Why Do Firms Sell Out? Separating Targets' Motives from Bidders' Selection of Targets in MA

Zha Giedt, Jenny

George Washington University

23 August 2017

Why Do Firms Sell Out?

Separating Targets' Motives from Bidders' Selection of Targets in M&A

Jenny Zha Giedt*

George Washington University

zhagiedt@gwu.edu

This version: August 23, 2017

This paper explores why firms seek strategic alternatives, effectively putting themselves up for sale in the market for corporate control. Using a sample of firms that are observed to be exploring strategic alternatives, I model (1) the self-selection of firms to become potential takeover targets, which is distinct from (2) the selection of targets by bidders. The findings suggest that firms seek strategic alternatives because they are performing poorly and face financial constraints, yet corporate governance mechanisms prompt the disruptive attempt to maximize shareholder value. In contrast, the subset of firms that actually receive bids have relatively better growth prospects and performance, and lower market risk – which suggests that bidders do not prefer under-performing targets, contrary to conventional thought. The largely contrasting profiles of firms that are volitionally supplied by sellers versus demanded by bidders modify our conventional understanding of target firms' motives and target selection in M&A.

Keywords: strategic alternatives; mergers and acquisitions; target motives; takeover prediction; financial constraints; deal initiation; voluntary disclosure; media leaks

JEL classifications: D84, G34, M21

Data availability: publicly available

---

* Correspondence address: 2201 G Street NW. Funger Hall, Suite 601. Washington, DC 20052. I appreciate helpful comments received from Michael Kimbrough, Todd Kravet (2017 AAA discussant), Oded Rozenbaum, and participants at the 2017 Washington Area Research Symposium. This paper is based in part on my dissertation at UC Berkeley ("Voluntary Disclosure of Strategic Alternatives: A Cost-Benefit Analysis") for which I thank my committee members, Richard Sloan (Chair), Michael L. Anderson, Patricia Dechow, Alastair Lawrence, and Panos Patatoukas. While this paper focuses on the antecedent determinants of seeking strategic alternatives, I refer readers interested in the future effects of disclosing strategic alternatives to a related paper, "Economic Consequences of Announcing Strategic Alternatives."

1. Introduction

Seeking "strategic alternatives" is jargon for exploring the potential sale or merger of the company in the precursory mergers and acquisitions (M&A) setting. Whether to pursue strategic alternatives is one of the most disruptive corporate decisions a company faces in its lifetime, since the firm that seeks strategic alternatives is calling into question its future existence as a stand-alone entity. As the transactional landscape moves away from hostile takeovers that dominated the 1980's and earlier decades and towards predominately friendly takeovers in the 1990's and beyond, it is increasingly important to understand the motives behind this category of takeovers, where the selling side is amenable to being sold. This study focuses on the sell-side and seeks to illuminate, first, why firms set out to explore strategic alternatives, by characterizing the attributes of firms that are volitionally seeking their own sale. The analyses naturally lead to additionally documenting what attributes make target firms desirable to bidders, by examining the characteristics of firms that actually receive bids from the sample of self-selected potential target firms. While the "supply" of selling firms is inherently distinct from the *ex-post* targets demanded by bidders, prior papers have not been able to distinguish between the two. This paper aims to rectify this limitation.

A review of strategic alternatives is the catalyst to the sale process, yet this event has been largely overlooked by M&A researchers. In this process, the company's directors and executives consider and evaluate a possible sale or merger of the company; members of the company board may form a Special Committee to discuss whether it is an appropriate time to seek potential buyers and what a third party may be willing to pay for the company. The senior management and the Special Committee retain an investment bank as the financial adviser, who contacts third parties to gauge their interest in a potential acquisition. The company seeking strategic alternatives may enter into separate confidentiality agreements with potential acquirers, and provide confidential and non-confidential company information to them in the course of due diligence. Some firms' strategic reviews will result in bids while other firms' reviews will not.

In this amorphously defined sale process, I observe which firms are exploring strategic alternatives (identified by corporate disclosures and media leaks) and which firms become actual targets (identified by the receipt of merger bids). To the extent that I do not observe all the firms seeking strategic alternatives or all the firms receiving bids, the respective empirical results would be understated.

