could pay more for more synergy potential. Third, if they tend to behave more for themselves, *per se*, if there is agency problem, can the presence of non-controlling large shareholders such as institutional investors be an agency control mechanism?

In two ways, this paper differs from the previous research in the area of Korean M&A and ownership structure. While most of the previous studies including Bae, Kang, and Kim (2002) and Cho and Jun (2004) consider the 'bidder' ownership structure possibly due to lack of target data, this paper focuses on the effect of 'target' ownership structure on the firm value. Considering that target managers and non-management target blockholders could have different motivations in the event of a takeover attempt (Stulz, Walking, and Song 1990; Song and Walkling 1993; Bae, Kang, and Kim 2002; Moeller 2005), it seems more meaningful to investigate the effect of target ownership structure rather than bidder ownership on the takeover premium.

In the study, the sample period (1996-2007) is updated to incorporate significant current events such as the Asian financial crisis in 1997 and the Korean M&A market liberalization around 1998. As Cho (2007) maintains, during the liquidity-scarce period of 1996-2006, many changes in regulations and market conditions have been made in the Korean M&A market. It seems timely and interesting to understand how the distribution of target ownership is related to the division of takeover gains during the credit crunch period or after M&A market liberalization.

The result shows that the effect of owner-management

2) A *chaebol* is defined as a group of companies whose more than 30 percent equity is owned by the group's controlling shareholder and its affiliated companies.

shareholding is negatively significant. It may indicate that the owner-managers' ownership portion of a target significantly affects the target's premium, and that the more the owner-managers own the target's shares, the less wealth gains would be created for the target shareholders upon acquisitions. Because more ownership allows more control power to the owner-managers in their managerial decisions in acquisitions, if they behave for the maximum benefit of overall shareholder wealth, positive wealth gains will be created for the target shareholders. However, as suggested by many scholars including Stulz, Walking, and Song (1990), Sudarsanam, Holl, and Salami (1996), and Moeller (2005), if they behave for the benefit of controlling shareholders only, negative wealth gains will be created, and it may suggest that an agency problem exists between owner-managers and non-controlling shareholders. As for the *chaebol* effect, the *chaebol* membership of a bidder is not likely to have a significant impact on the takeover premium of a target. The study also suggests that the presence of institutional investors could be an effective agency control mechanism to resolve the agency problem.

The paper is organized as follows: the second section discusses the theoretical framework; the third section presents the hypotheses regarding the impact of ownership structure; in the fourth section, the methodology and sample are described; the fifth section discusses the results; and the final section provides conclusions.

THE THEORETICAL FRAMEWORK

Much literature has documented the potential conflict between (professional) managers and shareholders, (Salter and Weinhold 1979; Ruback 1988; Seth 1990; Moeller 2005) as it is often observed in the US, where ownership and management are clearly divided and secured. In many Asian countries including Korea, partly due to cultural propensity for family- or relationship-oriented social atmosphere, if any, the conflict between owner-managers (controlling shareholders) and non-controlling shareholders appears to be more serious than the conflict between managers and shareholders (La Porta, Lopez-de-

Silanes, and Shleifer 1999; Johnson et al. 2000; Bae, Kang, and Kim 2002). In fact, there are many listed companies in Korea whose controlling shareholders (ownership) play a critical role in the management of the companies both directly and indirectly (management). Unlike the US, they are shareholders or owner-managers who control management. Among 36 target firms in our sample, for instance, owner-managers own on average 35.67% of equity. Considering that the targets are public firms, the managers' ownership is much higher than that of US public firms.

Besides cultural propensity, other reasons for the prevalence of owner-managers among Asian firms may include a relatively short period of capitalism and an underdeveloped market for professional managers. Furthermore, the history of successful companies is not long enough to make a distinction between ownership and management: in most cases, the founders and their families are still in management positions. In any event, the potential conflict between managers and shareholders, a central issue for many previous literatures, is no longer important. Rather, for some companies in Korea, other Asian countries, and Latin America, the potential conflict between owner-managers and non-controlling shareholders is crucial.

Owner-Managers and Agency Problem

There are two competing views concerning the relationship between (owner) managers and shareholders: neoclassical and the agency framework. In the neoclassical view, managers' acquisition decisions are supposed to enhance shareholder wealth (Salter and Weinhold 1979; Seth 1990). According to this view, the objectives of owner-managers' acquisition decisions are tightly aligned with those of shareholders, say, to maximize overall shareholder value. The owner-managers' actions are assumed to maximize the benefits of all shareholders including minority shareholders.

Increased managerial ownership by owner-managers would encourage diligence and reduce incentives to make poor acquisition decisions because owner-managers bear a higher fraction of the cost from such poor decisions. Thus, it is expected that managerial equity has a positive impact on target

shareholder wealth (Stuiz, Walkling, and Song 1990; Song and Walkling 1993). The hypothesis 1a is derived from this view as follows:

H1a: The wealth gains of target shareholders increase, with large owner-managerial shareholdings due to managerial alignment (the neoclassical model).

