Stock Price Reactions to M&A Market Events in Korea

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Received 28 July 2006 ; Accepted 4 October 2006

Abstract

This paper conducts event-studies on two of the most important events in recent history of Korean M&A market, to examine which firms were regarded more vulnerable to hostile takeover. First is the event on December 14th, 1993, in which the Congress unexpectedly delayed for two years the repeal of the law prohibiting hostile takeover. Second is the event on March 11, 1997 in which leading Korean companies announced that they would act together to block the on-going attempt to takeover Midopa Department Store. Both these events abruptly ended the expectation that hostile takeovers will rise in Korea and lead to sharp price drops of the stocks of the firms deemed to be the primary targets of the first M&A wave in Korea. This paper shows that the first event affected the firms that were small and financially weak, while the second event affected the firms that held controlling shares of many subsidiary firms but are not big Chaebols.

Keywords : M&A; Hostile Takeover; Chaebol; Securities and Exchange Act

JEL classification : G34

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1 Introduction

It was early 90's when the idea of hostile takeovers was first introduced in Korea. Until then, a law prohibiting acquisition of more than 10 percent share of a public company made hostile takeover virtually impossible (Section 200 of Securities and Exchange Act). In 1993, an amendment of Securities and Exchange Act was passed removing this provision. Other restrictions on M&A were also taken down after the financial crisis of 1997. As a result, Korea began to see some M&A activities in mid 90's, and the M&A market kept growing thereafter. M&A activities were mostly concentrated on small firms in KOSDAQ in the early years but later expanded into larger firms. In 2003, a foreign hedge fund (Crest Securities) acquired a significant share of SK inc, which was the flagship company of then third largest Chaebol group in Korea. Although the fund announced that they were not interested in taking over the control of SK, the acquisition showed that even the largest companies were not safe from M&A any more.

A hostile takeover pushes up the stock price of the target company as the acquirer and the incumbent controlling shareholders race to increase their shares. The stock price would rise even before the takeover process formally kicks off, with rumors of a possible takeover. Of course the stock price sharply falls back when the takeover fails. With deregulation in M&A, Korea experienced several stock price rallies for possible M&A targets. This paper investigates the stock price movements of the companies listed in Korea Stock Exchange in two events which had a strong and general impact on the possibility of hostile takeover affecting many of the potential M&A targets. The first one is when the Congress passed an amendment of the Securities and Exchange Act removing the 10 percent barrier in December 1993 but unexpectedly decided to delay its enactment by more than two years. The passing and immediate enactment of the amendment was widely anticipated, and the stock prices of many potential M&A targets had considerably appreciated in the run-up to the Congressional final decision (December 14th). The decision to delay its enactment was a surprise, and many stock prices tumbled at the news. The second event was in early 1997, when a takeover attempt toward Midopa failed because of an announcement by the Federation of Korean Industries (FKI) that its member firms will join the target to fend off the attack. FKI is the club of large Korean Chaebols, whose joint defense effort would frustrate any M&A attempt. This was an incident in which a Chaebol member became an M&A target for the first time, and the acquirers involved foreign capital. Midopa was a leading company in a Chaebol group, Daenong, which ranked 34 among Korean Chaebols. As the M&A effort made progress, Midopa's stock price sharply rose, and so did the stock prices of many other similar firms reflecting the expectation that they too can be M&A targets. The surprise FKI announcement ended such expectation. Again, many stock prices collapsed at the news.

These two events are similar in that widespread M&A expectation was suddenly crushed by surprise, ending and reversing a stock price rally of potential M&A targets. So they provide a unique opportunity to find which companies were regarded as potential M&A targets. They must be the ones whose stock prices strongly reacted negatively to the events. The two events are also similar in that they were largely unanticipated, making them suitable for event studies. The two events have differences, too. The first one is about regulation: a ban on hostile takeover is lifted but its implementation was delayed for more than two years. The second one is about the market environment: a large scale hostile takeover would not be tolerated by the leading Korean business community.