Understanding target takeover motives and common attributes of target firms is a key component to understanding why takeovers occur from the target firm's perspective, and this topic is relevant to managers and directors, investors, and sell-side and buy-side advisers. Takeovers can occur for many reasons, such as being driven by the stock market or by rational efficiency, behavioral biases, or agency problems of acquirers.[1] However, from the target firm's perspective, conventional wisdom predominantly supports the value-maximizing, efficiency explanation of takeovers, also known as the "q-theory" or "inefficient management" hypothesis. According to economic theory, acquirers choose as targets the relatively undervalued and underperforming firms that are in need of a major restructuring of corporate assets and an overhaul of inefficient management. The acquirer takes control to discipline or replace the inefficient managers who have mismanaged the firm's assets and caused the firm to be undervalued (Jensen, 1986, Shleifer and Vishny, 1988).

Despite the theoretical literature, empirical evidence has not come to a consensus about the typical profile of a target firm (e.g., Agrawal and Jaffe, 2003; Rhodes-Kropf and Robinson, 2008). Even if prior papers do come to a consensus about the antecedent characteristics of target firms, it has been impossible to infer target firms' takeover motives, due to confounding effects of bidders' selection and shareholder and regulatory approval tainting the sample. An analogous sample and research design flaw is akin to inferring the determinants of targets receiving bids using targets of completed transactions.[2]

[1] There are other purported determinants of takeovers due to the acquiring firm's agency problems, such as excess cash flow, managerial hubris, and empire building. However, this paper focuses on the target's, not acquirer's, determinants of takeover activity.

[2] Wong and O'Sullivan (2001) review the reasons these two events are not equivocal.

Moreover, the guiding economic theories of mergers require an acquirer to do the disciplining or exploit the synergies, which leaves no clear interpretation for what the target firm's motives are for entering the M&A sale process before an acquirer materializes.

A sample of potential target firms that are seeking strategic alternatives—before they become actual targets—is a cleaner setting to uncover the targets' pure motives for M&A, before bidders come into the picture and before shareholder approval and regulatory approval bias the sample selection. In my setting, firms self-identify that they are amenable to a possible takeover and henceforth become *potential* target firms. The first set of analyses models the selling firms' self-selection to explore their own sale or merger, and identifies the fundamental, market, managerial, and ownership characteristics that, on average, influence this decision.

The unanswered question of why firms seek to be taken over is further motivated by anecdotal evidence, which piques our interest with a spectrum of possible target motives. For example, firms may seek strategic alternatives when they are facing financial constraints and their valuations have reached a bottom. In October 2014, The Financial Times leaked that Angie's List was exploring strategic options, including the possible sale of the business (Appendix 1, Panel A). Angie's List had just restructured its debt and its shares were trading at its 52-week low. In contrast, firms in a growth state and high performance may also seek to sell themselves to an acquirer with resources to sustain the growth and performance. In October 2014, Conn's announced that it was exploring strategic alternatives, including the possible sale of the company (Appendix 1, Panel B). Conn's grew same-store sales and diluted EPS for fiscal 2014 by +26.5 percent and +62.8 percent, respectively. However, its credit-financing business struggled due to increased delinquencies and deteriorating credit scores. Therefore, an empirical approach can characterize what the typical firm seeking strategic alternatives looks like, with respect to its financial condition, performance, and other properties such as its market, managerial, and ownership characteristics.

I observe firms that seek strategic alternatives and voluntarily announce it through corporate disclosures and I also observe firms that intended to shop themselves privately yet were involuntarily leaked by the media. Additional insight can be gained about the different types of firms that utilize each of these two information channels. Firms that announce strategic alternatives using corporate disclosures are likely to be smaller firms with lower analyst coverage and experiencing curtailments. Their managers appear over-optimistic and inaccurate, and their incentives are aligned in the short-term, but not long-term, horizon (i.e., more likely to have golden parachutes, but less insider ownership). In contrast, firms with leaked strategic alternatives are distinguished from their peer firms by having higher valuations, greater operating cash flows, and greater analyst coverage. These findings imply that less visible firms with less able managers choose to announce strategic alternatives in response to declining stock prices and operations, whereas firms with greater visibility are more likely to have their strategic reviews leaked by the media.

