CORPORATE GOVERNANCE AND TAKEOVERS: INSIGHTS FROM PAST RESEARCH AND SUGGESTIONS FOR FUTURE RESEARCH

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Abstract

This paper reviews the literature on the association between corporate governance and takeovers. It approaches takeovers as an effective external corporate governance mechanism. The main conclusions to be drawn is that although the mere threat of an active market for corporate control may be positively correlated with good internal governance, takeovers will always take place independently of good internal corporate governance by targets and that managerial ownership is crucial for a favorable shareholder outcome in a takeover event. We believe future research on corporate boards, cross-national takeovers and managers of bidding firms would be of great interest.

Keywords: Takeovers; Corporate Governance; Mergers and Acquisitions

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Introduction

This paper reviews literature concerning corporate governance and its relation to corporate takeovers. Jensen (1988) views the market for corporate control as a competition between different management teams that fight to manage a bundle of assets that is owned by shareholders. Thus, the topics of corporate governance and takeovers are inevitably linked. Besides the principal-agent problem this review approaches issues like the disciplinary-synergistic dichotomy for takeovers, takeover defense provisions and failed takeovers. Although the tendency is for takeovers to be more and more synergistic, this does not mean that the disciplinary takeovers have completely disappeared. The simple fact that there is an active market for corporate control may act as a threat to managers and be enough to ensure good internal governance (even without takeovers having to take place). One thing is certain: takeovers will always take place independently of good or bad corporate governance. Takeovers that target firms with good internal governance are consistent with shareholder welfare theory and the main reason for the takeover event has to do with synergies or with a strategic market move by the acquiring firm, in cases where the target company has poor internal governance the market for corporate control tend to be disciplinary towards the so called “bad managers”.

This study also identifies some ideas for future research. There is a need for studies on effective management evaluation systems and how to make boards of directors stronger: what can be done besides having independent directors in the board? More research using samples of cross-national takeovers is also necessary, in this time of globalization: do the different existent corporate governance models of each country/continent make it difficult for takeover moves to take place? Finally, literature on what happens to managers of bidding firms after failed takeovers is also a relatively unexplored field of research since literature tends to focus on target managers after a failed takeover.

This paper is organized as follows. Section 2 provides a background on takeover history. Section 3 presents the reasons for takeovers to take place. Section 4 incises on the principal agent problem. The disciplinary-synergistic dichotomy for takeovers is reviewed in section 5. Takeover defense provisions are approached in Section 6 and weather or not they serve management entrenchment as well as destroy firm value. Section 7 reviews the relatively unexplored area of failed takeover attempts. Finally, section 8 briefly focuses on the post acquisition performance and section 9 resumes the major conclusions to be drawn from this study.

Historical perspective on takeovers and corporate governance

Corporate governance and corporate takeovers history is written by different waves of takeover activity. The environment around each of these takeover waves is their origin and each one has different and unique. Despite their diversity, all waves have similarities: they are preceded by technological or industrial shocks and occur in a positive economic and political environment together with stock market booms (Martynova & Renneboog, 2005).

US companies were the takeovers' pioneers, when they started this activity in the 1890's. This first takeover wave was triggered by the technological growth of the United States into a major industrial economy. At this time many horizontal combinations and consolidation of several industries where taking place. This first wave came to an end with the crash of this new industrial equity market in 1905 and the rise of the first Great War (Gaughan, 2002).

Takeover activity picked up again in the 1910 decade. This fact is explained, according to Sudarsanam (2003), by the creation of anti-trust laws and their consequent enforcement after the first merger wave. The 1929 depression came to put an end to this second wave of takeover activity along with another stock market crash.

With the 1960's came the third wave of takeovers. The Second World War was finished and the need for reconstruction of several countries set the opportunity for industrial activity to pick up again and with it a new breath of fresh air in the "war" for corporate control. This wave would only come to an end when the oil crisis of 1973 pushed the market to another big recession. This was the conglomerate wave of M&A in the US. Corporations focused on diversification and formed huge conglomerates with much diversified businesses. UK takeover activity was still a step behind since it still focused essentially on horizontal growth with the objective of increasing market power (Gaughan, 2002).

