DO TRADE SALE PRIVATIZATIONS IN EUROPE CREATE VALUE TO SHAREHOLDERS OF ACQUIRING FIRMS?

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Abstract

Many authors have identified zero to negative announcement returns for acquirers in traditional mergers and acquisitions. When purchasing state-owned enterprises as compared to public assets the acquirer faces one particular difference: the distinct characteristics of the seller. The selling government is assumed to lack bargaining power and experience selling off its assets and also often to consider non-economic objectives when privatizing. Furthermore it has a tendency to privilege domestic acquirers. By conducting standard event study methodology and analyzing 90 European trade-sale privatizations we document that acquirers in a privatization context yield significant positive abnormal stock returns.

Keywords: mergers and acquisitions; privatization; event study; acquirer

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1. Introduction

Since the first privatization program initiated by the government of Prime Minister Margaret Thatcher in the United Kingdom at the beginning of the 1980s, the sale of state owned enterprises (SOEs) has become an important objective for many governments throughout the Western world. According to Brune, Garret and Kogut (2004), in the period from 1990-2002 governments of OECD countries generated revenues of US$ 649bn through privatization. Globally, during the period of 1985-1999, more than 8,000 transactions, valued at over $1.1 trillion, were documented. Over the next 20 years this trend will likely continue to grow and over $6 trillion in privatization assets will be sold (Shafik, 1996). While the majority of privatizations during the last decade were conducted through public offerings, governments recently were increasingly selling its assets directly to strategic or financial investors due to volatile and uncertain market environments (OECD, 2002). From a mergers and acquisitions (M&A) perspective as well as from the focus of a shareholder value maximizing management this poses the question whether capital market reactions of bidder stocks in the case of trade-sale privatizations behave different from privately held M&A targets. And if so, do they lead to different valuations of the acquirer, i.e. do shareholder wealth gains differ?

There is good reason that they should indeed differ. When attempting to purchase a state-owned enterprise as compared to a public or private target, the acquirer faces one difference in particular. The selling party is not the target holding company's or the target company's management but the government. As the negotiating party, the government has distinct characteristics which might influence the valuation of the acquiring party. The government usually is assumed to lack experience in selling its assets and also is believed to have lower bargaining power than other selling parties. Also, while a government mainly privatizes out of an economic rational, political or social objectives could additionally drive the decision to privatize. Taken these factors into account, we argue that acquirers in a privatization context are in a superior position and should hence be rewarded with sales prices which are below fair-value leading to an increase in shareholder wealth. Although mergers and acquisitions in general have received wide attention in academic literature, research concerning trade-sales privatizations is limited. To our knowledge, the proposed questions have not been addressed so far. To provide additional insight into the role of governments as the seller and to show whether bidders benefit from privatization acquisitions, we examine the stock market's perception of trade-sale privatization in Europe in the period from 1989 to 2003. Using daily stock return data we address two issues. First, does the stock market positively revalue bidding firms after announcing the acquisition of a state owned enterprise? Second, what other factors influence the revaluation? To this end, the paper is organized as follows. In *Section II*, important theoretical aspects of mergers and acquisitions within the context of privatizations are developed to provide a thorough foundation for the following empirical analyses. Also, a short review of empirical studies about shareholder wealth effects to acquisitions is presented. In *Section III*, the empirical study about announcement effects of trade-sale privatizations to the acquirer's shareholders is presented.

2. Theoretical Considerations and Empirical Review

2.1 Theoretical Considerations

Privatization, in the following understood as the transfer of ownership and control from the government to private investors (e.g. Megginson et al, 2004; Vickers and Yarrow, 1991), via the direct sale to private investors has yet received little attention in academic literature. However, conceptual differences seem to exist. The shift from state to private ownership inherent in privatizations suggests differences in the acquisition process implying specific market reactions to these acquisitions. As proposed by Uhlenbruck and De Castro (1998), compared to traditional mergers and acquisitions, the three involved parties SOE, government and acquirer do not only differ in their characteristics and objectives, but to the most extent in their interplay. In the following, different characteristics of and objectives for the target and acquiring firm are briefly described. It is discussed why these differences per se – under the assumption of efficient markets – should not result in shareholder wealth gains to the acquirer deviating from those observed in "traditional" mergers and acquisitions. It is argued that it is only the involvement of the government as the bargainer in particular which causes the proposed differences.

Evidently, in trade-sale privatizations the target significantly differs from "traditional" private targets. One key difference is the often inefficient performance of state-owned enterprises. In general a different *ownership* structure and the lack of *competition* are cited as causing these inefficiencies (Boycko, Schleifer and Vishny, 1996; Vickers and Yarrow, 1991; Wallstein, 2001). Shirley and Walsh (2000) argue, for example, that management of SOEs is not as effectively monitored since there is no risk of a takeover when performing poorly. Also, several empirical studies indicate that lack of market competition induces less efficient management and performance of SOEs (Peltzman, 1971; Jones, 1985). These instances should result in particularly high synergies through the inherent transfer to capital market funding and competitive product markets in trade-sale privatizations. In efficient markets, however, the selling party will also require an adequate price for these potential synergies and hence, valuation consequences – i.e. positive or negative announcement effects caused by a deviation from the target's fair value – should not differ from traditional mergers and acquisitions as long as the selling party does not differ in its capability to evaluate the target's fair value.

