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Target CEO age, ownership decisions, and takeover outcomes☆

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ABSTRACT

This paper examines the effect of target CEO age, in association with target corporate governance mechanisms, on the ownership decisions and takeover outcomes in eight East and Southeast Asian countries. The results show that acquirers are more likely to select partial-control acquisitions of target firms managed by older CEOs, and that the impact of target CEO age on the partial-control acquisition propensity is much stronger in emerging markets relative to developed economies. The study further finds that target CEO age leads to a lower probability of obtaining desired equity ownership levels compared to unmatched ownership achievements, controlling for target corporate governance structures. The findings also run robustness checks regarding variations in the compulsory acquisition cut-off in the sample countries. Overall, this paper adds to the growing of mainstream corporate governance literature regarding the relevance of CEO personal characteristics in agency problems for corporate decisions.

1. Introduction

Since 2000, East and Southeast Asia has experienced a steady increase in M & A activities to levels never seen before with an average increase of about 32% in the 2000–2013, following the fifth takeover wave which started in the late 1990s (UNCTAD, 2014). The main reason for this achievement relates to reforms in the corporate governance and institutional environments (Kim and Lu, 2013). The focus of this study is not on the association between country-level corporate governance practices and takeover activities across East and Southeast Asian countries. Instead, our paper aims at examining the impact of firm-level CEO personal characteristics of target firms on the bidders' ownership choices and takeover outcomes. Accordingly, we ask two questions: (1) What is the impact of target CEO age on the bidders' equity ownership choices and takeover outcomes? (2) What happens to target firms at the time of the acquisition announcement across different CEO age groups?

Deciding on an appropriate ownership level is one of the most important strategic decisions of firms in acquisitions. Given a chance to purchase another partner, the acquirers have the choice of obtaining a minority ownership position (less than 50%), or purchasing more than 50% but less than 100% ownership (partial-control), or obtaining 100% ownership (full- control) of the acquired firm. The existing literature has provided a vast amount of research that has indicated that the acquirers' acquisitions drivers can differ across equity ownership levels from the perspective of the bidders (Maksimovic and Phillips, 2001; Fee and Thomas, 2004; Ouimet, 2013; and Liao, 2014), and from the perceptions and attributes of target firms (Dang and Henry, 2016).

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This study adds to the growing literature regarding the relevance of CEO personal characteristics in agency problems for corporate decisions through examining whether target CEO age can explain the drivers and outcomes of equity ownership decisions and value creation to target shareholders. Yim (2013) and Serfling (2014) examine the association between bidder CEO age and risk-taking behaviour in acquisitions, and find that younger CEOs tend to make more acquisitions while older CEOs pursue less risky acquisition opportunities, suggesting that high-risk takeover deals decrease as CEOs become older. From the target firm's perspective, Bargeron et al. (2009) and Graham et al. (2013) find that target CEOs play an important role in target firm decisions in the control and takeover space, such as seeking out a bidder or making negotiations with bidders. This suggests that full-control acquisitions may have serious setbacks to target CEOs' careers as target CEOs commonly lose their jobs after a merger and, hence, the target CEO may resist a full-acquisition bid in an attempt to keep his job. However, little work has been done on whether CEO age of the target firm affects the bidder's equity ownership decisions in acquisitions. This study, therefore, will shed additional light on the impact of unique CEO personal characteristics on corporate strategic decisions in the context of acquisitions.

In terms of the nature of knowledge and the nature of society, as indicated by Burrell and Morgan (1979), there are four paradigms for the analysis of social theory: radical humanist, radical structuralist, interpretive and functionalist. The four paradigms are mutually exclusive as they provide alternative views of social theory. Specifically, each paradigm is built upon a narrow set of metatheoretical assumptions, which offers the different ways of reviewing the society. By extension, the financial world can be analysed from different perspectives and that a given theory can only be considered valid within the boundaries of implicit paradigmatic assumptions (Lagoarde-Segot, 2016). In terms of modern finance, we assume that social world is made up of stable, tangible entities which are autonomous and external to the observers. Thus, they can be identified through the study of causal mechanism and the properties of the whole society can be determined by the properties of the sub-part (Lagoarde-Segot, 2016).

Based on underlying assumptions of the mainstream academic finance theory and practice (functionalist paradigm),[1] our work observes the phenomenon and identified the order that prevails within that phenomenon via the rigor and technique of the scientific method (econometric methodology). Thereby, this study first finds that, controlling for target corporate governance structures, bidders consider target CEO age when deciding the level of desired acquisition ownership, and that targets with older CEOs are more likely to be sought in partial-control rather than through full-control takeovers. This finding supports the prediction that target CEO age is a significant predictor of the equity ownership decisions in takeovers. Interesting, the paper implies that the correlation between target CEO age and the partial-control acquisition propensity is much stronger in emerging markets relative to developed economies. Our study also shows a positive correlation between target CEO age and the probability that a partial-control ownership outcome is achieved after the transaction. We further find that target CEO age leads to a lower probability of achieving desired equity ownership levels compared to unmatched ownership outcomes. The central contribution of this paper is the expansion on prior empirical studies by Yim (2013), Serfling (2014), Jenter and Lewellen (2015), and Dang and Henry (2016), both to a new regional setting and one where partial acquisition transactions are particularly prevalent, and identifies CEO age as an important factor potentially affecting corporate decision-making in general and acquisitions-related risk-taking behaviour in particular.

In terms of the target firm gains, the results show that target firms with the oldest CEOs (59 or more) experience the lowest abnormal returns, while target firms led by the 53–58 age group CEOs gain the highest returns. This finding is in line with the idea that when target CEOs feel that retirement is close they act in a manner that maximizes their private benefits before they leave the firm, leading to lower returns to target shareholders.

The rest of the paper is organized as follows. Section 2 elaborates on the institutional setting around which the paper is based, provides a review of the existing literature, and the related hypotheses are also developed in this section. Section 3 describes the sample, while Section 4 discusses the research methods. Section 5 reports empirical results, and Section 6 concludes the paper.

2. Theoretical background and hypotheses

2.1. Institutional setting and environment

As a starting point to the paper development, it is pertinent to address relevant institutional and environment aspects. This examination can be divided up along a number of dimensions. Firstly, the regional focus for the paper is East and Southeast Asia. This provides a particularly useful and attractive setting to analyse issues relating to agency theory, corporate decision-making and control. The attraction is that this represents a region of close geographical proximity, but which has a mix of countries at very different points of the development cycle. The region encompasses highly developed and leading world economies (such as Hong Kong and Singapore), countries which have experienced significant recent growth and emergence (such as South Korea, Taiwan and Malaysia), and countries that are still very much at the developing economy level (Indonesia, The Philippines and Thailand). This is expected to result in empirical examination of companies with differing size and scale, degree of international integration, prevailing economic conditions, growth profile, and ownership and control characteristics.

Secondly, and particularly relevant to this study, is the firm- and country-level corporate governance environments. Corporate governance practices in the Asian region generally were significantly strengthened following the 1997 Asian Financial Crisis, as the existence of sub-standard corporate governance systems was identified as one of the underlying causes of the crisis event. Dang and Henry (2016) indicate that, consistent with country development status, developed economies such as Hong Kong and Singapore

[1] One should know that the results of sophisticated mathematical models used in this paper may change as the underlying assumptions of mainstream corporate governance are changed (see Ardalan, 2008, 2017; Lagoarde-Segot, 2016).