I interpret the common attributes across both information channels as the firm determinants that reveal why target firms are motivated to sell themselves. Results reveal significant differences between firms that seek strategic alternatives and their industry-year peers. On average, firms seeking strategic alternatives have worse financial condition and worse performance (higher leverage, lower liquidity, lower revenues, lower prior returns, and lower EPS growth forecasts) than their industry-year peers. However, they have higher blockholder ownership and a higher incidence of golden parachute provisions, which may help monitor and align incentives of managers and directors so that they may maximize shareholder value through strategic alternatives. The self-selection process can be interpreted as: firms with financial and operational problems are desperate for a strategic solution, and in addition, monitoring by blockholders and the presence of short-term financial incentives can prompt the managers and directors to take action.

A question that naturally follows is, what attributes distinguish firms that actually receive bids? The sample of firms seeking strategic alternatives serves as a known supply of potential target firms,

which also allows a cleaner setting to model the bidders' selection of actual targets, thus revealing the desirable firm attributes demanded by bidders.[3] In light of the financially and operationally unhealthy nature of firms seeking strategic alternatives, an element of perceived growth potential and increasing investment needs may attract an acquirer that can provide value to the selling company's stockholders; otherwise, the potential target firm could undergo bankruptcy or recapitalization rather than a merger or acquisition. From those firms that are knowingly "on the block," 44 percent receive at least one merger bid within one year, and 51 percent receive at least one bid within two years. The probability of receiving a bid is increasing in perceived growth prospects, operating performance, and blockholder ownership, and decreasing in market risk – attributes that are plausibly desirable to an acquirer.

The striking takeaway that's only possible by modeling the two selection processes separately (the targets' self-selection and the bidders' selection) is that while firms seeking strategic alternatives appear to be low types (based on fundamentals, market prices, and analyst expectations), those that actually end up with bids are the relatively better picks in the barrel. In contrast to the inefficient target management hypothesis of mergers, which predicts that bidders choose to acquire underperforming firms, I find that bidders try to acquire firms with greater opportunities, better operations, and lower market risk. This conclusion can be plausibly reconciled to earlier papers because the incidence of hostile acquisitions (which would discipline inefficient target managers) is rare in my post-1990 sample period (Andrade, Mitchell, and Stafford, 2001). Henceforth, I suggest that readers interested in the M&A sale process could update their prior expectations of how the selection process works with these findings from a more recent time period. In the post-1990 period when transactions are overwhelmingly friendly, the operationally- and financially-challenged sellers appear to start disciplining themselves, and bidders

[3] This characterization of the target's sale process does not apply to hostile takeovers. The generalizability of this study is not hindered because hostile takeovers are rare in the post-1990 sample period used in this study. Andrade, Mitchell, and Stafford (2001) find that merely 4 percent of transactions in the 1990's were hostile.

do not prefer to pick the relatively poorly-run, undervalued or mismanaged targets—rather, I find evidence to the contrary.

Finally, this paper provides evidence on the role of corporate governance as an important factor in the preliminary M&A sale process. The presence of golden parachute provisions appears to prompt managers and directors to seek a sale of their company, but parachutes do not appear to be an influential factor in the probability of receiving a bid. The presence of institutional blockholders, however, appears to be positively influential at both stages. This finding is consistent with blockholders active monitoring directors and managers, and bidders' preference for targets with better corporate governance (Shleifer and Vishny, 1986).

The rest of the paper is organized as follows. Section 2 motivates the research questions and highlights the contributions of this paper. Section 3 describes the data and sample construction. Section 4 describes the research design and empirical measures. Section 5 presents the results. Section 6 concludes.

2. Research Questions and Contribution

Bolstered by much empirical work before and during the 1980's, M&A researchers conventionally view takeovers as a control device or as a mechanism to achieve synergies between two combining firms. Under the control perspective, takeovers are disciplining mechanisms to monitor the firm's management team and replace it when necessary, when other corporate governance mechanisms, like the board of directors, fail (Jensen, 1986; Shleifer and Vishny, 1988). Takeovers lead to the replacement of managers whom the board is unable or unwilling to discipline. This disciplining theory for M&A predicts that targets are undervalued and underperforming companies, due to industry-wide problems or firm-specific problems. Firms in more difficult external operating environments are expected to become M&A targets.[4] Although the disciplining theory does not distinguish between

[4] Pastena and Ruland (1986) and Amit, Livnat, and Zarowin (1989) provide evidence of firms becoming takeover targets in order to avoid the costlier alternative of bankruptcy. The empirical implications of the bankruptcy hypothesis are

whether such firms voluntarily seek to become M&A targets or are involuntarily targeted by hostile bidders, the consensus from empirical research is the latter (Morck, Shleifer, and Vishny, 1988). In contrast, this paper provides novel evidence that firms facing financial and operational difficulties appear to "self-discipline" (with corporate governance monitoring and aligned incentives) by voluntarily reviewing strategic alternatives.

