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Value Impact of Debt Issuances by Targets of Withdrawn Takeovers

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Abstract:
Existing finance theory predicts that managers of takeover targets will increase leverage to enhance managerial control which can, in turn, allow target managers to thwart a takeover attempt altogether. We find that targets significantly increase leverage, by not only issuing more debt, but also by repurchasing more equity. We also find that debt issuances by poorly performing target managers made between takeover announcement and withdrawal result in significantly negative abnormal returns at the time of the issuance, consistent with the entrenchment role of debt. On the other hand, debt issued by high-performing target managers is not found to result in these same negative returns. Additionally, we document that debt-increasing, poorly performing targets experience significantly more negative returns at withdrawal announcement, also followed by significantly negative post-withdrawal stock performance, while these negative effects are offset for high-performing targets. Overall, our findings suggest that managerial motivations to block takeover attempts with increased debt issuance differ and that these differences in motivation are recognized by the market.

Keywords: Debt issuances, Bank debt, Mergers and Acquisitions gains
JEL Classification: G32, G34

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