A competing view is the agency problem, in which owner-managers (as agent) may not always act in the interests of all the shareholders (as principal), and may pursue their own self-interest (Jensen and Ruback 1983). Applying the agency problem between managers and shareholders into the cases of 49 countries, La Porta, Lopez-de-Silanes, and Shleifer (1999) assert that “the central agency problem in large corporations around world is that of restricting expropriation of minority shareholders by controlling shareholders.” Johnson et al. (2000) further argue that the owner-managers or controlling shareholders have strong incentives for ‘tunneling’ to siphon overall shareholder wealth from the firm for the benefit of the owner-managers. The view implies the owner-manager’s entrenchment that they could make poor acquisition decisions in order to maximize their own interests.

When they possess a large portion of firm directly or indirectly, target owner-managers could control the firm, making non-controlling shareholder intervention costly. For instance, large ownership could allow more seats on the board. In these circumstances, due to the agency conflict between owner-managers and non-controlling shareholders, even when a bid is value additive to their shareholders, the target management (controlling shareholders) may resist the bid and launch various defensive strategies to frustrate it (see Ruback (1988) and Moeller (2005)). Managerial resistance to a bid could be influenced by the managerial need for independence. While golden parachutes may increase bid premium, many other actions such as stock repurchases, sale of crown jewels, and poison pills may reduce the incentive for bidders to bid, diminish the probability of a winning bid and entrench incumbent target managers (Ruback 1988). Thus, it is expected that managerial equity will have a negative impact on target shareholder wealth

(Moeller 2005). This view is examined using the hypothesis below:

H1b: The wealth gains of target shareholders decrease, with large owner-managerial shareholdings due to managerial entrenchment (the agency model).

Top 30 *Chaebol* Effect

Chaebol is a unique characteristic of Korean economy. The Korea Fair Trade Commission (KFTC) annually reports the top 30 *chaebols* on the basis of their total asset value. From the perspective of their importance and market power over the Korean economy, the top 30 *chaebols* differ clearly from other smaller *chaebols* or independent companies (Bae, Kang, and Kim 2002).

This paper explores the effect of the top 30 *chaebols* on the wealth of a target firm upon acquisition. When a target is acquired by a bidder who belongs to a top 30 *chaebol*, can target shareholders earn more? By analyzing the Korean acquisitions between 1981-97, Bae, Kang, and Kim (2002) posit that the *chaebol* membership has deteriorated its own firm value by providing the controlling shareholders of a group with an opportunity to siphon out the wealth of a target for other affiliates of the group for the benefits of *chaebol* groups overall, not solely for the benefits of a target firm. They claim that “while minority shareholders of a *chaebol*-affiliated firm making an acquisition lose, controlling shareholders of that firm benefit because the acquisition enhances the value of other firms in the group. This evidence is consistent with the ‘tunneling view’.”

Since the IMF crisis in 1997, the Korean economy including the business circle has been far enhanced in terms of transparency and appropriate governance structure. As noted by Cho (2007) and others, furthermore, the Korean M&A market have been legislated and liberalized since 1998, and any political, governmental, or institutional interference has become minimal. In the new circumstance reflecting its recent changes, would the ‘tunneling view’ be still sustainable?

According to the ‘value-added view’ (Khanna and Pelepu 2000), a business group could add value to its member firms. When

markets are not well developed or accessible, for example, the *chaebol* membership can add value by internally providing a necessary capital or captive market. If a target, say, an auto parts manufacturing company, is acquired to be a member of Hyundai Motor Company (HMC) group, for an extreme example, is this good or bad for the target shareholders? If the 'tunneling view' holds true, the shareholders would experience wealth loss because it can be expected that the target wealth would eventually be tunneled to the controlling shareholder of the HMC group. If the 'value-added view' holds true, on the other hand, they would gain wealth because the parts company can create positive synergy value by becoming a member firm of the HMC group.

Roughly speaking, the answer for the question of "would the 'tunneling view' be still sustainable?" may depend on the balance of both the possible costs of 'tunneling' and the amount of positive synergy or value the acquisition could create. If the benefits from being a member of a *chaebol* group surpass its corresponding costs, positive wealth could be gained for target shareholders because the *chaebol* bidder could pay more for higher synergy potential. To examine this interesting issue, the hypotheses are derived as follows:

H2a: The wealth gains of target shareholders decrease, with the acquisition of a *chaebol* bidder due to the tunneling effect. Or, if a bidder belongs to a *chaebol*, the wealth gains of target shareholders decrease.

H2b: The wealth gains of target shareholders increase, with the acquisition of a *chaebol* bidder due to internal capital and captive market. Or, if a bidder belongs to a *chaebol*, the wealth gains of target shareholders increase.