As concerns the bidding firm in trade-sale privatizations, there is no reason to believe why the rationale for acquisitions should differ from those of other acquirers. Also, there is no evidence that acquirers of state-owned enterprises differ in their firm characteristics. *Profit-maximization theory* suggests that management considers corporate takeovers as a way of increasing profitability and creating shareholder wealth (Manne, 1965). Literature names synergistic effects as one of the major reasons for takeovers (Bradley, 1980; Jensen and Ruback, 1983; Berkovitch and Narayanan, 1993). Also other financial considerations might cause managers to engage in takeovers. Halpern (1983) for example argues that asymmetric information regarding the value of the target firm might lead to the purchase of a possibly undervalued firm, thus creating value through buying a corporation at a price lower than its actual fair value. While these rationales should also hold within the context of privatization, the specific possibilities of how to create or capture this (shareholder-) value might be distinct. As Uhlenbruck and De Castro (1998) argue the acquirer often has the possibility to enter completely new and most of all underserved markets when acquiring a SOE. However, this per se shouldn't yield in any different valuation compared to traditional acquirers as it should also be adequately reflected in the sales price.

Considering that the selling party in the context of trade-sale privatizations is the target's countries government, there seems to be a fundamental difference as compared to other mergers and acquisitions. Both characteristics and objectives of the selling party are distinct and deserve a thorough discussion in order to understand trade-sale privatizations and its immediate effects on the bidding shareholders' wealth upon the announcement of an acquisition. As compared to private targets, the selling and negotiating party in privatizations can be assumed to be less experienced. While it is common for private firms to participate in the market for corporate control and buy and sell assets as a means of growth or restructuring, governments are rarely involved in doing so. More importantly, not only does the government itself lack experience in disposing its assets, but furthermore, overall experience in selling state-owned property is lower than in the regular market for corporate control. Scarcely can a government revert back to experience from other disposals. Drawing on own experience from former sales is difficult since these are only comparable if within the same industry. Also, privatizations in other countries are difficult to compare since they occur under distinct political and institutional conditions. For these reasons the governments even with the help of financial advisors can be assumed to have its difficulties in assessing and evaluating the value of changing ownership structures and introducing competition. While the acquirer arguably is in a similar position and at least also lacks comparable transactions to correctly price for example potential synergies the bidding firm is still in the better bargaining position. The success of a privatization program to a large degree depends on a expeditious and smooth overall process. When a government decides to sell state owned assets, this is usually publicly known and a failure of negotiations might go along with the connotation of the offered assets being

of bad quality. The selling government therefore should tend to prioritize a frictionless overall privatization process at the expense of generating less revenue for an individual asset which leaves the acquirer in a better negotiating position. In addition, a government's efforts to privatize are not always entirely driven by economic objectives and thus the sales price is not always key decision variable for the government. Brandt, Li and Roberts (2001) state that governments privatize in order to directly or indirectly benefit from the revenue generate by the sale of state owned property or from the decreasing burden of subsidizing inefficient SOEs respectively. The findings of Bortolotti, Fantini and Sinisalco (2003) who document that governments with stressed fiscal or economic conditions privatize more than governments in healthy fiscal situations further support this argument. López-de-Silanes (1997) even showed in an empirical investigation that in 98% of all privatized SOEs the price which was offered by the acquirer motivated the decision to choose the appropriate acquirer party. However, a government might also have other objectives than raising revenues when privatizing. Regulatory motives might at least complement pure economic rationale when privatizing SOEs. This might include the promotion of competition to an entire (prior monopolistic) industry usually occuring when the government combines privatization with the promotion of competition by reducing or abolishing the legal barriers to enter a certain market sector. Furthermore, it can be argued that governments are rather willing to sell to domestic corporations and thus may charge a higher price for foreign acquirers or give domestic acquirers other advantages throughout the sale process. First of all, the overall goal of the government involves more than simply maximizing revenue, it has a social responsibility. The government has to ensure the adequate supply with certain goods such as electricity or water. Therefore, the government will be more willing to sell to domestic companies to be able to ensure this supply and retain appropriate control mechanisms. Also, privatization involves regulated industries in which the government, even after the sale, has control over the corporation in the form of passing new laws. In this context, the government will also favor domestic corporations to ensure maximum control. Furthermore, a patriotic aspect should not be neglected. Corporations with strategic importance or corporations within an important or prestigious industry will therefore also be rather sold to domestic corporations then to foreign acquirers. Summarizing, the particular characteristics and objectives of the selling party involved in trade-sale privatization leave the acquirer in a better bargaining position which should result in sales prices better than in traditional mergers and acquisition. As Uhlenbruck and De Castro (1998) argue, for example, purchasing a SOE at a potential discount is very likely since the government might lack market-driven parameters and also be facing internal and external economic and political forces, pushing it to sell below market value. It is therefore proposed that acquisitions in trade-sales privatization lead to positive revaluations after the announcements of such acquisitions and that these revaluations are higher than for "traditional" acquisitions. However, since governments are assumed to prefer selling to domestic firms, these negative deviations from the fair value should to a larger degree persist for domestic acquirers.

2.2 Empirical Review

Despite a myriad of empirical literature analyzing shareholder wealth effects of mergers and acquisitions, to our knowledge there is no study examining the announcement effects following acquisitions of SOEs. However, a review of existing studies concerning "traditional" mergers and acquisitions is necessary in order to understand how acquisitions are generally perceived by the capital markets and to be able to compare these perceptions to acquisitions within a privatization context.

In an analysis investigating the effect of merger bids on share price returns Asquith (1983) analysis abnormal stock returns throughout the entire merger process for both successful and unsuccessful mergers. He shows that bidding firms earn small but insignificant initial returns. Similarly, in analyzing 1,800 UK takeovers in the period from 1955 to 1985, Frank and Harris (1989) document that acquirers earn zero to moderate positive initial returns around the announcement of a takeover. In a study conducted by Malatesta (1983) bidders shareholders are reported to significantly lose when acquiring a (public) company. Instead of using percentage stock price returns, he uses abnormal dollar returns to analyze effects on the acquiring companies. He finds that shareholders of acquiring firms suffer significant wealth losses both immediately before and well before a merger. He concludes that acquisitions are negative net present value projects for the acquirer.