The fourth merger wave, in the 1980's, had one unique feature: the "corporate raider" became a common and active figure in the market for corporate control. This player made use of a powerful weapon of this time, the junk bonds. Although "corporate raiders" existed before the 1980's we can say that it never had such great financing power that could change the outlook of corporate management. It exposed managers to outstanding outside threats and introduced the disciplinary takeover. Goldstein (2000), tried to use the free cash flow theory to explain the takeover activity wave that started in the 1980's. His attempt was unsuccessful, as empirical results were inconsistent with the predictions of this theory. Restructuring in its more pure state can also be an explanation for this wave of takeovers, putting an end to the diversified conglomerates of the previous wave. The fourth wave of the 1980's ended when the junk bond market collapsed in the end of the decade.

In 1992 the market witnessed the rise of the fifth merger wave. This period featured even larger and more outstanding mergers than the 1980's. Deals at this time were strategic with companies seeking to expand into new markets and taking advantage of the more and more trendy concept of synergies. These two last takeover waves are studied by Kini (2004) and empirical results show that the role of takeover market as a disciplinary measure for poor performing management and companies changed from the 1980's to the 1990's.

Reasons for takeovers

There is a wide range of economic reasons that can explain a merger and the literature is vast (and not our objective). One of the main motives is growth: companies see in takeovers a way to grow quickly, either horizontally or vertically. Economic gains can also drive a company to acquire another firm; these economic gains can either come from economies of scale or economies of scope. Firms may also merger to get better financial benefits, a larger firm that resulted in the merger of two small ones may have better access to capital markets and lower cost of capital. Various other motives exist for mergers and acquisitions including R&D acceleration and tax motives.

However, one can not forget the existence of a strong human influence. Hubris, rather than objective analysis, may also motivate a takeover. Roll (1986) argues that managers impose their own valuation and often pay a very high premium for targets. The author introduces this hypothesis in the sense that if the markets are efficient the only thing that can explain such overpaying actions is manager's pride, since it makes it hard for them to back-off a bid even if premium value doesn't make sense to the market.

Merret and Houghton (1999) have come to reinforce Roll's hypothesis since they find evidence that managers actions are motivated by strong reputational effects that are not widely recognized in the contemporary literature as a force that powerfully drives corporate governance. Meeks and Meeks (2001) findings are also consistent with the hubris hypotheses. They find that managers of bidding companies create artificial incentives to go ahead with an "inflated" bid or to make a bid which offers no benefit to their shareholders. Finally, according to Goergen and Renneboog (2004), managerial hubris is a credible motive for takeovers and, for a third of firms, managerial hubris leads to poor decision making on mergers and acquisitions.

Alexandridis *et al.* (2006) find that the existence of blockholders mitigates short-run overpricing in takeover situations and thus eliminates the chances for post takeover long-run abnormal returns, ensuring the efficiency of the takeover market. In other words they find that the hubris hypothesis is less credible in companies with blockholders.

The agency problem and takeovers

It is well know that the separation of capital and operations brings about agency problems, which need to be dealt with via corporate governance instruments. If managers put their interests ahead of the interests of the shareholders and the corporation faces a takeover the agency cost can be even more severe. According to Bebchuk et al. (2007), remaining independent reduces returns for target shareholders relative to accepting the hostile takeover bid or selling to a white knight. Since a takeover can affect the wealth of managers and shareholders differently, shareholders may benefit financially from the process while managers could loose their jobs in the case of a change in ownership.

A seminal paper in this area is Gompers et al. (2003). In this study the corporation is viewed as being a republic where the ultimate authority rests with voters, the shareholders. The voters elect representatives (directors) who delegate most decisions to bureaucrats (managers). Gompers et al. (2003) view this republic as having two extremes. One that has the characteristics of a democracy: managers have little power and shareholders can quickly replace directors. The other extreme tilts towards a dictatorship: management has extensive power and shareholders face strong restrictions to replace directors. We next analyze the vast literature, by dividing it into the following subsections: (i) managers and internal directors, (ii) executive compensation, (iii) boards and outside directors and (iv) shareholders.

