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Advising Shareholders in Takeovers

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Abstract

This paper studies the advisory role of the board of directors in takeovers. I develop a model in which the takeover premium and the ability of the target board to resist the takeover are endogenous. The analysis relates the influence of the board on target shareholders and the reaction of the market to its recommendations to various characteristics of the acquirer and the target. I also show that the expected target shareholder value can decrease with the expertise of the board and it is maximized when the board is biased against the takeover. Generally, uninformative and ignored recommendations are not necessarily evidence that the target board has no influence on the outcome of the takeover. Perhaps surprisingly, under the optimal board structure, target shareholders ignore the recommendations of the board, which are never informative in equilibrium.

KEYWORDS: Board of Directors, Communication, Corporate Governance, Free-riding, Takeover.

JEL CLASSIFICATION: D82, D83, G34

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