In a study conducted by Fuller, Netter and Stegemoller (2002) returns to shareholders of acquiring firms making five or more successful bids within three years between 1990 and 2000 are analyzed. Using a sample of over 3,000 takeovers, they show that bidding shareholders on average significantly gain when acquiring private firms but lose when a public enterprise is purchased. To our knowledge this study is the first to demonstrate that the target's legal form has a significant influence upon the success of the transaction. In analyzing bidder firms which acquired various enterprises over a certain time period they are able to attribute the returns to the acquirer solely to the transaction characteristics. They argue liquidity is the reason for differences when acquiring public or private companies. Private firms are less attractive since it is more difficult to buy and sell enterprises in a relatively illiquid market. Thus, bidder shareholders

receive higher returns since the valuation of those assets reflects a liquidity discount.

Furthermore, Chang (1998) analyzes the relationship between announcement effects of bidders and the method of payment for takeovers of privately held targets and compares them to acquisitions of public targets. He finds bidders who pay with common stock experience positive abnormal return and bidders who pay with cash earn zero abnormal returns when acquiring private companies. This observerd relationship is reversed when acquiring public companies. He argues that the acquisition with stock creates large outside blockholders serving as effective monitors of managerial performance. To test his thesis he separates his sample by whether or not new blockholders emerge. He reports evidence for his thesis and shows that abnormal returns in the case of the emergence of a blockholder are significantly higher. Although this effect can be created for both private and public targets, the creation of a blockholder is more likely with private targets since public targets generally have less concentrated ownership. These findings are interesting and serve as one possible explanation for differences in returns to bidder shareholders when acquiring private targets as compared to public ones. However, in the special case of the target company not only being private but also state-owned, this effect is not very likely. For several reasons, stock is not very likely to be the medium for pay. First, the selling government often has fiscal reasons for privatization and thus will claim a cash payment. Also, the acquiring firm most likely prefers paying with cash since a stock payment would likely be creating a large state-run blockholder.

Summarizing, returns to shareholders of acquiring companies seem to be positive when acquiring private targets for the reasons that they can be acquired at a (liquidity) discount and lead to the creation of a blockholder. While the first argument should also apply in the context of trade-sale privatizations, the second argument does not hold since the method of payment in privatizations is usually cash. Consistent with this argument, in the analyzed sample only 7 transactions where (partially) financed with stock. On the other hand, when acquiring public targets, bidder shareholders seem to lose. It has to be noted however, that estimating bidder returns has its difficulties. First, even value-creating acquisitions might have no observable impact on the bidders' stock price if targets are small relative to the bidder. Second, the stock price reaction to an acquisition can only represent the surprise component of the acquisition. If a bidder is known to be engaging in an acquisition strategy, the stock price reaction to any acquisition announcement will only represent how the market perceives that acquisition to be different from the anticipated acquisition.

3. Announcement Effects to Acquirers of State-Owned Enterprises: Empirical Evidence

In the particular context of privatizations, the target's government as a seller plays a key role and might have significant impact on the success of the acquisition and thus on the returns to acquiring shareholders. It could be argued that the state as the seller is in a rather disadvantageous negotiation position since it is usually publicly know that each particular sale is only one part of an intense privatization program. The state is under the pressure to successfully manage each particular sale since negative publicity could cause the overall privatization program to come to an end. Hence, the acquirer in a privatization context seems to be in a better position than in a regular mergers and acquisition context. Surprisingly, no empirical research concerning the announcement returns of acquirers of state-owned targets is yet available. The presented study therefore attempts to bridge this gap and analyses how the capital markets react towards the announcement of the acquisition of SOEs.

3.1 Data sample

For further investigation of the previously outlined hypotheses, a transaction sample from the Thomson Financial Securities Data™ (TFSD) Mergers & Acquisition database was drawn. The initial sample contains 568 European transactions both bidder and target headquartered in Western Europe, which were announced and completed in the period from 1985 to 2003. Relevant market data for each firm and the market index are taken from the DataStream database. The following criteria had to be met:

- Announcement date is known
- Transfer of ownership of more than 50%
- Deal value is known and above $25m
- Method of payment is known
- Deal can be classified as either cross-border or domestic
- Historic stock market data on the acquirer is available from DataStream
- Stock of the acquirer is regularly traded (liquid)

Our final sample includes 90 transactions fulfilling the above stated criteria. Table 1 and Figure 1 give an overview about the average deal sizes and number of transactions per year. The overall sample has an average deal value of $572m ranging from $27m to $7,457m and contains companies from 15 target countries and 16 acquiring companies. The average market value of the acquiring enterprises is $5,263m ranging from $24.65m to $43,395m. The sample data contains acquisitions from 1989 to 2003 with 1996 being the most active year with 12 transactions and 1989 and 2003 the least active year with one transaction each. Table II shows the average transaction value by target and acquirer country (Panel A) as well as industry (Panel B). Panel B

indicates a concentration on three main industries namely Manufacturing, Transportation, Communication, Utilities and Financial Institutions, this concentration holds for both target and acquirer firm.