We examine the stock price reactions of the listed companies to see which companies were affected by the events. More specifically, we conduct regression analyses of cumulative abnormal stock returns around the event dates on such factors as corporate financial structures, corporate governance structures and profitability. The results show that the lift of M&A ban mostly affected small companies in financial trouble. The second event affected companies with controlling shares of many subsidiary firms but are not members of the leading Chaebols. Corporate governance related variables did not have significant effects on the stock reactions. These results imply that, in Korea, M&A was expected to be used as a means of expanding control over more affiliated companies instead of helping improve corporate governance. Especially, they show the market expectation that introduction of M&A would do little to improve the governance of leading Korean Chaebols.

There is a huge literature on M&A, and there are several survey articles summarizing the findings of existing works (Shleifer and Vishny (1988), Jarrell et at (1988), Scherer (1988)). Gaughan's book (Gaughan (1999)) also provides a good survey of the literature. They find that the target companies tend to be under-performers (Palepu (1986), Morck, Shleifer and Vishny(1988, 1989), and that most of the acquired companies experience management turnover (Martin and McConnell (1991)). There are also many studies about how the news of M&A affects the stock prices of the target companies and the acquiring companies. It is well known that the news positively affects the target stock price (Jarrell et al (1988)). However, Shleifer and Vishny (1997) argues that M&A alone cannot do much to improve corporate governance because it is costly and requires a well-developed capital market. They also argue that M&A can be abused as a means of expanding managerial influence and is subject to political interference.

Korea has a short history of hostile M&A with few real cases. So there aren't many empirical studies on hostile M&A in Korea. Most existing works focus on institutional details or the prospect for the future M&A market. Shin (1997) constructed a sample of the public companies that experienced turnover of the largest shareholder in the period of 1994-1996, regardless of the reason of the turnover. He then compared this sample with a comparison group. He found that the largest shareholders of the control sample tend to have relatively low shares, and that the companies in the control sample had lower profitability. However, their Q-values tend to be higher. There are studies on the M&A's registered in the Korea Stock Exchange, but few of these M&A's are hostile. Bae, Kang and Kim (2002) show that M&A news in Korea has a positive effect on the acquirer's stock price, but when the acquirer is a Chaebol member, the news has a negative effect. This suggests that Chaebol companies use M&A for the private benefit of the controlling families or the management at the expense of other shareholders. Lee, Byun and Park (2002) examine how stock price reactions to M&A news differ by the type of M&A and the attributes of the involved parties.

The remainder of the paper is organized as follows. Section 2 explains the two events that we consider in more detail. Section 3 discusses the data and methodology employed in the study, and Section 4 presents the results. Section 5 concludes the paper

2 The Events

2.1 Securities and Exchange Act Amendment in 1993

It was mostly thanks to Section 200 of the Securities and Exchange Act that there was no hostile takeover in Korea until 80's. Section 200 prohibited acquisition of more than 10 percent share of a public company by outsiders without the approval of the government authority or going through a tender offer. This provision was introduced in 1976 in order to protect the corporate founders. Though an hostile takeover was theoretically possible (by going through a tender offer), the provision reflected a social consensus disapproving hostile takeover.

Voices for changes began to emerge in early 90's, demanding repeal of Section 200. In 1991, the vice prime-minister Choi argued that the provision should be removed. By 1993, the discussion to removed the provision gained momentum. On Feburuary 16th, the Ministry of Finance announced a plan for deregulation which included repeal of Section 200 and approval of own-stock repurchasing. In June, the plan to amend the Securities and Exchange Act was reconfirmed. The amendment package also included countervailing measures strengthening the disclosure rule for over 5 percent share purchases. It also included a rule reducing the limit of preferred stock issues from 50 percent of the total stock issues to 25 percent. Since then, M&A has become the hottest issue in Korean stock market. Public companies with low ownership concentration or high asset value relative to the stock price drew a lot of attention. Broker dealer firms published lists of potential M&A targets, and in some companies, competition to accumulate shares erupted even before the amendment was enacted.

However, too much attention to M&A lead to a backfire, inducing a public opinion against a full-blown M&A war. A rumor that Samsung was preparing to takeover KIA Automobile created a great public concern that M&A will be used by the Chaebols to expand their territory by acquiring independent companies. The news that Samsung has been secretly accumulating KIA shares through its member financial companies such as Samsung Securities Co., Samsung Life Insurance, and Ankuk Fire Insurance confirmed this rumor and shocked the entire nation. KIA started defense tactics, encouraging its employees to purchase the company stocks. It also began a public campaign against Samsung's attempt, taking advantage of the negative opinion toward Chaebols. The prospect of the largest Chaebol taking over independent KIA pleased almost nobody in Korea. Samsung eventually gave in to the public opinion and implicit pressure from the government and aborted the pursuit.