Institutional Shareholders as Agency Monitors

If the agency problem is prevalent as posited in hypothesis 1b, unless there are mechanisms in place to control this agency conflict, managerial decisions in acquisitions may be made to maximize owner-managers' own wealth because they control the firm and make non-controlling shareholder intervention costly.

One of the most popular agency control mechanisms to increase managerial alignment is monitoring by large (non-controlling) institutional blockholders (Stuiz, Walkling, and Song 1990; Sudarsanam, Holl, and Salami 1996; Moeller 2005). Large institutional investors, whose main goal is maximizing their financial gains from their investments, may have more experience, information, power and incentive than minor individual shareholders to monitor the managerial behaviors of owner-managers. If 'professional' institutional investors could effectively monitor their managerial behavior, as Shleifer and Vishny (1986) suggest, the potential agency cost would be minimized, and the target firm would be highly valued prior to the bid. Thus, the created value that the bidder could bring about would be smaller while the subsequent bid premium would be smaller.

As a resolution of IMF crisis, DJ Kim's administration has deregulated the Korean M&A market. Deregulation completely opened its equity market and invited many institutional investors both inside and outside Korea. Its underlying logic would be that the sophisticated shareholder would control owner-managers' opportunistic behavior, if any, and enhance transparency, governance structure, and value. The value enhancement through check-and-balance activities by institutional investors can be seen in the event of SK Corporation (SK) and Sovereign Asset Management (Sovereign) in 2003~4. While it has bought about 15% of outstanding shares of SK which was then managed and owned by Chairman Tae Won Choi and his family (owner-manager), Sovereign asked its incumbent owner-managers to resign from and to reform the structure of board of directors. During the event, the share price of SK rose from about USD 11 to about USD 40. It was reported that Sovereign earned the capital gains of around USD 800 million upon settlement in 2004.

In this paper, we test this hypothesis: if a target company has institutional investors in its ownership, the target's takeover gain would be inversely related to the fraction of target equity held by institutions because the value that the bidder could create would be smaller. The third hypothesis is derived as follows:

H3: The wealth gains of target shareholders decrease, with

large institutional shareholdings due to efficient monitoring.

METHODOLOGY AND SAMPLE

The traditional method of event study (Brown and Warner 1985) is used to estimate the wealth gains of the target shareholders. Daily returns data are used from the Korea Securities Research Institute (KSRI) stock database. The parameters of market model are estimated over the period -250 to -6 trading days prior to the bid announcement day, say, Day 0.

Abnormal returns over an initial observation period, Day -5 to Day +5 (in trading days) around the event day, Day 0, are estimated. To check the stability, abnormal returns over the observation period of Day -1 to Day +1 (in trading days) around the event day, Day 0, are also estimated. The abnormal returns from the market model are averaged each observation day and tested for statistical significance. The daily average abnormal returns (ARs) are then cumulated to yield the cumulative average abnormal returns (CARs) which are tested for statistical significance.

To examine the effect of the agency related explanatory variables on the wealth gains of target shareholders, we regress the CARs to target shareholders as a dependent variable on the explanatory variables for the various ownership measures embodied in our hypotheses and on the control variables.

Sample

The sample consists of mergers and acquisitions for Korean publicly listed companies by other Korean publicly listed companies with an announcement date between January 1, 1996 and June 30, 2007. The deals are identified in the Securities Data Company (SDC) Mergers and Acquisitions database. To be included in the sample, companies must have 250 days' share prices prior to a bid and 5 days' share prices after a bid for both bidders and targets in the Korea Securities Research Institute (KSRI) stock database. The sample should also have all the necessary data for the ownership and control

Table 1. 2 digit SIC of Bidders and Targets

Division	SIC	#Target	#Bidder
Metal Mining	10	1	0
Building Construction General Contractors And Operative Builders	15	2	2
Food And Kindred Products	20	2	3
Textile Mill Products	22	2	2
Apparel And Other Finished Products Made From Fabrics and Similar Materials	23	1	3
Paper And Allied Products	26	1	0
Chemicals And Allied Products	28	7	5
Petroleum Refining And Related Industries	29	0	1
Rubber And Miscellaneous Plastics Products	30	2	1
Stone, Clay, Glass, And Concrete Products	32	2	1
Primary Metal Industries	33	3	3
Industrial And Commercial Machinery And Computer Equipment	35	2	0
Electronic And Other Electrical Equipment And Components, Except Computer Equipment	36	2	4
Transportation Equipment	37	3	4
Miscellaneous Manufacturing Industries	39	1	1
Communications	48	1	0
Electric, Gas, And Sanitary Services	49	1	0
Wholesale Trade-non-durable Goods	51	0	1
Automotive Dealers And Gasoline Service Stations	55	1	0
Holding And Other Investment Offices	67	2	4
Business Services	73	0	1
Total		36	36

variables, and the final sample is reduced to 36. Table 1 exhibits the industries where bidder and target firms belong at the 2-digit SIC. Most of acquisitions have been made within manufacturing industries or SIC of 2 and 3.