Managers and internal directors

The way directors are elected can have an impact on the probability of a firm being acquired. In Bebchuck (2007), targets are classified into three types, from least to most vulnerable to a hostile bid, based on their director election process: (1) "Effective Staggered Board" targets, whose boards are protected by a non-evadable staggered board, therefore cannot be substituted before two annual meetings; (2) "Effective Annual Term" targets, whose boards can only be replaced at the next annual meeting; and (3) " No Minimum Term" targets, which have boards that can be replaced by shareholders quickly by filing written consents or by calling a special meeting.

Another determinant factor when facing a bid can be the level of managerial ownership. In their study of this latter issue, O'Sullivan and Wong (1998) find that it does play a crucial role in both the nature and outcome of takeover bids. Typically companies were executive directors own a significant proportion of equity are less likely to contest a takeover bid, since in these types of target corporations, bidders launch a bid only after obtaining the target management approval. This finding is consistent with one of the most common internal governance mechanism that is applied in modern management, managerial compensation through stock options. "The efficacy of corporate governance has greater impact on equity-based compensation when compared to fixed compensation" (Cyert et al. 2002).

While O'Sullivan and Wong (1998) center their study on a sample of takeovers during the period between 1989 and 1995, Cosh et al. (2006) focus on the same hypothesis but used a wider range of years in their sample (from 1985 up to 1996). The big difference between these two studies is that while O'Sullivan and Wong (1998) only approach a period where takeovers were believed to be less disciplinary and more synergistic, Cosh et al. (2006) also covers the 1980's, when takeovers were mainly disciplinary. Their findings show strong evidence of a positive relation between takeover performance and CEO ownership and that the effect of CEO ownership is more relevant at low levels of holdings since CEO's with high levels of holdings may have the sufficient voting power to create an entrenchment situation. Shivdasani's study (1993) supports this analysis, concluding that decreasing CEO's shares from 90th to 10th percentile increases the probability of a takeover 4 times.

Harford's (2000) findings also show that when facing a takeover bid managers face a complicated set of incentives. In situations where managers have low share ownership it is unreasonable to assume that they will act appropriately strictly out of altruism. What this set of findings shows is that the idea of managerial ownership positively related with good performance in terms of shareholder welfare when facing a takeover bid and that this holds for different takeover surrounding environments.

Henry (2005) left out managerial ownership to see if there is any other sort of internal mechanism that aligns interests and reduces the agency problem. He concludes that target directors have an overwhelming tendency to support takeover bids offering share-exchange transactions, which provides lower post-acquisition shareholders returns. Furthermore, Henry (2005) finds that common governance initiatives such as the independence of the board of directors, separation of CEO and chairman responsibility and reduced board size and increased director remuneration, do not appear to be sufficient in aligning the interests of shareholders and corporate managers in a situation of takeover decision-making.

Executive Compensation

"*In Judging whether corporate America is serious about reforming itself, CEO pay remains the acid test. To date results aren't encouraging.*"

Warren Buffet, letter to shareholders of Berkshire Hathaway Inc. (2004)

Lewellen et al. (1985) analyze merger decisions and argue that a more effective compensation plan is due to a larger fraction of firm's stock hold by the management team, but "this argument ignores the riskiness of the compensation" as the discount rate used by stockholders depends on non-diversifiable risk, and the manager's risk is frequently a function of firm's total risk.

Jensen and Ruback (1983) view the market for corporate control as the arena in which management teams compete for the right to manage corporate resources. In this perspective, incumbent management teams detain sufficient power to increase takeover costs against the competing team. Such resistance does not eliminate the probability of a successful takeover but can discourage various competing teams and lead to a much higher takeover costs. Moreover, opposition between the incumbent management team can harm stockholders, consequence of management self-interests when not allied with stockholders best welfare. Furthermore, Bertrand and Mullainathan (1999) find that executive compensation increases with the passage of antitakeover legislation.