The relevant literature is comprised of empirical papers that examine the financial, investor, and governance characteristics of actual takeover targets (e.g., Hasbrouck, 1985; Palepu, 1986; Ravenscraft and Scherer, 1987; Morck, Shleifer, and Vishny, 1989; Powell, 1997; Agrawal and Jaffe, 2003). These prior empirical papers test possible target motives by identifying differences between actual target firms and non-target firms. Despite the generally-accepted prediction that targets are underperforming and undervalued firms, empirical studies come up with mixed findings. Furthermore, for any empirically significant target firm attribute, do firms seeking to sell themselves display that attribute, or do bidders select for that attribute? The paper addresses two related research questions to provide new insight to this debate.

Research question 1: *Why do firms seek strategic alternatives (by examining the determinants of firms that seek strategic alternatives, compared to their industry-year peers)?*

Research question 2: *Why do certain firms receive bids while others do not (by examining the determinants of firms that receive a bid, compared to those that seek to sell themselves but do not receive a bid)?*

The main contribution of this paper to existing literature is two-fold. A sample limitation of the prior research is that they do not observe firms that attempt to initiate a sale but were not met with interest from bidders, nor do they observe targets of bids that were not successful. The prior studies' samples are based on target firms that received bids or targets that were actually acquired, which likely

indistinguishable from the target inefficiency theory; target firms have higher financial leverage than the general population of firms.

includes *ex-post* sample selection bias. The first contribution of this paper is to address this issue by using a novel dataset of firms that are exploring strategic alternatives, which includes even those do not receive bids and therefore are not acquired. This is a plausibly cleaner setting that can inform us about target motives, before selection by bidders, shareholder approval, and regulatory approval come into play. Moreover, prior studies treat the two selection processes (seeking strategic alternatives and being an acquisition target) as one amalgamated process, which presents a problem in empirical studies modeling target selection. Therefore, the second contribution of this paper is to model target motives and target selection as two selection processes, rather than in one step.

To see why a cleaner setting and two-step selection model can change our priors, consider the following example. Suppose that from the entire population of firms, those with low attribute x will seek strategic alternatives. However, bidders prefer and only make offers to targets with relatively high x. Although x is a sell-side motive and a distinct attribute of target selection, the association between x and being an *ex-post* observed target may be statistically insignificant or mixed when prior researchers do not observe the intermediate sample of firms seeking strategic alternatives. This would cause researchers to incorrectly fail to reject the null that x is not an important determinant in target selection. My results suggest that the prior literature's mixed conclusions about the role of target (under)performance could potentially be due to this problem.

Empirical studies of whether targets are underperforming or undervalued firms have produced mixed evidence. Agrawal and Jaffe (2003) conclude that target firms are not underperforming firms with respect to their prior operating earnings and prior stock returns. Palepu (1986) and Ambrose and Megginson (1992) find conflicting results about whether poor prior stock market performance is related to the probability of takeover. Hasbrouck (1985) and Morck, Shleifer, and Vishny (1988) provide conflicting evidence on whether Tobin's Q is negatively related or not related to the likelihood of takeover. Morck, Shleifer, and Vishny (1988, 1989) analyze 40 target firms that were acquired in hostile acquisitions and 34 in friendly acquisitions. Their multiple regressions show that only hostile targets,

not friendly targets, have lower Tobin's Q, abnormal stock returns, and employee growth. "Targets of friendly acquisitions have Tobin's Q comparable to that of nontargets… Friendly targets are…basically indistinguishable from the sample as a whole [Fortune 500 firms] in terms of performance variables" (p.103). Their evidence suggests that the acquirer disciplines underperforming, badly-managed target firms using hostile acquisitions, whereas the willing targets of friendly acquisitions do not appear to be distinguished by poor performance. In contrast, my evidence suggests that unhealthy firms seeking strategic alternatives are willing to become takeover targets. Since I also document that bidders select targets that are relatively healthier, prior empirical papers may have muddled the two confounding effects when examining targets of friendly transactions.