Table 2 presents some characteristics of bidder and target firms. The average sale of bidders or KRW 3,238 billion is more than 3 times more than that of targets or KRW 920 billion. Reflecting their temporal disturbance from the Asian crisis, the target firms show negative net income, while the bidders realize positive profits. Due to the depressed stock market, the market-to-book ratios of targets and bidders are close to 1.

Table 2. Firm Characteristics of Bidders and Targets

Targets:

(Unit: billion KRW)

	Average	Stdev	Min	Max
Sales	920	1,445	27	6,382
Assets	1,211	1,980	15	8,953
Net Income	-.2	99	-383	298
Market Cap.	342	1,019	5	5,810
Book Value	269	414	-179	1,872

Bidders:

(Unit: billion KRW)

	Average	Stdev	Min	Max
Sales	3,238	4,644	4	19,012
Assets	3,257	3,760	18	12,518
Net Income	100	355	-146	2,005
Market Cap.	902	1,576	18	7,371
Book Value	972	1,013	13	3,539

Ownership Variables

In this study, the fraction of target shares held by executives, directors and controlling shareholders including 'specially' related shareholders is defined as 'owner-manager ownership' (TGTMGR). 'Institutional ownership' (TGTINST) is the fraction of target shares held more than 1% by institutional investors. Korea Listed Companies Association (KLCA) database reports ownership of officers, directors, controlling shareholders including 'specially' affiliated shareholders, and institutional investors. BID30GRP is a dummy variable equal to 1 if the bidder belongs to one of the top 30 *chaebols* as reported annually by the KFTC. TGTMGR, BID30GRP, and TGTINST are at the end of fiscal year before the bid announcement date as reported in the SDC Mergers and Acquisitions database.

Control Variables

These variables endeavor to capture the important impacts other than target ownership structure. As Cho (2007) maintains,

a crucial aspect for shareholder value creation in the Korean acquisitions between 1996 and 2006 was operational and growth synergy. As suggested by Cho (2007), in order to control the influence from the operational and growth synergy, a proxy for operational synergy (RELATE) and a proxy for growth synergy (GAPGROW) are used, which are defined as below, respectively.

The measure for the operational synergy is RELATE. RELATE is a dummy variable equal to 1 if the bidder and target operate in the same industry at the four-digit level of Standard Industrial Classification (SIC). Unrelated mergers have RELATE = 0.

The measure for the growth synergy is GAPGROW, which estimates the gap between bidder and target in terms of resources (i.e., current assets) and current growth rates in their business. GAPGROW value is larger when the gap between bidder and target is larger.

$$\begin{aligned} \text{GAPGROW} &= (\text{Bidder's current assets} - \text{Target's current assets}) \\ &\times (\text{Bidder's sales growth rate} - \text{Target's sales growth rate}) \end{aligned}$$

If the current assets of bidders are greater than those of targets in the first term above (liquidity-rich bidders) as is the case in our sample, GAPGROW becomes positive when there is a restructuring opportunity by fixing the target's temporal troubles (as measured by the target's lower growth rate) or becomes negative when there is a superior investment opportunity (as measured by target's higher growth rate) to be shared with bidders.

The bid process characteristics are also controlled. 'Bidder ownership' (BIDTOE) is the percentage of target's equity held by a bidder before a bid announcement. MULTIBID is a dummy variable equal to 1 if the target has multiple bidders in the deal process. MERGER is a dummy variable equal to 1 if the deal type is merger. Otherwise, the deal type is tender. CASH is the method of payment offered by the bidder as consideration for the acquisition. Two methods of payment are included: cash and equity. Each method of payment is coded as a dichotomous variable. TIME is a dummy variable equal to 1 if the transaction is announced during 1997-2000 period to control the IMF effect. Otherwise, TIME is 0. The target's market capitalization of equity a priori a bid (TGTSIZE) controls the size effect of targets.

COMPLETE is a dummy variable equal to 1 if the deal is complete. Otherwise, COMPLETE is 0.

RESULTS

The Cumulative Abnormal Returns (CARs) based on the market model for the period Day -5 to Day +5 are used as our measure of wealth gains to shareholders (-1 to +1 shows the similar results). Over the period Day -5 to Day +5, as shown in Table 3, target shareholders earn -1.26%, significant at 1%. As shown in Table 4, the combined value-weighted CAR to the portfolio of bidders and targets in our sample is 0.49% (significant at 1%). As a result, the sample mergers create slight overall value. Considering that bidders gain 1.97% and targets lose 1.26% (significant at 1%), as shown in Table 3, there is a wealth transfer from target to bidder shareholders.