After the incident, some members of the business community argued that the amendment should be postponed. The amendment was scheduled to be decided in December, but some Congress members expressed their concern about the amendment. As the finance subcommittee discussed the issue, the hope for the passing of the amendment went up and down, and so did the stock prices of potential M&A target companies. It turned out that the amendment was passed on December 14th, but its enactment was delayed from April of 1994 to early 1997. The same day, the stock prices of the potential M&A targets (the so-called asset stocks) tumbled. The following is a newspaper article about the market reaction to the news.[2]

"A compromise was reached on the amendment of Section 200 of Securities and Exchange Act to lift the 10 percent limit of stock purchases. The amendment was passed but its enactment was postponed by two and half years to early 1997. The stock market showed disappointment at this news, with M&A related stocks tumbling. The unexpected delay seems to be a negative shock. In the first half of the day, M&A related stocks rallied on the news that the amendment was likely to be passed as planned. But those stock prices tumbled in the afternoon after the news of postponement reached the market. Investors were apparently disappointed as they had believed that the amendment, sponsored by the Ministry of Finance, would pass the Congress. ..."

Figure 1 shows the stock price movements of the companies that were regarded as prime targets in the first M&A wave: Manho Steel, Sungchang, Bang-rim, Choongnam Spinning Co.

[2]Maeil Business Newspaper, December 15th, 1993.

Figure 1. The price movements of "asset stocks" around the announcement of the delayed enactment of the amended Securities and Exchange Act (normalized by the price level of June 1st, 1993).

2.2 Midopa

Though the enactment of the amendment was delayed to 1997, the fact the it was passed in the Congress had an impact in the M&A market. Since 1994, several small scale hostile takeover took place. A major takeover event took place in early 1997 just before the enactment of the amendment. It involved a large company, Midopa, which was a key member of a medium-sized Chaebol group, Daenong. First, rumors about a possible takeover threat for Midopa began to circulate, and then Shindongbang took the formal step of tender offer together with several large friendly shareholders such as Sungwon Construction. Midopa's parent company, Daenong, immediately began an all-out defense against the threat, issuing bonds with warrants in a large scale to increase friendly shares. The would-be acquirers involved foreign capital, which was still very rare in Korea. Once again M&A became a hot issue in Korea, and the stocks of similar companies rallied. Business presses suggested lists of potential M&A targets in the wake of Midopa takeover. They included medium-sized parent companies with controlling shares of many subsidiaries. Haitai Confectionary, Ssangyong Cement, Hanwha, Kolon, Doosan, Asia Cement were among the companies frequently mentioned. In fact, the stock price of Haitai rose 42.9 percent since the beginning of 1997. The stock prices of Doosan and Asia Cement rose 42.8 and 35.2 percent, respectively.

But the largest Chaebols of Korea jumped in Midopa's defense. The finance subsidiaries of Hyundai, Samsung and LG purchased Midopa's bonds with warrents in large numbers, blocking the takeover attempt. Further, the Federation of Korean Industries (FKI), a club of large Korean companies, made an announcement on March 11th that FKI members will act together against hostile takeovers in the future. This put an immediate end to the M&A frenzy, sending the stock prices of Midopa and other similar firms into a tailspin. The next day, a business newspaper ran an article saying,

Figure 2. The price movements of M&A related stocks around the announcement of the plan to act against hostile takeovers by Fedeartion of Korean Industries (FKI) (normalized by the price level of September 1st, 1996).

"As the business community announced that it would act together against hostile takeovers, the stock prices of Midopa related companies fell by the daily limit. So did the stock prices of many other similar companies that had been considered potential M&A targets."[3]

3 Research Methodology and Data

The day on which the decision to postpone the enactment of amended Securities and Exchange Act was otherwise a quite day without any particular events affecting the stock market. It is more or less the same with the day on which the FKI announced a plan to act collectively against hostile M&A. In 1993, the stock price increased sharply in a short period of time, but in December the stock market was relatively quite. The stock market was in a slump in early 1997 without any exciting issues. So we assume that our two events were the most important events around the respective event dates in the entire stock market. This implies that the stock price movements around the event dates indicate the extent to which the company was regarded as a potential target of hostile takeovers. Since both events had negative impact on the general possibility of hostile takeovers, we expect that a potential M&A target experienced a stock price decrease. That is, the more a company was regarded as a potential M&A target, the more its stock price decreased.