3.2 Methodology

We apply event study methodology to estimate the wealth creation to bidder shareholders (see e.g. Fama et al., 1969; Brown and Warner, 1985). We estimate market parameters using country indexes corresponding to each acquirer's nation.[1] As estimation period for the market parameters of each stock j a window between 250 and 40 days before the event date is chosen. Applying the market model, the abnormal return is calculated as follows:

$$AR_{jt} = R_{jt} - (\alpha_j + \beta_j Rm_t) \quad (1)$$

Where AR_{jt} is the abnormal return of stock j of the acquiring company for day t and R_{jt} is the actual observed return of stock j for day t. The bracket term is the expected return of the market model. We calculate abnormal returns for the intervals [-20;10], [-10;10], [-5;5] and [-1;1] around the event window. The cumulated abnormal returns (CAR) for the different event windows [t1;T] and the average abnormal daily returns (AAR) of event day t are calculated as follows:

$$AAR_t = (1/n)\sum_{j=1}^{n} AR_{jt} \quad (2)$$

$$CAR_j = \sum_{t=t_1}^{T} AAR_{jt} \quad (3)$$

Where t_1 is the first day and T is the last day of the event window. In addition, the method used by Malatesta is applied, using cumulated abnormal dollar returns (CADR) to determine the actual absolute wealth effect to the acquirer. This is done by multiplying abnormal returns with the market value of the respective acquirer. Average abnormal dollar returns and cumulated abnormal dollar returns are then calculated as presented in equation 1 and 2. Market value 40 days prior to the event is used to adjust for changes in market value induced by the event itself. This method partially overcomes the problem that even value-creating acquisitions might have no observable impact on the bidders' stock price if targets are small relative to the bidder.

4. Results

Table III reports average cumulated abnormal returns in relative and absolute terms. Panel A shows cumulated abnormal returns for various periods. The results do not provide evidence that acquirers of state owned targets achieve significant positive abnormal returns for a short period around the announcement date. For all periods symmetrically around the announcement day as well as pre-event periods positive CARs can be observed. However, results are not statistically significant indicating that on average trade-sale privatizations do neither result in an increase nor a decrease in shareholder wealth in relative terms. Interestingly the observed positive CAR disappear for the post event period. Cumulative abnormal dollar returns are reported in Panel B. Contrary to relative returns for all periods absolute returns to acquiring shareholders are negative. Also, these are statistically insignificant. To analyze the development of CARs and CADRs during the period under investigation, Table IV shows announcement returns for two subsamples. For the announcement date of an acquisition there is a statistical significant indication for higher returns in the period between 1996–2003. Other periods do not show any significant differences however. In total, an analysis of average cumulated abnormal returns – both in relative and absolute measures – does not provide evidence for our hypothesis that bidder of state owned targets achieve significant positive abnormal returns around the announcement of an acquisition. Table V divides the sample into "domestic" and "cross-border" transactions. For period [0] results show evidence that domestic acquirers gain more than foreign acquirers when announcing the purchase of state owned enterprise. Both, CARs and CADRs are higher for domestic acquirers and statistical significance is also given. These results indicate that governments indeed seem to favor domestic acquirers and reward them with better prices resulting in better revaluations for the acquiring firm. However, contrary results for the post announcement period indicate that these positive revaluations are possibly due to an overreaction of investors. To provide additional insights and to add to our contrary findings so far we examine announcement returns of acquirers with a multivariate regression analysis.

4.1 Multivariate Analysis

To provide additional insights, we analyze the cross-sectional determinants of trade-sale privatizations initial returns. We use four explanatory variables and additional three control variables to ensure robustness of results. See *Table VI* for an overview.

As discussed, the selling government should have a significant impact on the terms of contract thus influencing the overall success of an acquisition. Hence, three variables controlling for this influence are introduced. The first explanatory variable used is the level of the target's government public debt. The fiscal condition of the selling government might influence its decision to privatize and most likely influences the initial objective for privatization, i.e. the need for cash flow generation. As a variable for public debt, the ratio between net financial liabilities and GDP in the year of transaction is used.

[1] Transactions are clustered by acquirer nation. A country index is then assigned to each cluster resulting in 16 different country indexes.

Additionally, a binary dummy variable "cross-border" is included to examine the difference between domestic and cross-border deals and their effect on shareholder wealth. It is hypothesized that a negative cross-border effect should exist since the government should prefer selling to domestic firms. However, as Uhlenbruck and De Castro (1998) note governments might also sell to foreign enterprises as a means of capturing foreign managerial and technical know-how from superior developed countries. While this might certainly be true, it should not be evident in the analyzed sample since only western European countries are analyzed for which a rather equal development can be assumed. To test this, the Human Development Index (HDI) published by the UN is used as a proxy. The HDI is a comparative measure of education, literacy, life expectancy and poverty of an economy. In order to measure the differences in development between the target and the acquiring country, the absolute difference between the acquirer's country HDI and the target's country HDI is included into the model. Furthermore, the business relation between target and acquirer is included as a variable since in the context of trade-sale privatization the acquirer might significantly benefit from the entry into new, previously monopolistic, markets. Business relation is tested using the first two digits of the SIC-code classification. The binary variable takes a value of "1" if the businesses are related (i.e. the first two SIC-codes are identical). To ensure robustness of results, three variables controlling for certain transaction specific effects are included. The percentage of equity acquired is included as a proxy for power of control transferred to the acquirer. Finally, two transaction specific variables, the natural logarithm of transaction size and the natural logarithm of the ratio of transaction size and acquirer size are included. Note that method of payment has been subject to various studies and is often included as a variable as it is said to have high explanatory power. However, in the context of trade-sale privatization, the sole method of payment is generally cash which is also reflected in the examined sample.