The finding that the target shareholders lose, while bidder shareholders gain is new, unique, and different from the observations in the US-based M&A research. In a recent paper, Cho (2007) claims that during the Asian IMF crisis, "a motive for acquisitions under the turbulent liquidity-scarce environment could be associated with successful firms' growth strategy into related business utilizing their rich cash-base in acquiring

Table 3. CARs for the Top 30 Chaebol Group and Non Top 30

	Targets					Bidders				
	Total	TGT- Top30	TGT- Non30	BID- Top30	BID- Non30	Total	TGT- Top30	TGT- Non30	BID- Top30	BID- Non30
Sample #	36	11	25	23	13	36	11	25	23	13
Average	-.0126	-.0903	.0215	-.0451	.0447	.0197	-.0104	.0329	.0093	.0381
Median	.0160	-.0723	.0262	-.0543	.0431	.0091	-.0249	.0168	-.0003	.0213
Stdev	.1868	.1709	.1863	.1950	.1626	.0940	.0928	.0933	.0965	.0902
Min.	-.4834	-.4834	-.3893	-.4834	-.3133	-.1884	-.1884	-.1069	-.1884	-.0969
Max.	.4028	.1055	.4028	.3895	.4028	.2753	.1022	.2753	.2753	.2492

TGT-Top30 means the target firms which belong to the top 30 *chaebols*.

TGT-Non30 means the target firms which do not belong to the top 30 *chaebol*.

BID-Top30 means the bidders which belong to the top 30 *chaebols*.

BID-Non30 means the bidders which do not belong to the top 30 *chaebol*.

available good targets at cheaper premium". During the period, the Korean M&A market had been extremely favorable to bidders due to the turbulent and liquidity-scarce environment caused by the Asian financial crisis in 1997. In other words, various targets were available at cheaper prices, while there were few qualified bidders. Therefore, targets could have been underpaid, and targets lose.

Characteristics of Ownership and Control Variables

Table 4 provides the descriptive statistics for the explanatory and control variables. Owner-managers own on average 35.7% of equity. Considering that the targets are public firms, the managers' ownership is extremely high on global standards. About two thirds of bidders or 63.9% are among the top 30 *chaebols*. It can be inferred that during 1996-2007 the top 30 *chaebols* are the most active bidders who possess a wealth of cash and take advantage of favorable M&A market conditions. Institutional ownership is 16.4% on average.

Twenty five percent of the sample is related company mergers, i.e., their 4-digit SICs are the same. This suggests that a good portion of acquisitions have been made to achieve a growth strategy of related diversification. GAPGROW is -.282 in Table 4. To interpret it properly, GAPGROW is decomposed as in Table 5. As exhibited in Table 5, the average excess cash over target is KRW 568 billion, and targets' growth rate exceeds that of bidders by about 8% overall. When the sales growth rates of bidders are less than those of targets (investment opportunity), their averages of both differences in growth rates and CARs are -25.75% and -.06%, respectively. On the other hand, when the growth rates of bidders are greater than those of targets (restructuring opportunity), their averages of both differences in growth rates and CARs are 14.22% and 4.92%, respectively. In other words, 44% of acquisitions between 1996 and 2007 have been motivated by the opportunity to restructure temporally troubled companies, and their wealth creation to the shareholders is positive.

Bidder's toehold averages 12.8%. Eight percent of the sample involves competing bids. Thirty three percent are mergers while sixty seven percent are tender offers. Cash payment has been made in forty seven percent of sample transactions. Half of the

Table 4. Descriptive Statistics

	Mean	CART	Value weighted portfolio	Owner-manager ownership	Institutional ownership	Bidder ownership (TOEH-OLD)	BID30-GRP	RELATED	GAPG-ROW	MULT-IBID	MERGER	CASH	TIME	Market value of target equity	
CART	-.013	1													
Value weighted portfolio	.005	.6679*	1												
Owner-manager ownership	.357	-.1001	-.2595	1											
Institutional ownership	.164	-.2809	-.1852	-.015	1										
Bidder ownership (TOEHOLD)	.128	.3118	.2077	.5922*	-.2449	1									
BID30GRP	.639	-.2342	-.2428	-.1873	.3213	-.1488	1								
RELATED	.25	-.0074	-.0725	-.0107	-.032	.0625	.0334	1							
GAPGROW	-.282	.2253	.1603	.018	-.0716	.2736	-.1882	.124	1						
MULTIBID	.083	-.1261	.128	-.0815	.1936	-.1911	.0174	.2901	-.0595	1					
MERGER	.333	-.0042	-.0636	-.1402	.0583	-.133	.0409	0	.107	-.2132	1				
CASH	.472	.2319	.0777	.1851	-.0003	.11	-.0998	-.0321	-.1973	-.0839	-.5508*	1			
TIME	.5	-.1382	-.0242	-.1309	.2144	-.3959*	.1735	-.0642	-.2532	.1005	0	-.0556	1		
Market value of target equity	.342	-.4294*	-.4577*	-.0223	-.0624	-.0999	.2281	.4162*	-.0426	.17	.1286	-.1832	.2333	1	
Complete	.556	-.298	-.2816	.1346	.1708	-.102	.1422	.2582	-.085	.2697	.0395	.0622	.2236	.2123	1