Cyert et al. (2002) stress the issue of executive compensation and its relation to the market for corporate control, as their empirical findings indicate that external takeover threats play a major role in executive compensation design. Bebchuk and Fried (2003) view the design of executive compensation not only as an instrument for addressing the agency problem between managers and shareholders but also as part of the agency problem itself. They argue that in publicly traded companies with dispersed ownership managerial influence might lead to substantially inefficient compensation arrangements that produce poor or even perverse incentives. Other studies have come to reinforce Bebchuk and Fried's findings. Jiraporn et al. (2005), for example, focus on CEO compensation and demonstrate that it is inversely related to the strength of shareholder rights. In other words, CEO's obtain more favorable compensation in firms where there are greater agency problems.

Bebchuk and Fried (2005) discuss the existence of pay without performance. Their main inference is that the problem does not reside in the levels of executive pay but rather on the distortion of incentives caused by compensation. To address this problem they propose three kinds of changes: (i) increases in transparency; (ii) improvements in pay practices; (iii) improvements in board accountability to shareholders. Future research is needed to monitor if these suggestions are being considered by firms.

Boards and outside directors

The role of a corporate board of directors in what concerns good corporate governance is to hire, monitor and evaluate top management efficiently so that the market for corporate control doesn't have to act in a disciplinary fashion and do that job for the board members. In a study of the major methods by which managers of major corporations are removed Hirshleifer and Thakor (1998) present two hypotheses. They argue that it is either the market for corporate control that substitutes bad managers or it is the board of directors that anticipates and fires managers in the fear of a "kick-in-the-pants" effect, by which the board might be dismissed by a successful acquirer who views it as lax. They find that the need for external corporate governance to come in play is lower when internal corporate governance does not work well and that a well functioning internal control mechanism (the board) does not obviate the need for external control (takeovers). O'Sullivan and Wong (1998) produce similar results in their research on the interaction between internal and external control mechanisms by analyzing board composition and ownership characteristics in the context of UK takeover activity. Their findings indicate that targets for hostile bids exhibit strong internal governance in terms of board composition and ownership. Both studies suggest that if the internal governance is strong, prompted by a strong corporate board, shareholders rights will be protected and that takeovers bids that reflect target shareholder gains are more probable to be successful.

In a more recent study, Webb (2006) also approaches the issue by analyzing the relation between board of directors and takeover defenses. The findings of this study reveal that having a strong governance mechanism in place mitigates the effects of having another mechanism in place. The marginal benefit of each mechanism appears to decline as the use of the other increases. Therefore, a strong board is inversely related to strong shareholder protection in the form of takeover defenses. Webb's findings are consistent with the previous findings that a strong board is enough to ensure that shareholders interests are protected.

But how can a firm design a strong board of directors? Petra (2005), aims at determining weather or not an assumption made by public perception has credibility or not: the idea that outside independent directors strengthen corporate boards. Shivdasani's (1993) empirical results prove that a very large impact on takeovers outcome, and a good proxy to measure the quality of directors, is the additional outside directorship. Weisbach (1993) argues that although the evidence is consistent, additional outside directorship may be a poor proxy measure as good directors with market value in the market of directorships resign during bad times. Furthermore, in Weisbach's (1993) review of Shivadasin's (1993) study, he emphasizes the expected effect of blockholdings on the probability of a takeover. Specifically, he says that "ownership by unaffiliated blockholders is associated with a large increase in the predicted probability while ownership by affiliated blockholders is associated with a large decrease in the predicted probability of a takeover". As strong corporate boards appear to be the solution to get back the market's confidence in the ability of firms to govern themselves, this should be an area for future research to approach. Research on effective management evaluation systems is also needed since it is one of the designed tasks for boards to carry out.