We first conduct event studies on all the sample firms to compute the cumulative abnormal stock returns (CAR) around the event dates. Then to figure out the attributes of the companies regarded as potential M&A targets, we regress the standardized CAR on the company characteristics.

More specifically, the dependent variable of the regression analyses are cumulative abnormal returns for 15 days (day -7 to +7), 7 days (day -3 to +3), 3 days (day -1 to +1), and 2 days (day 0 to +1) around the event dates. A market model is used to compute the cumulative abnormal return, which is then normalized by the standard error of the

[3]Maeil Business Newspaper, March 12th, 1997.

abnormal returns. The market model was estimated for the period of -300 to -60 day. Also since we are only interested in the negative effects of the two events and don't expect that the two events would have a positive effect on M&A targets, we substituted zero for any positive cumulative abnormal returns.[4]

Cumulative Abnormal Return ($CAR_{s,t}$) : sum of abnormal returns from the market model from day s to day t, divided by the standard error of the abnormal returns. Positive values are replaced by zero.

Three groups of explanatory variables are used: 1) corporate governance related variables; 2) variables related to company affiliation; 3) financial structure or performance related variables. The followings are the variables in each group.

1) Corporate governance related variables

LARGESH: The ownership share of the largest shareholder
FNI: Total ownership share of financial institutions
OTHI: Total ownership share of non-financial and non-government institutions
GRLOAN: loans to affiliated companies (relative to the asset size)
EXLOAN: loans to shareholders, exeuctives or employees (relative to the asset size)

2) Variables related to company affiliation and Chaebol membership

GR_10: A dummy variable for a member of top 10 Chaebol groups (as of 1995)
GR_30: A dummy variable for a member of top 11 to 30 Chaebol groups (as of 1995)
GR_65: A dummy variable for a member of top 31 to 65 Chaebol groups (as of 1995)
GR_non: A dummy variable for others

[4]The regression results are qualitatively the same without the normalization or the truncation of the abnormal returns.

GRINV: Investment in affiliated companies relative to the asset size

3) Financial structure or performance related variables

PBR: asset value per share / stock price(year end)
SIZE: log(asset)
FIX: fixed asset / asset
CASH: (cash and deposit) / asset
OPI: operating income / sales
DEBT: total liability / (total liability + market value(year end))

4) Others

12 industry dummies based on two digit industry codes.

The above variables and sometimes their interactive terms were included in the regression analyses. The implications of these variables are as follows. Among the corporate governance related variables, the ownership structure variables indicate the extend to which a hostile M&A is probable. When the ownership is highly concentrated with majority shareholders, hostile M&A's are not likely to succeed. However, the effect of the shares held by institutions (financial or non-financial) depends on which side the institutions are on. If the institutions are not affiliated, concentration of ownership on them may increase the possibility of a successful M&A. In 1990's, however, most of the financial institutions did not actively take part in corporate governance, and many of them were affiliated with the company. In this regard, high ownership by financial institutions are expected to have a negative effect on M&A possibility.

Loans to affiliated companies, shareholders, executives or employees are regarded as an indicator of bad corporate governance. Loans to affiliated companies used to be abused as a means of subsidizing other companies, which a well-functioning capital market would have denied. Loans to shareholders, executives or employees are often used for the purpose of tunneling corporate asset. A company experiences financial distress when it fails to recover large loans to insiders. For instance, SK Global, which experienced severe financial distress in 2003, caused trouble for other members of SK group which gave loans to SK Global. Jinro had about 200 million dollar loans to its chairman Jinho Chang when it filed bankruptcy in 2003. These examples suggest that loans to insiders indicate weak corporate governance, and that firms with more loans to insiders are more vulnerable to hostile takeover.