With respect to other firm characteristics, prior papers have found that targets are smaller (Hasbrouck, 1985; Palepu, 1986; Morck, et al., 1988; Ambrose and Megginson, 1992; Powell, 1997; Cornett, Tanyeri, and Tehranian, 2011), have lower liquidity (Powell) or higher liquidity (Hasbrouck), lower growth (Palepu), higher leverage (Powell), higher free cash flow (Powell), and a higher portion of tangible fixed assets to total assets (Ambrose and Megginson).

Note, however, that even though prior studies use *ex-post* target samples, they vary in their definition of the target firms (i.e., targets that receive bids or targets of completed transactions?) and vary in their choice of a comparison sample; see Exhibit 1. Prior papers partitioning on deal characteristics have compared acquired targets of friendly deals against acquired targets of hostile deals (Morck, Shleifer, and Vishny, 1988, 1989). Papers have also compared acquired targets in target-initiated deals against acquired targets in acquirer-initiated deals (Aktas, de Bodt, and Roll, 2010; Fidrmuc and Xia, 2017).[5] While initiating the sale of the firm and exploring strategic alternatives both reflect a firm's willingness to sell itself, the prior studies do not observe firms that seek strategic

[5] Aktas, et al. (2010) examine the determinants of target-initiated deals using a sample of completed M&A transactions. They find that firms with lower Tobin's Q, lower institutional ownership, and higher institutional shareholding concentration are more likely to initiate their own sale compared to targets of completed deals initiated by the acquirer. Return-on-assets and sales growth are not associated with the probability of target deal initiation.

alternatives but do not receive a bid and become acquired, which introduces sample bias. Omitted firms could have displayed legitimate target motives but they do not appear in a sample of targets using only completed acquisitions.

In general, because prior research only considers the takeover process as it evolves from the initial bid to deal completion, there is no extant analysis about firms that seek to sell themselves and those that succeed versus fail at obtaining an offer.[6] Once a firm has started reviewing strategic alternatives, it is unclear whether it will continue on the M&A sale process and whether or not it receives an offer from an interested buyer. If a firm does not proceed with the sale process, it could attempt to increase shareholder value as a stand-alone entity and/or through more painful alternatives such as restructuring, selling off assets, laying off employees, and reducing wages. Yet, no paper has yet examined why some selling firms fail to receive a bid. Some papers use a sample of target firms who received bids and compare the firm attributes of those in completed versus failed deals.[7]

Additional contributions of this paper include providing evidence on the role of corporate governance in firms attempting to salvage firm value with strategic alternatives, and distinguishing between the firms that transmit strategic alternatives information via corporate disclosures versus media leaks. My findings are consistent with large institutional owners actively monitoring firm performance under classical theory (Edmans, 2014) by prompting the evaluation of strategic alternatives and blockholder ownership being a desirable trait. However, I do not find evidence that firms seeking strategic alternatives nor those that receive bids have greater activist ownership compared to their peers, which fails to support the role of activists as catalysts for M&A (Brav, et al., 2008). The presence of

[6] Zha Giedt (2017) provides the only extant empirical description of firms seeking strategic alternatives, but that paper focuses on the future economic outcomes following the announcement of strategic alternatives, rather than the antecedent determinants. Boone and Mulherin (2007, 2008) mention strategic alternatives in their description of the sale process, but they do not use any empirical constructs or tests based on strategic alternatives data.

[7] Asquith (1983) finds that the cumulative excess returns (days -480 to -5) of successful target firms are lower than those of unsuccessful target firms, though both groups of targets experience negative prior returns. In contrast, Malmendier, Opp, and Saidi (2016) find that the mean target firm's Tobin's q is weakly higher in completed deals than in failed deals. De Bodt, Cousin, and Demidova (2014) and Marquardt and Zur (2015) also characterize the targets of completed deals relative to those of failed deals. See Exhibit 1.

golden parachutes, while often viewed unfavorably as a proxy for managerial entrenchment, appears to be a favorable governance mechanism to neutralize the job loss disutility of managers and directors when they put the firm up for sale.

Finally, the differing determinants of firms voluntarily disclosing strategic alternatives versus firms leaked by the media (i.e., involuntary disclosure) highlight the characteristics of firms and their information environment that predispose some to take control of their company news versus getting leaked. My findings suggest that firms with low visibility in the market may seek to proactively disseminate news themselves (Healy, Hutton, and Palepu, 1999), whereas firms with more robust information intermediaries and visibility in the market experience involuntary news dissemination.