Shareholders

In the event of a takeover it is reasonable to think that target shareholders would look forward to it as they see it as an opportunity to maximize their wealth by selling their stock to the highest bidder. Thus, other stakeholders may be forgotten by management and not see their interests served. Schneper and Guillén (2004) provide a cross-national study of hostile takeovers, considering not only shareholders, but also all major stakeholders of company. This study puts the shareholder-stakeholder dichotomy in the spotlight and looks at the U.S. market as being shareholder centred and the European and Japanese markets as stakeholder oriented. The major findings of this study are that hostile takeovers are accepted as an efficient corporate governance mechanism in more shareholder centred markets as they increase in frequency with the extent to which shareholders are protected and decrease with the degree to which workers' and banks' rights are protected.

To better understand Schneper and Guillén (2004), Baums and Scott (2005) compare how the interests of minority shareholders are served in the U.S. and in the German markets. They do this by studying four dimensions of corporate governance which include one that is relevant for this literature review: the market for corporate control. They conclude that the minority shareholders in the U.S. are better protected in the event of corporate takeovers. The authors also point out a list of proposed changes that would enhance the idea of "taking shareholders seriously".

A big question related to the agency problem that remains unanswered is: are post-takeovers financial results of privately held companies different from big corporate ones? One possible way of studying this could be by comparing post-take-over financial characteristics of corporate firms with post-take-over financial characteristics of privately held companies. Unfortunately, very few studies have addressed the performance of smaller unquoted companies involved in take-overs. Thus, we believe this is a good topic for future research.

Takeovers: disciplinary or synergistic?

Hostile takeovers became more and more a market trend from the 1980's on until the 1990's, when friendly takeovers prospered. Stout (1992) and Weisbach (1993) view hostile takeovers as disciplinary and friendly takeovers as being synergistic ones. Kini (2004) views the market for corporate control as a "court of last resort". Theory and empirical results also suggest that firms with ineffective internal governance mechanisms are more likely to suffer external takeover pressures as internal and external governance mechanism are seen as substitutes and that the presence of one type of governance mechanism mitigates the need for existence of the other (Webb, 2006).

Weir and Wright (2006) study takeovers from a different point of view: they focus on takeovers that ended in public to private transactions during the 1990's decade. Their findings show that public to private transactions have different characteristics then the public to public transactions. Specifically, their findings indicate that the public to private transactions are consistent with a non-disciplinary perspective where takeovers are complementary to internal governance. This is consistent with the rise of friendly takeovers during the 1990's. This happens because these types of transactions have different characteristics from the public to public transactions as they are mostly result of MBO's where there is already a management ownership of the firm and managers have private information that leads them to think that the market has a wrong view of the firm and is under-pricing it.

Camerlynck and Ooghe (2000) studied companies that are not quoted on financial markets (in Belgium) and they show that acquired firms are not mainly financially distressed firms or underperforming firms in the pre-acquisition period, but that target firms are in general more profitable than their industry medians. So, it can be said that "acquisition is not an alternative to bankruptcy". Sinha (2004), reinforces this point in her paper and empirically concludes that firms who have relatively ineffective internal governance mechanisms and have poorer financial performance are not necessarily the ones that are the likely targets for hostile takeover bids. These findings are consistent with the argument that there are many more reasons for takeover activity that may have nothing to do with the fact that the firm may be underperforming or that it simply badly managed. Strategic moves by some firms of the market in view of integration or increase in market power may be in the origin of takeover approaches. Other approaches can be found in the "Growth-resource mismatch hypothesis" (firms with a mismatch between their growth and the financial resources at their disposal are likely targets), or in the "Industry disturbance hypothesis" (firms that are in an industry subjected to economic disturbances are likely acquisition targets) or even in the "size hypothesis" (the likelihood of acquisition decreases with the size of the firm)

Goergen and Renneboog (2004) reinforce Sinha's (2004) findings. In their research they investigate whether the predominant reasons for takeovers is synergies, agency problems or managerial hubris. The results suggest that synergies are the prime reason for takeover bids and that both the targets and bidders share the wealth gains of the transaction. Both of these two last referred studies come to give evidence on the fact that takeover philosophy changed from the 1980's to the 1990's, since samples from both research papers focus essentially on the 1990's period and on the fifth takeover wave.