The dummy variables for affiliation with Chaebol groups are included to test whether members of large Chaebols are shielded from hostile takeover. Chaebol members are linked to each other through cross-shareholdings and are all under common control of the so-called "owner" family. They can act together to defend a member firm when it is under a hostile takeover threat. However, a company holding controlling shares of many subsidiaries is an attractive target of takeover. Once the acquirer takes over its control, it gains control of many other firms. In fact, in 1997 when Midopa was under attack, medium-sized holding companies got most attention as next takeover targets.

PBR is a measure of under-valuation of the stock. A stock with high PBR was called an 'asset stock' implying that it has relatively more asset compared with the stock price. These stocks are regarded as good long-term investment. FIX and CASH are included to test whether tangible assets or cashholdings make the firm a takeover target. Profitability variables are to test whether M&A targets are under-performers. The 12 industry dummies are to control unobserved industry effects that might have been caused by an industry specific event around the event date.

The sample consists of the listed companies in Korea Stock Exchange. The stock price data and other company data are taken from KIS-FAS2002. The companies with a negative net asset value were excluded.[5] The 1997 sample excludes Midopa and Daenong which were actual takeover targets.

4 Results

4.1 Securities and Exchange Act Amendment in 1993

[5]When these companies were included, we had very high correlation between PBR and OPI.

Table 1 shows the estimated regression models for the cumulative abnormal returns (CAR) around December 14th, 1993, when the Securities and Exchange Act amendment was passed with delayed enactment. A negative CAR value indicates that the stock price declined by more than average, implying that the firm was regarded as a probable target of the first M&A wave that would have occurred without the delay. Therefore, a large negative value of an estimated coefficient implies that the variable is positively related with the M&A possibility.

Table 1 shows that the factors contributing to stock price falls in the event period are more or less the same regardless of the length of the event period, except $CAR_{-1,1}$. They are SIZE (smaller size), CASH (lower cashholdings), DEBT (higher leverage), and OPI (lower profitability). These variables are mostly related to the financial strength of the company, and the signs of the coefficients suggest that financially weak firms were regarded as the prime target for the first M&A activities in early 1993. Among the corporate governance related variables, only FNI has significant effects, meaning that companies with more shares by financial institutions were more probable M&A targets. Neither GRLOAN nor EXLOAN, the two variables indicative of bad corporate governance, has a significant effect.

The models with shorter event period have much lower explanatory power. In the model with $CAR_{-1,1}$, none of the explanatory variables has a significant effect. The adjusted R^2 of 33 percent must be thanks to the 12 industry dummies. Without the industry dummies, the model loses most of the explanatory power. This may be because, on day -1, there were conflicting pieces of news about the prospect of the amendment passing the Congress. Up until the morning of December 14th, the market was optimistic about the amendment, pushing up the stock prices of potential M&A targets. The price falls on the second half of the 14th and the next day (15th) must have been offset by these earlier price movements. Then the total price changes for the three days of 13th, 14th and 15th might contain little information about the M&A possibility.

Table 1. Regression models of the cumulative abnormal returns around the event of announcement of delayed enactment of amended Securities and Exchange Act (December 14th, 1993)

Explanatory Variables	$CAR_{-7,7}$	$CAR_{-3,3}$	$CAR_{-1,1}$	$CAR_{0,1}$
SIZE	0.690***	0.492***	-0.056	0.201***
	(3.10)	(3.22)	(-1.00)	(3.23)
PBR	-0.268	0.132	-0.043	0.012
	(-0.96)	(0.69)	(-0.62)	(0.41)
DEBT	-3.517**	-2.145**	0.338	-1.062**
	(-2.48)	(-2.21)	(0.95)	(-2.67)
FIX	1.177	0.791	-0.247	-0.027
	(0.76)	(0.67)	(-0.62)	(-0.06)
CASH	6.570**	4.569**	-0.662	1.621*
	(2.03)	(2.06)	(-0.82)	(1.78)
OPI	6.592**	4.708**	0.019	1.438
	(2.06)	(2.14)	(0.02)	(1.60)
GRINV	-3.170	-3.170	-0.569	-0.745
	(-0.69)	(-1.00)	(-0.49)	(-0.58)
GRLOAN	2.684	-1.315	-0.700	1.140
	(0.60)	(-0.43)	(-0.62)	(0.90)
EXLOAN	10.948	9.134	-1.309	10.029
	(0.28)	(0.34)	(-0.14)	(0.92)
LARGESH	0.017	0.019*	0.003	0.006
	(1.12)	(1.89)	(0.80)	(1.47)
OTHI	0.002	-0.001	-0.002	-0.003
	(0.11)	(-0.08)	(-0.54)	(-0.85)
FNI	-0.040**	-0.035***	-0.006	0.0003
	(-2.20)	(-2.78)	(-1.41)	(0.07)
GR10	-0.752	0.108	-0.206	-0.070
	(-0.91)	(0.19)	(-0.99)	(-0.30)
GR11_30	0.793	1.054	0.079	-0.036
	(1.21)	(0.19)	(0.48)	(-0.20)
GR31_65	-1.365*	-0.650	-0.106	-0.120
	(-1.94)	(-1.35)	(-0.60)	(-0.61)
Nobs.	457	457	457	457
Adj R^2	0.65	0.63	0.33	0.50