Table 5. Mean on Current Assets, Growth Rates and CARs

Targets (N = 36)

	n	Mean of CA _B *-CA _T **	Mean of G _B ***-G _T ****	Mean of CAR _T *****
G _B -G _T < 0 (Investment Opp.)	20	536 bil.	-25.75%	-.06%
G _B -G _T > 0 (Restructuring Opp.)	16	608 bil.	14.22%	4.92%
Total	36	568 bil.	-7.99%	-1.26%

* CA_B = Current Assets of Bidders

* CA_T = Current Assets of Targets

*** G_B = Growth rate of Bidders

**** G_T = Growth rate of Targets

***** CAR_T = Cumulative Abnormal Return of Targets

Table 6. VIF for Model 4 in Regression

	VIF	1/VIF
Target's owner-manager ownership	1.91	.524837
BID30GRP	1.38	.724215
Target's institutional ownership	1.39	.718856
RELATED	1.45	.688475
GAPGROW	1.28	.779127
Bidder ownership (TOEHOLD)	2.23	.448909
MULTIBID	1.48	.675665
MERGER	1.77	.564709
CASH	1.74	.574669
TIME	1.4	.714058
Market value of target equity	1.51	.660676
Complete	1.34	.744804
Mean VIF		1.57

transactions are announced during the IMF period — between the years of 1997 and 2000. The average market value of target equity is KRW 342 billion. Half of the transactions are completed.

To check the multicollinearity among the variables, the values of Variance Inflation Factor (VIF) are calculated as shown in table 6. The values are less than 2, and thus there is no problem

using these variables in regressions.

The Effect of Target Ownership Structure on the Target Shareholder Returns

Table 7 presents the results of the regression of target wealth gains on the explanatory variables. It shows that our ownership

Table 7. Regressions Using the CARs as the Dependent Variable

Variable	Model 1	Model 2	Model 3	Model 4	Model 5
Target's owner- manager ownership		-.3309** (-2.15)	-.3523** (-2.22)	-.2942** (-1.98)	.2947** (-1.88)
BID30GRP			-.0383 (-.68)		-.0007 (-.01)
Target's institutional ownership				-.2515** (-1.84)	-.2509* (-1.66)
RELATED	.0945 (1.29)	.0773 (1.12)	.0751 (1.08)	.0758 (1.15)	.0758 (1.13)
GAPGROW	.0216 (1.12)	.0169 (.93)	.0146 (.78)	.0183 (1.05)	.0183 (1.00)
Bidder ownership (TOEHOLD)	.2565* (1.70)	.4867*** (2.74)	.4951*** (2.75)	.4270** (2.47)	.4273** (2.40)
MULTIBID	.0795 (.70)	.0824 (.78)	.0761 (.71)	.1163 (1.13)	.1161 (1.09)
MERGER	.1252* (1.70)	.1245** (1.81)	.1212** (1.73)	.1391** (2.10)	.1390** (2.04)
CASH	.1395** (2.03)	.1517** (2.34)	.1470** (2.23)	.1590*** (2.57)	.1589** (2.49)
TIME	.0821* (1.33)	.0890* (1.53)	.0906* (1.54)	.1037** (1.85)	.1037** (1.81)
Market value of target equity	-.0843*** (-2.72)	-.0811*** (-2.79)	-.0773*** (-2.59)	-.0889*** (-3.17)	-.0888*** (-3.00)
Complete	-.1231** (-2.07)	-.0960* (-1.68)	-.0898* (-1.54)	-.0895* (-1.64)	-.0894* (-1.59)
Constant	-.1212* (-1.61)	-.0551 (-.72)	-.0258 (-.29)	-.0379 (-.51)	-.0375 (-.43)
R-squared	.4631	.5470	.5554	.6032	.6032
Adj	.2772	.3658	.3517	.4213	.3961
F	.0333	.0121	.0194	.0068	.0133
Number	36	36	36	36	36

Note: Values shown are unstandardized coefficients. *, **, *** significant at the 10%, 5% and 1% levels respectively, one tailed test.

and control variables have significant explanatory power. For instance, the model 5 shows an adjusted R^2 of 39.61%. Among the ownership variables, target owner-managers ownership (TGTMGR) is significant at the 5 % level, institutional ownership (TGTINST) is significant at the 5 and 10 % level, but the top 30 *chaebol* effect (BID30GRP) is not significant.