Multi-factor analysis is conducted using cumulated abnormal returns in relative and absolute terms for the time period of one day around the announcement day. We estimate four different models. In models 1a and 1b the dependent variables is the CAR of the [-1;1] event period. Models 2a and 2b use alternatively the CADRs of the [-1;1] period as the dependet variable. The estimated four models are presented in *Table VI.* Panel A reports regression results for Models 1a and 1b. Surprisingly Model 1a indicates a positive cross-border effect. International deals seem to create more value for bidding shareholders as the coefficient is positive and statistically significant at the 90% level. This contradicts our hypothesis of governments preferring domestic acquirers and is somewhat puzzling. As presumed Model 2a shows that differences in country development cannot explain this effect since the difference between the human development indexes of both countries does not have any explanatory power within our model. How then can this observed cross-border effect be explained? It could be argued that the capital market perceives cross-border trade-sale privatizations as a valuable means of geographic diversification. The chances to enter new and often underserved markets might outweigh the risk of being charged a high price by the foreign government. Also, other traditional theories for positive cross-border effects such as internalization or asset sharing could serve as explanations. As regards the other variables of Models 1a and 1b no significant effect can be observed. Panel B shows CADR as the dependent variable. Results indicate that weighting cumulative returns by the firm's respective market value yields more robust results. For both models, the overall model fit and the adjusted R^2 is higher. Intercepts are positive and statistically significant for both models indicating that acquirers on average significantly gain after announcing a purchase of a state owned entity. This provides evidence that in the context of privatization when adjusting for several transaction specific variables acquirers indeed gain shareholder wealth. The stock market seems indeed to positively revalue bidding firms after announcing the acquisition of a state owned enterprise. However, there are several factors impacting these revaluations. Contrary to our prior discussed findings the puzzling positive cross-border effect cannot be observed. Also differences in human development do not show any significant results.

However, the level of a target's government public debt negatively affects shareholder wealth. The higher the level of public debt relative to gross domestic product, the more decreases the shareholder wealth to the acquirer. This shows that the success of an acquisition in the context of privatization is to a large degree dependent on the overall target country's condition. A possible explanation for the identified negative relationship between the level of public debt and the shareholder wealth creation to bidders could be the following. A government which suffers from high debt levels might privatize mostly out of fiscal reasons. Introducing competition to a monopolistic industry or increasing efficiency through the change of ownership is not its rational. The capital market might therefore question the sustainability of the decision to privatize and fear that it is only temporary and political conditions might change unfavorably in the course of time. Henceforth, shareholder wealth to acquirers is negatively affected by the level of public debt. Furthermore, the target's company business is affecting bidders' shareholder wealth. An acquisition of an unrelated business creates significantly more value than acquiring a related business. This finding suggests that investors benefit trade-sale acquisitions as a means of diversification. This is surprising, since literature suggests that horizontal acquisitions are viewed to be value-creating since the resulting synergy gains are considered to be large (see e.g.

Eckbo, 1983). Fee and Thomas (2004) argue for example, that improved productive efficiency and buying power are the main sources of gains to horizontal mergers. However, in the context of privatization, an acquisition particularly yields possibilities to enter new, often previously underserved markets. Hence, acquiring a non-related target can be interpreted as entering a new market in a comparable cheap way. This suggests that in the context of privatization it is not so much the potential for synergies but more the possibility to acquiring undervalued assets that is thought to create shareholder value.

Surprisingly, the percentage of stake acquired by the bidder has a negative effect on shareholder value. The coefficient for "% of acquisition" is negative and statistical significant. Traditional literature suggests, that the higher the amount of control, the higher the potential for gaining from the acquisitions. However, in the context of privatization, there might be one possible reason for the negative impact of control. Newberry (1997) argues that in the context of regulated industries an acquisition is rather a transfer of ownership than one of control even if the majority of voting rights is captured by the acquirer. This is due to the fact that in a regulated industry sector the government still has the power to intervene and thus can hinder a complete transition towards a competitive market. A further argument for the negative wealth effect of increased control over the target could be that the market considers it to be positive if the government remains an important shareholder in the company since this is could be an indication for the importance and the quality of the sold asset. However, analysis indicates that even if an acquirer purchases a 100% stake in a state-owned target, bidder shareholder can still gain from this transaction. Summarizing, the analysis yields ambiguous results. No clear finding is available on whether or not shareholders of acquirers of state-owned targets gain from such acquisitions. However, results indicate that – unlike in "traditional" acquisitions – shareholder wealth does not decrease, but is at worst unchanged. Furthermore, the analysis shows that especially the selling government and its relative position to the acquirer's government are highly influential on the positive outcome of an acquisition.

5. Conclusion

This paper analyzes the topic of privatization under a mergers and acquisition perspective. While the majority of privatizations during the last decade were conducted through public offerings, governments recently are increasingly offering its assets directly to investors. From a mergers and acquisition perspective this poses the question whether or not these trade-sale privatizations differ from "traditional" mergers and acquisitions. We argue that they differ indeed due to the distinct characteristics of the selling party – the government. The government not only lacks own experience with selling its assets through mergers and acquisition but also cannot revert back to experience from privatization programs in other countries due to the special political, economical and social distinctions between countries. This makes determining the fair value of the assets difficult for both the government as well as the bidding firm. Additionally, the government's objectives when selling its assets are not solely economically but also political or socially motivated. This in total leaves the government in a worse bargaining position as compared to private sellers. We therefore argue that the capital market should perceive trade-sale privatizations positively which should result in positive abnormal returns to the acquiring firms. While a univariate analysis cannot provide evidence for this thesis and at bests indicates zero abnormal returns, a multivariate analysis shows that positive announcement returns indeed can be observed when adjusting for other transaction characteristics. We find a positive cross-border effect for relative announcement effects which contradicts our proposition that the selling government favors domestic transactions. Also, we find that government liabilities, industry relation and the percentage of equity stake acquired all negatively affect announcement returns to the acquiring company.

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Appendices

Table I. Transaction value by year of trade-sale privatization

This table shows average transaction values denominated in US$m by year. Additionally, the number of transaction within respective year is specified.