Note: Each model included 12 industry dummies, the coefficient estimates of which are not reported. The numbers in the parentheses are t-values, and ***, **, * indicates significance at the 1 percent, 5 percent, and 10 percent level, respectively. The definitions of the variables are in Section 3 of the text.

The results from Table 1 do not exactly support the newspaper analyses of the event. Many newspaper articles predicted that the so-called asset stocks will be prime targets of hostile M&A. But our results show that PBR did not have significant effect on M&A possibility at all. Neither did FIX, the ratio of fixed asset. Instead, our results suggest that small and financially weak companies experienced the biggest price decreases in the event period. In other words, they were the companies that the market expected to be the first M&A targets in Korea.

4.2 Midopa in 1997

Table 2 is for the event of the Midopa incident in which the large business community announced a plan to act against hostile M&A. Here again, some variables have significant effects regardless of the event period, but they are not the same as in Table 1 DEBT, GRINV, and OTHI have significant effects. But OPI, CASH, SIZE and FNI have much weaker effects than in 1993.

The weaker effect of SIZE is consistent with the story that the takeover attempt for Midopa expanded the potential M&A targets beyond small firms. The strong coefficients of GRINV supports the argument that the M&A targets after Midopa would be the companies similar to Midopa. As explained before, Midopa was a member of a medium-sized Chaebol group, Daenong, and held controlling shares of many subsidiaries. Didopa played the role of a holding-company in the group. The strong negative effect of OTHI is confusing. If the institutional block shareholders are friendly forces, their share would discourage M&A. However, if they are neutral, they can be teamed up with the acquirers, facilitating the takeover.

Table 2. Regression models of the cumulative abnormal returns around the event of announcement of a plan to act against hostile takeovers by FKI (March 11th, 1997)

Explanatory Variables	$CAR_{-7,7}$	$CAR_{-3,3}$	$CAR_{-1,1}$	$CAR_{0,1}$
SIZE	-0.016	0.162	0.181***	0.154**
	(-0.13)	(1.40)	(2.61)	(2.55)
PBR	0.396*	0.135	0.241**	0.182*
	(1.89)	(0.67)	(2.00)	(1.73)
DEBT	-1.371*	-1.743**	-1.343***	-1.011**
	(-1.69)	(-2.20)	(-2.84)	(-2.45)
FIX	-0.874	-0.179	-0.792*	-0.654
	(-1.06)	(-0.22)	(-1.66)	(-1.57)
CASH	-0.516	0.360	-0.582	-0.487
	(-0.32)	(0.23)	(-0.62)	(-0.59)
OPI	0.439	-0.596	-0.845	-0.376
	(0.32)	(-0.45)	(-1.07)	(-0.55)
GRINV	-6.779***	-6.197***	-1.549	-2.489***
	(-3.38)	(-3.18)	(-1.33)	(-2.80)
GRLOAN	-1.106	-0.504	-0.088	-0.396
	(-0.45)	(-0.21)	(-0.06)	(-0.32)
EXLOAN	-9.464	-6.865	-5.168	2.136
	(-1.49)	(-1.11)	(-1.41)	(-0.67)
LARGESH	0.007	-0.004	-0.007	-0.004
	(0.84)	(-0.54)	(-1.53)	(-0.93)
OTHI	-0.017**	-0.015**	-0.011***	-0.010***
	(-2.31)	(-2.10)	(-2.62)	(-2.75)
FNI	0.008	-0.009	-0.015**	-0.009
	(0.71)	(-0.85)	(-2.39)	(-1.61)
GR10	-0.624	0.036	0.238	0.216
	(-1.45)	(0.09)	(0.95)	(0.99)
GR11_30	0.132	0.004	0.051	0.236
	(0.35)	(0.01)	(0.23)	(1.22)
GR31_65	-0.656*	-0.318	-0.450**	-0.112
	(-1.70)	(-0.85)	(-2.01)	(-0.58)
Nobs.	501	501	501	501
Adj R^2	0.38	0.41	0.49	0.44