The significant negative coefficient of target owner-managers ownership suggests that if more shares are owned by owner-managers in a target firm, more control power would be given to them at the board or higher level, and minority shareholders' intervention in decision-making of selling a company would be difficult or costly. In this circumstance, the owner-managers could decide at their discretion not for all shareholders, but for themselves. Specifically, they may choose to decide for their own interests for the sake of their continued independency or job security. Therefore, the result supports our hypothesis 1a that owner-managers have more incentives for managerial entrenchment rather than alignment with minor shareholders (Ruback 1988; Moeller 2005). The result may imply that in the owner-managers dominated acquisitions the agency framework between owner-managers and non-controlling shareholders is more relevant than the neoclassical framework. It also suggests that the minority-protection systems may be necessary to remedy such inefficiency (La Porta et al. 1999).

The top 30 *chaebol* effect (BID30GRP) is not significant, suggesting that there is no significant wealth creation or destruction in acquisitions when a *chaebol*-owned bidder takes over. Nonetheless, the negative coefficient of BID30GRP indicates that target shareholders lose when a *chaebol* takes over. As shown Table 3, targets lose whenever a *chaebol* takes over (CAR of -4.5%) or whenever *chaebol* targets are taken over (CAR of -9.0%). On the other hand, bidders gain on average (CAR of 2.0%). In table 3, when top 30 *chaebol* bidders acquire a target, the average CAR is 0.9%, which is more than four times smaller when non-*chaebol* bidders do (the average CAR of 3.8%). Although not statistically significant, these observations may imply that the benefits of being a top 30 *chaebol* group, i.e., internal captive market, may be less than the agency costs.

The negative coefficient of target institutional ownership (TGTINST) supports our hypothesis 3 that due to efficient

monitoring in the pre-bid period, the bid premium would be smaller. This result is consistent with Shleifer and Vishny (1986), Stulz et al. (1990) and Slusky and Caves (1991). The result may imply that if necessary, large outside institutional blockholders could intervene in strong owner-management anytime at a low cost, and their efficient monitoring capacity would make the firm value high enough. Upon acquisition, therefore, room for further value creation via acquisitive restructuring would be smaller.

Among control variables BIDTOE, MERGER, CASH, TIME and TGTSIZE are significant. The positively significant impact of BIDTOE may imply that a bidder's action before a bid to accumulate some target shares would signal to the public that the deal is excellent and that there is much more synergy to be realized than known to outsiders. When they know the deal is very attractive because of excellent restructuring opportunities available (Cho 2007), the bidder may want to buy more toeholds when shares are cheaper before the bid. This result is consistent with that of Choudhry and Jegadeesh (1994), which posits an information asymmetry model in which a toehold is a bidder's signal of the post-acquisition value of the target.

Consistent with earlier studies, MERGER and CASH have a significant positive impact on target shareholder wealth compared to TENDER and STOCK exchange offer, respectively. The positively significant coefficient of TIME implies that acquisitions during the IMF period, 1997-2000, are a value enhancing strategic choice for 'troubled' target shareholders (Cho 2007). The negative coefficient of RELSIZE suggests that target shareholders gain when the bidder takes over a smaller target. The smallness of the target enables it to be more easily integrated with the bidder, and thus more premiums could be paid to the target shareholders.

The Effect of Ownership Structure on the Combined Value-Weighted Portfolio Returns

The regression model for the combined value-weighted portfolio returns in Table 8 is significant at 1% with an adjusted R^2 of 49.57%. Among the ownership variables, which include both target- and bidder-related ownership variables, target owner-

Table 8. Regressions Using the Combined CARs of Value-Weighted Portfolio of the Bidder and the Target as the Dependent Variable

	Model 1	Model 2
Target's owner-manager ownership	-.279*** (-3.36)	-.203** (-1.81)
Target's institutional ownership	-.09 (-1.13)	-.097 (-1.13)
Bidder's owner-manager ownership		-.15 (-1.11)
Bidder's institutional ownership		-.04 (-.32)
BID30GRP	-.023 (-.74)	-.021 (-.65)
Bidder ownership (TOEHOLD)	.325*** (3.46)	.307*** (2.86)
RELATED	.014 (.4)	.017 (.47)
GAPGROW	.004 (.41)	.005 (.55)
MULTIBID	.152*** (2.69)	.178*** (2.85)
MERGER	.05* (1.39)	.031 (.76)
CASH	.045* (1.32)	.023 (.57)
TIME	.076*** (2.51)	.066** (1.98)
Market value of target equity	-.054*** (-3.46)	-.056*** (-3.45)
Complete	-.046* (-1.53)	-.042* (-1.35)
Constant	.045 (.99)	.097* (1.43)
R-squared	.6686	.687
Adj	.4957	.4784
F	.0026	.0068
Number	36	36

Note: Values shown are unstandardized coefficients. *, **, *** significant at the 10%, 5% and 1% levels respectively, one tailed test.

managers ownership (TGTMGR) is significant at the 1 and 5% level, respectively. The coefficients of owner-managers ownership (TGTMGR) and institutional ownership (TGTINST) are both negative. Although it is not significant, the coefficient of the *chaebol* effect (BID30GRP) is negative, which indicates that target shareholders could lose when a *chaebol* takes over. These results coincide with those of the preceding model 5 in Table 7, which uses target's CARs as independent variable.