Year	ϕ value	N	%	cum. %
1989	293.0	1	1.1%	1.1%
1990	1343.1	6	6.7%	7.8%
1991	416.0	3	3.3%	11.1%
1992	761.9	5	5.6%	16.7%
1993	467.5	11	12.2%	28.9%
1994	315.5	7	7.8%	36.7%
1995	345.4	10	11.1%	47.8%
1996	757.6	12	13.3%	61.1%
1997	551.2	8	8.9%	70.0%
1998	479.5	8	8.9%	78.9%
1999	274.0	7	7.8%	86.7%
2000	247.2	3	3.3%	90.0%
2001	891.4	5	5.6%	95.6%
2002	83.9	3	3.3%	98.9%
2003	2608.4	1	1.1%	100.0%
Total	572.5	90.0	100.0%	-

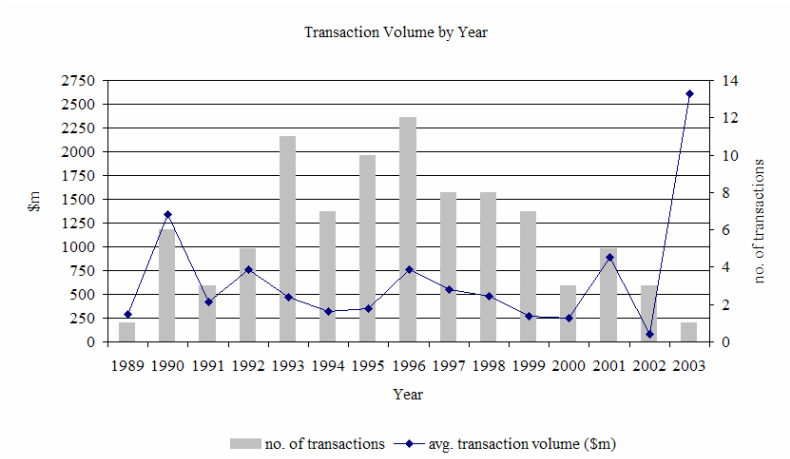

Figure I. Transaction value and number of transactions by year

Table II. Transaction value (in $m) by year of trade-sale privatization

This table shows average transaction values denominated in US$m by country and industry whereas the column "by target" presents information for the target and the column "by acquirer" gives information for the acquirer, respectively. Panel A presents average transaction size and number of transactions by country. Panel B presents information for industry involved in the transaction.

Panel A: Transaction value (in $m) by country

	by target			*by acquirer*		
Country	ϕ value	N	%	ϕ value	N	%
Austria	545.5	3	3.3%	793.7	2	2.2%
Belgium	1318.3	3	3.3%	497.3	1	1.1%
Denmark	387.0	2	2.2%	711.5	1	1.1%
Finland	284.9	6	6.7%	811.5	5	5.6%
France	323.2	11	12.2%	867.0	5	5.6%
Germany	573.4	12	13.3%	610.1	12	13.3%
Greece	848.7	2	2.2%	848.7	2	2.2%
Ireland-Rep	345.6	2	2.2%	486.0	3	3.3%
Italy	422.9	10	11.1%	194.7	6	6.7%
Netherlands	1567.0	5	5.6%	1819.8	6	6.7%
Norway	150.3	4	4.4%	315.6	6	6.7%
Portugal	182.8	2	2.2%	52.6	1	1.1%
Spain	319.2	6	6.7%	359.8	6	6.7%
Sweden	1191.7	11	12.2%	911.6	8	8.9%
Switzerland	-			166.2	2	2.2%
United Kingdom	233.9	11	12.2%	251.9	24	26.7%
Total	572.5	90	100.0%	572.5	90	100.0%

Panel B: Transaction value (in $m) by industry

	by target			*by acquirer*		
Industry	ϕ value	N	%	ϕ value	N	%
Division B: Mining	358.2	6	6.7%	738.6	7	7.8%
Division D: Manufacturing	498.8	23	25.6%	547.6	22	24.4%
Division E: Transportation, Communication,	529.4	27	30.0%	371.0	24	26.7%
Division F: Wholesale Trade	-			181.4	1	1.1%
Division G: Retail Trade	162.5	2	2.2%	162.5	2	2.2%
Division H : Financial Institutions	943.5	24	26.7%	867.1	27	30.0%
Division I: Services	80.4	8	8.9%	212.7	7	7.8%
Total	572.5	90	100.0%	572.5	90	100.0%

Table III. Cumulated abnormal returns to acquirer

This table shows cumulated abnormal returns in relative and absolute terms. Panel A shows cumulated abnormal returns (CARs), Panel B shows cumulated abnormal dollar returns (CADRs). Information is provided for the events periods [-20,10], [-10,10], [-5,5], [-1,1], [0], [-20;1], [-10;-1]; [1;10] around the announcement of an acquisition of a state-owned target.Cumulated abnormal returns are calculated by adding up abnormal returns for the respective period. The stated figures are equally weighted averages of all 90 events. We used two different test statistics to estimate statistical significance for CARs. Besides the Böhmer-Test (BMP) the Wilcoxon Rank Sum Test is conducted to ensure that test results are not due to the false assumption of normality. For each test the respective Z-Value is presented. In Panel B for CADR the BMP-Test can not be conducted, hence, a standard t-test is used and again verified by the Wilcoxon Rank Sum Test. ***, ** and * indicate a significance level of 1%, 5% and 10%, respectively.

Panel A: CARs

				Böhmer Test		Wilcoxon Rank Sum Test	
Period	CARs	Pos.	Neg.	*z-value*	*p-value*	*z-value*	*p-value*
[-20;10]	0.64%	43%	57%	-0.37	0.71	-0.52	0.50
[-10;10]	0.57%	43%	57%	-0.10	0.92	-0.39	0.60
[-5;5]	0.22%	47%	53%	-0.27	0.79	-0.15	0.74
[-1;1]	0.41%	49%	51%	0.65	0.51	-0.38	0.76
[0]	0.21%	43%	57%	0.31	0.76	-0.18	0.86
[-20,-1]	0.58%	46%	54%	-0.36	0.72	-0.96	0.34
[-10;-1]	0.50%	48%	52%	0.06	0.96	-0.40	0.69
[1;10]	-0.15%	46%	54%	-0.28	0.78	-0.54	0.59
No. Of observations	*90*						