Note: Each model included 12 industry dummies, the coefficient estimates of which are not reported. The numbers in the parentheses are t-values, and ***, **, * indicates significance at the 1 percent, 5 percent, and 10 percent level, respectively. The definitions of the variables are in Section 3 of the text.

To investigate the effects of GRINV and OTHI in more detail, we interacted them with the dummy variables for the Chaebol membership. Table 3 shows the results.[6] The effects of GRINV vary depending on the Chaebol membership. It has no effect for the firms belonging to top 30 Chaebols but has a very strong effect for the firms in top 31 to 65 Chaebols. This results is consistent with the story that holding companies of small to medium sized Chaebols were thought to be the next M&A targets. OTHI has effects only for non-Chaebol firms in three out of four models, implying that, for the non-Chaebol firms, the institutional shareholders are not necessarily friendly to the incumbent management. In other words, they were not affiliated with the company. However, the strong coefficient of OTHI for top 10 Chaebol firms in the model with $CAR_{7,7}$ is hard to explain.

Comparing the results in Table 1 and Table 2, we can see the differences in the effects of the two events. In 1993, when hostile M&A would have been first introduced in Korea, it was mostly small and weak companies that were regarded as the targets of the first M&A activities. But when an actual takeover attempt was made against Midopa, which was a large company belonging to a Chaebol group, the market expectation changed. Instead of small and weak companies, acquirers would choose a target that will expand their control over many companies. GRLOAN and EXLOAN did not have significant effects in either event, suggesting that M&A's were not considered as a means of improving corporate governance. It was rather considered as a means of increasing the size of the assets under the acquirer's control.

[6]Table 3 does not show the coefficients of other variables.

5 Concluding Remarks

The amendment of Securities and Exchange Act to allow hostile takeover was a first step in deregulation of the Korean capital market. But in 1993, when the amendment was first to be enacted, there still remained many other implicit or explicit restrictions in the capital market against hostile takeovers. As witnessed in the Samsung-KIA incident, the government and the general public were both against the idea of a larger company taking over a smaller company. The incident showed how deeply the Korean public was concerned about Chaebols' growing influence in Korea. Also there was restriction on foreign capital in purchasing Korean stocks. Under these circumstances, the market must have expected that an hostile takeover would be allowed only if the target company is small and in trouble. In other words, takeover would be justified only if the company needed external help.

The Midopa incident showed that the market expectation has changed a lot during the three years from 1993 to 1997. The passing of the enactment itself had the effect of changing the general perception toward hostile takeover. They were not regarded as an unethical act of infringing upon other peoples' right. As a result, some M&A activities began even before 1997. They used tender offers, which were already allowed. Several hostile takeover activities targeting merchant banks were reported. In 1994, the prices of preferred stocks sharply declined across the board. It may be because preferred stocks do not have voting rights

The takeover attempt toward Midopa showed the market that even large firms with Chaebol membership can be an M&A target, unless they belongs to leading Chaebols. Further, foreign capital was involved in the takeover attempt, and the government did not interfere with the attempt. All these changes lead the market to believe that a company as big as Midopa could be taken over against its will. And the market expected that the most likely targets of the coming M&A wave would be the companies playing the role of holding companies of medium-sized Chaebols.

Hostile takeover has two opposite implications on corporate governance. On one hand, it can improve corporate governance by removing entrenched management. On the other hand, it can help the incumbent managers expand the business under their control. The results of this paper suggest that the Korean capital market expects the second effect will be greater.

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