Although history suggests that takeovers have been changing from disciplinary to synergistic there are studies that contradict the previous two. Baums and Scott (2005) conclude that the active market for corporate control in the U.S. provides a threatfull environment and leads to better protection of minority shareholders and better internal corporate governance.

Overall, studies on the disciplinary-synergistic dichotomy tend to focus only on a sample of takeover processes in which the players are from the same country. There is space for future research sampling a set of cross-national takeovers.

Do takeover defense provisions hide internal governance problems and decrease firm value?

After the wave of the disciplinary takeovers of the 1980's, firms began to adopt more preventative anti-takeover measures, like poison pills (see Dowen et al. (1994), and in this way weakening what some literature considers to be a powerful external mechanism for corporate governance (Goldstein (2000) and Kini et. al. (2004)). An assumption made by theory on this matter is that internal governance mechanisms and external governance mechanisms behave as substitutes. So, does the mitigation of effects in what concerns external governance mechanisms such as takeovers through takeover defense provisions make room for a lack of efficiency in internal governance mechanisms? Do takeover defense provisions contribute to reducing the value of a firm? Research on these topics has found very distinct, and sometimes contradicting, results, both supporting the management entrenchment hypothesis (Bebchuk and Cohen (2005)) as well as the hypothesis that antitakeover measures lead target shareholders to obtain higher premium. However, Bebchuk et al (2007) find that target firms with effective staggered boards (ESB) do not extract higher premiums, when compared to non-ESB targets that sell.

Jiraporn *et al.* (2005) argue that CEO's of firms that deploy more takeover defenses, hence making managerial entrenchment more likely, receive higher levels of compensation and that CEO pay is positively associated with managerial protection. Cremers and Nair (2005) approach the subject by analyzing firm's takeover vulnerability and the existence of blockholders (stockholders that own more than 5% of the firm's outstanding shares). They conclude that firms with high takeover vulnerability and no blockholders have the highest value in the market and firms that have no takeover vulnerability, independently of having blockholders or not, have the lowest market value. This view supports the entrenchment idea in the sense that takeover defense provisions serve managers but destroy value to shareholders. This idea is particularly supported by Bebchuk et al (2007), who find that ESBs reduce target shareholders returns by approximately 20% in the five years after the hostile bid is launched.

Other papers study only some specific anti-takeover measure. Dowen et al. (1994) narrows its research on takeover defense provisions and their impact on management to isolate poison pills. Findings suggest that management efficiency has no relation to poison pills and that this defense mechanism, protecting firms with redeployable assets and innovative activity, may actually be an economically rational choice. Barnhart et al. (2000) provide a study on firm and State antitakeover provisions and CEO pay adjusted to firm performance. They conclude that the potential entrenchment resulting from reduced threat of external control provided by antitakeover provisions may allow the CEO to deliver a lower level of firm performance relative to their compensation. Brown and Caylor (2006) study how two measures of managerial entrenchment (the poison pill and the staggered board) affect firm value. Evidence in their research shows that a firm that has no poison pill and no staggered board will witness a significant positive impact in its valuation.

Other papers analyze several anti-takeover measures, creating indices. Gompers et al. (2003) construct an index based on 24 distinct corporate governance provisions for approximately 1500 firms since 1990. This index is set to proxy for the strength of shareholder rights. The empirical results show evidence of higher agency costs in a positive relationship between the index and both capital expenditures and acquisition activity. Bebchuk et al. (2005) defend that the index constructed by Gompers et al. (2003) has a very large set of provisions and that in such a large sample of governance provisions many are likely not to matter or to be an endogenous product of others. Thus, Bebchuk et al. (2005) suggest a new entrenchment index that is based on only six of the 24 IRRC governance provisions. Among the six provisions suggested by Bebchuk et al. (2005) there are four "constitutional" provisions (staggered boards, limits to shareholder bylaw amendments, supermajority requirements for mergers and supermajority requirements for charter amendments), these provisions are designed to prevent a majority of shareholders from having their way. The other two provisions are for "takeover readiness" (poison pills and golden parachutes). Adopting the view that "less can be more", Bebchuk *et al.* (2005), find evidence that firms with high entrenchment index are associated with large negative abnormal returns. What the results suggest is that takeover defense provisions serve management entrenchment and not shareholders interests.

