ABSTRACT

Managerial economics has stipulated that takeover usually occurs to undervalued companies. However, acquisitions of pulic listed companies in most international bourses actually happened during 'boom' times in the stock markets. Undervalued firms are usually hard to come by in these bull periods. In addition to the notion of undervaluation, it is said that companies acquired are normally less efficient in generating profits, resulting in low returns to their respective shareholders.

This research is set up to investigate the financial characteristics of companies acquired in the Kuala Lumpur Stock Exchange (KLSE) from August 1990 to December 1993. This period corresponded to the bull period in KLSE. The main objective of this research is to find out whether those companies taken-over are under or overvalued, and whether they are actually less efficient in generating profits.

Twenty financial variables were selected to study the valuation, short-term liquidity, leverage structure, profitability, activity and growth opportunity of the acquired public listed firms. These characteristics were compared to those firms of similar sizes from similar industries that were not taken-over. The analysis started with general overview based on average group means, before subsequently proceeding to univariate statistical analysis (t-test), factor analysis and multiple discriminant analysis.

The results from this research indicated that firms acquired in KLSE during the stipulated bull run period were overvalued relative to their controls, less profitable, having higher portion of current liabilities in their capital structure and retaining less of their incomes that directly affected their growth rate in profitability. The univariate statistical analysis showed that the acquired companies had a significantly higher valuation ratio (VR), significantly lower net profit margin (NPM), return on capital employed (ROCE), return on investment ROI), return on shareholders' fund (ROSF) and times covered (TC), as well as significantly higher debt-to-equity (DE) ratio. Through factor analysis, it was observed that the most distinct difference between the acquired and non-acquired companies was that the non-acquired companies had a dimension for their shareholders that was absence in the acquired firms. The managements of the non-acquired firms were striving to maximize their shareholders' wealth. Two discriminators were produced from stepwise multiple discriminant analysis. These discriminators according to their discriminating powers were return on capital employed and valuation ratio.

The shareholders of those acquired firms were thought to be willing to part with their stake in those companies in order to reap capital gains. Their actions were justifiable in view of overvaluation against assets, low dividend yield, low in profitability and growth rate. The results from this research also reaffirmed the traditional theory of firm and agency theory, that profit maximization is the best way to avoid a company being acquired.