In the meantime, the effect of bidder-related ownership variables, say, bidder owner-managers ownership (BIDMGR) and the institutional ownership of a bidder (BIDINST), is not significant. It may imply that the bidder ownership structure does not create significant value in acquisitions while the target ownership structure does.

DISCUSSIONS

In this paper, using the case of Korean mergers and acquisitions where owner-managers play an important role in making acquisition decisions, the two competing views, the neoclassical and agency view, are examined within the context of owner-managers and non-controlling shareholders. Like much previous literature, our result is favorable for the agency view in that there could be situations when target owner-managers have incentives to deviate from the optimal divestiture-decisions that maximize the benefits of all the shareholders. When a tender is a right choice for all shareholders, for example, managers may choose to decide not to tender for their own interests for the sake of their continued independency or job security.

As for the *chaebol* effect, it is not clear whether the "value-added view" or the "tunneling view" is true. If a target, say, an LCD parts manufacturing company, is acquired to be a member of Samsung Electronics group, for example, is this good or bad news for the target shareholders? The answer may depend on how to evaluate both the possible cost of 'tunneling' and the amount of positive synergy or value the acquisition could create. In our sample, the *chaebol* effect is not conclusive, but the negative sign may reflect the fact that target shareholders do not gain when a *chaebol* takes over.

Given that there is an imbalance of control power in management, favorably for owner-managers and unfavorably for non-controlling shareholders, how could the agency conflict be prevented, reduced or solved? This paper explores the effect of institutional ownership of a target on the takeover premiums in order to examine how effective it could be. The result implies that the presence of (proactive) institutional investors in the shareholding could ensure efficient monitoring of the opportunistic behavior of owner-managers. Assuming that they are more experienced and knowledgeable than individual investors, intuitively, the involvement of institutional investors at the board or share holding level would deter any opportunistic decisions by owner-managers and would improve the quality of corporate governance structure.

In sum, we find evidence that the distribution of target ownership is related to the wealth gains of target shareholders in owner-manager dominant acquisitions. While the agency conflict between managers and shareholders is central in the literature based on the mergers and acquisitions in US, in owner-manager dominant acquisitions, more crucial is the agency problem between owner-managers and non-controlling shareholders. For many Asian public firms including our sample Korean firms, the agency conflict is more likely to arise between controlling shareholders and minority shareholders.

Nowadays, for many Asian public companies, a founder still manages his own company; a founder has a strong emotional attachment for his business he has built from a scratch; sons of the founder or related family members are currently involved in the management; a founder and his family believe that they ultimately own the business; professional managers could be hired, if necessary, but they have to follow 'our' directions; and a son would possibly succeed the founder. Under these sentiments which are quite common in the Asian society, professional managers would not have enough power to disobey the 'owners'. If owner-managers desperately maintain their control power in managing the business, it is likely that the incentives of owner-managers would not always be closely aligned with those of non-controlling shareholders.

Several implications may be drawn from the results. First, from the perspective of legislators, there may be a need to establish

some regulatory mechanisms to prevent potential abuse of minority shareholders. Second, ownership and management may need to be separated more clearly. Requiring some independent outside directors into the board could be one plausible way to resolve this issue. Furthermore, the reinforced role of board of directors with appropriate authorities and responsibilities may enhance the quality and transparency of corporate governance.

As an anonymous reviewer suggests, a major limitation of the study may be its inability to provide evidence for owner-managers' pursuit of private benefits. Although the regression result of the study may 'loosely' imply the owner-managers entrenchment, the interpretation could be a kind of conjecture. In order to rigorously maintain the owner-managers entrenchment hypothesis, some explanatory variables relating to manager entrenchment such as anti-takeover defensive devices should turn out to be significant in the additional separate regression test. Unfortunately, the data for anti-takeover defensive devices are not available in Korea because it is illegal to adopt such defensive devices. One direction of future research could be enhancing the rigorousness of the regression model by including 'observable' explanatory variables relating to owner-managers' pursuit of private benefits.

Another direction may be testing the effectiveness of alternative mechanisms to prevent potential abuse of minority shareholders. For one example, is the ownership of foreign investors effective as claimed once during the IMF crisis? If so, what types (or characteristics) of foreign investors could be more effective? For another example, is it effective adapting of independent outside directors into the board? If so, what characteristics of outside directors could be more effective?

The other direction may be developing further the *chaebol* effect. Although the result of this paper is inconclusive, many of scholars using old data before year 2000 have reported its significant negative influence on the firm value. During 1997-2007 under Kim and Noh administration, however, the quality of corporate transparency and governance structure has significantly improved. At the moment, it seems interesting and rewarding to investigate further whether the *chaebol* effect exists or not. If so, is it still negative?

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Received March 10, 2008

Revision received November 10, 2008

Accepted February 2, 2009