Failed takeover attempts: "what do they tell us?"

The takeover process is not always a successful one - in the past many takeovers have failed. This has led some researchers to approach the subject of corporate governance from the failed takeover point of view. What leads these attempts to fail? What do managers do after a takeover attempt? Do they keep the same strategy or look at the failed takeover as a second chance for their management?

O'Sullivan and Wong (2001) defend that once the management of the target firm opposes a takeover, the probability of the bid succeeding falls by fifty percent. These authors identify another cause for takeover failure, as they find evidence that weak bidders are more likely not to be taken seriously.

Chatterjee et al. (2003) try to understand the relationship between managers' behavior after a failed takeover and the degree of board independence of the target firm. The firms studied in this paper had high diversification strategies and the goal was to see whether managers would look at takeovers as a "wake up call" or not. The results suggest that a failed takeover attempt will probably reduce any existing agency problems in the target firms. Furthermore, firms that have independent and vigilant boards are more likely to keep the same strategy ex-post to the takeover attempt since there is the belief that the strong internal governance has monitored a good strategy and that the takeover attempt can have other origins like strategic moves by the potential acquirer. Given that literature on failed takeovers tends to focus on what happens to managers of target companies an area for future research would be to focus on managers of bidding companies after a takeover process has failed or on the trend of the values of the bidder and the target firm after the failed takeover.

Post-acquisition performance

Alexandridis (2007) focus on the effect that divergence of opinion between acquirers has on post-acquisition performances of the firm. This is contrary to the hypothesis of homogeneous expectations among investors that is usually assumed in text books. Information asymmetries and tendency of investors to assess information in different ways are the two main reasons for these divergences. When investors disagree about the value of a stock, and its price is initially set by optimistic investors, if expectations turn out to be wrong, the upward bias in the stock price will be corrected through time as more information is assimilated by financial markets. So, firms subject to high investor disagreement are overpriced prior to the acquisition announcement, and as a consequence, this overpricing is gradually corrected, thus generating post-acquisition underperformance, irrespective to the information conveyed by the announcement. Ooghe et al. (2000), focusing in 143 Belgian privately-held companies concluded that takeovers do not tend to increase acquirers' performances, probably due to the reason explained just above and to a "managerial control loss problem". One important aspect of this paper, is that it doesn't focus on stock returns (since these companies are not quoted on financial markets), but uses instead liquidity and leverage analysis.

Conclusion

This paper reviews literature concerning corporate governance and its relation to corporate takeovers. As this is a vast field of research this paper is divided into a few key sections of the subject at hand. Besides the principal-agent problem this review approaches issues like the disciplinary-synergistic dichotomy for takeovers, takeover defense provisions and failed takeovers. Although the tendency is for takeovers to be more and more synergistic, this does not mean that the disciplinary takeovers have completely disappeared. The simple fact that there is an active market for corporate control may act as a threat to managers and be enough to ensure good internal governance (even without takeovers having to take place). One thing is certain: takeovers will always take place independently of good or bad corporate governance. Takeovers that target firms with good internal governance are consistent with shareholder welfare theory and the main reason for the takeover event has to do with synergies or with a strategic market move by the acquiring firm, in cases where the target company has poor internal governance the market for corporate control tend to be disciplinary towards the so called "bad managers".

This paper also identifies some ideas for future research. There is a need for studies on effective management evaluation systems and how to make boards of directors stronger. More research using samples of cross-national takeovers is also necessary, in this time of globalization. Finally, literature on what happens to managers of bidding firms after failed takeovers is also a relatively unexplored field of research since literature tends to focus on target managers after a failed takeover.

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