Panel B: CADRs

				T-Test		Wilcoxon Rank Sum Test	
Period	CADRs	Pos.	Neg.	*t-value*	*p-value*	*z-value*	*p-value*
[-20;10]	-44.37	43%	57%	-0.47	0.64	-0.99	0.28
[-10;10]	-32.90	43%	57%	-0.44	0.66	-0.36	0.69
[-5;5]	-56.92	47%	53%	-1.08	0.28	-0.60	0.50
[-1;1]	-3.48	49%	51%	-0.13	0.90	-0.13	0.84
[0]	-4.50	43%	57%	-0.23	0.82	-0.71	0.48
[-20,-1]	-48.10	46%	54%	-0.71	0.48	-0.82	0.41
[-10;-1]	-18.49	48%	52%	-0.41	0.68	-0.48	0.63
[1;10]	-39.19	46%	54%	-0.78	0.44	-0.37	0.71
No. Of observations	*90*						

Table IV. Cumulated abnormal returns to acquirer for different subparts of the sample period

This table shows differences between cumulative abnormal returns to acquirers for different parts of the sample period. Panel A shows cumulated abnormal returns (CARs), Panel B shows cumulated abnormal dollar returns (CADRs). Information is provided for the events periods [-20,10], [-10,10], [-5,5], [-1,1], [0], [-20;1], [-10;-1]; [1;10] around the announcement of an acquisition of a state-owned target. WRST stands for Wilcoxon Rank Sum Test. ***, ** and * indicate a significance level of 1%, 5% and 10%, respectively.

Panel A: CARs

	1989 - 1995			1996 - 2003			Difference			
		T-Test	WRST		T-Test	WRST		T-Test		Wilcoxon
Period	CARs	t-value	z-value	CARs	t-value	z-value	□CAR	t-value		z-value
[-20;10]	-0.22%	-0.11	-0.37	1.14%	0.43	-0.46	-1.36%	0.41		-0.15
[-10;10]	0.09%	0.06	-0.13	0.85%	0.39	-0.48	-0.76%	0.30		-0.27
[-5;5]	-0.38%	-0.32	-0.53	0.56%	0.40	-0.04	-0.94%	0.51		-0.36
[-1;1]	-0.22%	-0.60	-0.56	0.93%	1.28	-0.87	-1.15%	1.30		-0.99
[0]	-0.33%	-0.98	-1.05	0.52%	1.46	-0.56	-0.85%	1.73	*	-1.03
[-20,-1]	0.63%	0.38	-0.06	0.56%	0.22	-1.27	0.07%	-0.02		-0.59

[-10;-1]	0.93%	1.09	-0.63	0.26%	0.13	-1.01	0.67%	-0.31	-1.13
[1;10]	-0.52%	-0.54	-1.05	0.07%	0.07	-0.02	-0.59%	0.42	-0.55
No. Of observations	33			57					

Panel A: CADRs

	1989 - 1995			1996 - 2003			Difference		
		T-Test	WRST		T-Test	WRST		T-Test	Wilcoxon
Period	CARs	z-value	t-value	CARs	t-value	z-value	□CAR	t-value	z-value
[-20;10]	-123.21	-1.08	-0.51	-73.61	-0.68	-0.89	-49.60	0.32	-0.19
[-10;10]	-12.41	-0.17	-0.15	-91.00	-0.90	-0.41	78.59	-0.64	-0.45
[-5;5]	-47.67	-0.82	-0.67	-81.74	-1.05	-0.40	34.07	-0.35	-0.07
[-1;1]	1.52	0.05	-0.01	-10.89	-0.28	-0.25	12.42	-0.25	-0.12
[0]	-11.80	-0.97	-1.08	-0.28	-0.01	-0.21	-11.53	0.35	-0.46
[-20,-1]	-88.94	-0.86	-0.17	-24.46	-0.28	-1.09	-64.48	0.47	-0.73
[-10;-1]	21.86	0.53	-0.63	-41.85	-0.63	-1.09	63.71	-0.81	-1.18
[1;10]	-22.46	-0.42	-1.14	-48.87	-0.67	-0.31	26.41	-0.29	-0.87
No. Of observations	33			57					

Table V. Cumulated abnormal returns to acquirer for national and cross-border transactions

This table shows differences between cumulative abnormal returns between domestic and cross-border acquisitions. Panel A shows cumulated abnormal returns (CARs), Panel B shows cumulated abnormal dollar returns (CADRs). Information is provided for the events periods [-20,10], [-10,10], [-5,5], [-1,1], [0], [-20;1], [-10;-1]; [1;10] around the announcement of an acquisition of a state-owned target. WRST stands for Wilcoxon Rank Sum Test. ***, ** and * indicate a significance level of 1%, 5% and 10%, respectively.

Panel A: CARs

	Domestic acquisitions			Cross-border acquisitions			Difference				
		T-Test	WRST		T-Test	WRST		T-Test		Wilcoxon	
Period	CARs	t-value	z-value	CARs	t-value	z-value	□CAR	t-value		z-value	
[-20;10]	-0.40%	-0.28	-0.85	2.22%	0.55	-0.09	-2.62%	0.70		-0.26	
[-10;10]	-1.10%	-1.04	-1.15	3.06%	0.94	-0.58	-4.16%	1.40		-1.09	
[-5;5]	-1.61%	-1.48	-1.24	2.97%	1.66	-0.96	-4.58%	2.32	**	-1.47	
[-1;1]	-0.25%	-0.47	-0.67	1.40%	1.27	-1.23	-1.66%	1.49		-1.38	
[0]	0.63%	1.89	* -1.27	-0.42%	-1.05	-1.78	* 1.04%	-2.01	**	-1.89	*
[-20,-1]	0.17%	0.16	-0.68	1.20%	0.30	-0.72	-1.03%	0.29		-0.26	
[-10;-1]	-0.52%	-0.79	-0.79	2.04%	0.64	-0.16	-2.56%	0.94		-0.53	
[1;10]	-1.20%	-1.46	-1.30	1.44%	1.07	-0.74	-2.64%	1.77	*	-1.39	
No. Of observations	54			36							

Panel A: CADRs

	Domestic acquisitions			Cross-border acquisitions			Difference				
		T-Test	WRST		T-Test	WRST		T-Test		Wilcoxon	
Period	CARs	z-value	t-value	CARs	t-value	z-value	□CAR	t-value		z-value	
[-20;10]	-92.47	-1.19	-1.18	-90.79	-0.55	-0.19	-1.68	0.01		-0.19	
[-10;10]	-107.51	-1.19	-0.84	5.82	0.05	-0.33	-113.33	0.81		-0.57	
[-5;5]	-97.29	-1.28	-1.19	-27.19	-0.39	-0.31	-70.10	0.64		-0.96	
[-1;1]	-3.70	-0.11	-1.31	-10.29	-0.23	-1.01	6.59	-0.12		-1.72	*
[0]	24.43	0.92	-0.43	-47.90	-1.69	* -1.65	* 72.32	-1.81	*	-1.50	
[-20,-1]	-28.33	-0.49	-1.30	-77.76	-0.53	-0.20	49.43	-0.36		-0.72	

[-10;-1]	-43.38	-1.16	-0.83	18.85	0.19	-0.17	-62.22	0.68	-0.71
[1;10]	-88.56	-1.16	-0.96	34.87	0.70	-0.39	-123.43	1.21	-0.85
No. Of observations	54			36					

Table VI. Overview – Regression variables

This table gives an overview about each of the seven variables included into the OLS regression model. Panel A explains how each variable was computed.Panel B shows descriptive statistics for all seven variables included into the OLS regression model.

Panel A. Description of variables

Variable	Description
Government Liabilities	Net financial liabilities$_{target}$ / GDP$_{target}$. Both figures are averages of the transaction year.
Cross-Border	Binary dummy variable: 1 = cross-border transaction, 0 = domestic transaction.
Human Development	HDI$_{acquirer}$ - HDI$_{target}$. Whereas HDI stands for the Human Development Index calculated and published by the UN
Industry relation	Binary dummy variable: 1 = match of the first two digits of buyer and target SIC code, 0 = no match of first two digits of buyer and target SIC code.
% of acquisition	% of target equity acquired by the bidding company.
Transaction size	Natural logarithm of the transaction volume.
Relative transaction size	Natural logarithm of the transaction volume divided by the logarithm of the market value of the acquirer 40 days prior to the announcement.

Panel B. Descriptive statistics

Variable	Mean	Std. dev.	Max	Min
Government Liabilities	39.13%	43.01%	132.41%	-97.08%
Cross-Border	40.00%	49.26%	1.00	0.00
Human Development	0.20%	0.97%	2.80%	-3.78%
Industry relation	68.89%	46.55%	1.00	0.00
% of acquisition	90.24%	17.26%	100.00%	50.10%
Transaction size	572.53	1069.88	7457.50	50.10
Relative transaction size	74.98%	25.19%	177.24%	35.24%

Table VII. Cumulated abnormal returns to acquirer

This table shows OLS-regression analysis of the determinants of returns to acquirers of state-owned targets. The dependent variables are cumulated abnormal returns (CARs) for the models shown in Panel A and cumulated abnormal dollar returns (CADRs) for the models shown in Panel B. The independent variables are: GOVERNMENT LIABILITIES is the ratio between net financial liabilities of the target's country and the gross domestic product. CROSS-BORDER is a dummy variable that takes the value one for cross-border acquisitions and zero for domestic acquisitions. Δ HUMAN DEVELOPMENT is the absolute difference between the HDI of the acquirer and the target country, whereas HDI is the Human Development Index published annually by the UN. RELATEDNESS is a dummy variable that takes the value one if both target and acquirer have identical SIC codes on the first two digits. % OF ACQUISITION gives the percentage amount of target equity acquired by the bidder. TRANSACTION SIZE is the natural logarithm of the transaction value. TRANSACTION SIZE / ACQUIRER SIZE is the logarithm of the ratio between the transaction value and the market value of the acquirer. ***, ** and * indicate a significance level of 1%, 5% and 10%, respectively.

	Panel A:		Panel B	
	Model 1a	Model 1b	Model 2a	Model 2b
Coefficients				
Intercept	2.16%	1.61%	485.14 **	482.15 **
	[0.657]	[0.747]	[0.030]	[0.034]
Government Liabilities	-1.44%	-1.70%	-116.42 *	-123.93 *
	[0.343]	[0.270]	[0.092]	[0.075]
Cross-Border	2.13% *	-	73.13	-
	[0.079]		[0.180]	
Δ Human Development	-	0.18%	-	-11.25
		[0.776]		[0.685]
Relatedness	-1.77%	-1.67%	-106.97 *	-106.21 *
	[0.164]	[0.197]	[0.063]	[0.068]
% of Acquisition	-2.27%	-1.47%	-336.22 **	-310.23 *
	[0.518]	[0.677]	[0.036]	[0.053]
Transaction Size	0.35%	0.44%	-13.79	-12.95
	[0.512]	[0.429]	[0.572]	[0.602]
Transaction Size / Acquirer Size	0.29%	0.13%	11.70	5.96
	[0.468]	[0.738]	[0.522]	[0.740]
F-statistic	*1.41*	*0.86*	*2.17*	*1.85*
	[0.220]	*[0.525]*	*[0.054]* *	*[0.099]* *
N	*90*	*90*	*90*	*90*
Adjusted R^2	*2.69%*	*-0.01%*	*7.29%*	*5.40%*