3. Data and Sample Construction

This study uses a unique hand-collected sample of firms seeking strategic alternatives during 1990 to 2014. I search on DirectEdgar for 8-K Filings and on Factiva for media leaks and press releases. Factiva's news sources include The Financial Times, The New York Times, Dow Jones Institutional News, Business Wire, PR Newswire, The New York Post, The Wall Street Journal, The American Banker, The Fly on the Wall, Bloomberg, The Boston Globe, Market Watch and Reuters News. I search for various combinations of the following key words and phrases (where * represents a wildcard): review*, assess*, evaluat*, consider*, strategic, alternatives, options, sale of the company, merger of the company, retained, engaged, advisor, special committee, board, maximize, enhance, shareholder, stockholder, value. I also review observations from SDC of target firms that are "seeking a buyer" after verifying the related 8-K Filing, media leak, or press release. I review each article to exclude search results that are false positives: announcements of a bid, announcements of a definitive agreement, announcements where only a division or limited assets are up for sale, and announcements of fire sales during bankruptcy proceedings. See Appendix 1 for two examples of firms seeking strategic alternatives in my sample; Panel A is a media leak, and Panel B is a voluntary corporate disclosure.

Table 1 shows that, after requiring non-missing key variables, my sample consists of 1,006 corporate disclosures (*SA_DISC*=1) and 151 media leaks (*SA_LEAK*=1) from 1990 to 2014. 20 firms that disclosed their strategic reviews after media leaks are only counted once, resulting in 1,137 total strategic alternatives observations (*SA*=1). To the extent that my manual data collection missed some strategic alternatives observations, my results are likely to be understated.

I require non-missing total assets ($ASSETS_{i,q}$), market value of equity ($MKVAL_{i,q}$), book-to-market of equity ($BTM_{i,q}$), leverage ($LEV_{i,q}$), cash and equivalents ($CASH_{i,q}$), change in quarterly earnings ($\Delta EARN_{i,q}$) from the same period in the prior year, quarterly cash flows from operations ($CFO_{i,q}$), quarterly cash flows from investing activities ($CFI_{i,q}$), quarterly operating accruals ($ACC_{i,q}$), prior 12-month market-demeaned returns ($RET_{i,y}$), and CAPM beta ($BETA_{i,y}$). I do not require other less populated variables to be non-missing in order to maximize my sample size. See Appendix 2 for variable definitions and data sources. All variables except returns are winsorized at 1 and 99 percent.

The strategic alternatives observations are compared with their peer observations taken from the same industry-years. When separately comparing the corporate disclosure or media leak subsamples to peer firms, respective industry-year subsamples of the peer group are used. No firm appears in the sample more than once every four quarters, to avoid the possibility that a firm is categorized as a strategic alternatives firm in one quarter and as a comparison peer firm in an adjacent quarter.

4. Research Design and Antecedent Firm Attributes

The general research design is straightforward and follows a case-control methodology partitioning on the variable of interest. To answer the first research question, I compare firms that disclose strategic alternatives (*SA_DISC* =1) to their industry-year peer firms (*SA_DISC* =0), and firms that seek strategic alternatives and have it leaked by the media (*SA_LEAK*=1) to their peers (*SA_DISC* =0). Since firm attributes may also impact the mode of information transmission, only the common attributes are interpreted as the determinants of seeking strategic alternatives. To answer the second research question, I start with the sample of firms that are seeking strategic alternatives (*SA*=1), and

compare firms that subsequently receive bids within one year (*BID1YR*=1) to those that do not (*BID1YR*=0).

The claim that the target selection reflects two different selection processes—the self-selection driven by the potential target firm's takeover motives, and the selection of the actual target by the bidder—is by no means clean-cut. There is undoubtedly going to be some muddling of the two processes, notably when a firm seeks strategic alternatives because it anticipates that it will be a desired target. If this were a significant issue, I would likely find the same determinants when modeling the probability of seeking strategic alternatives and when modelling the probability of receiving a bid. However, because I do not find a common set of determinants that influence both selection processes, the two selection processes appear to be distinct. Blockholder ownership is the only variable that is significant in both processes.

In order to analyze multiple facets of firms that seek strategic alternatives and firms that receive bids, the variables of interest encompass financial measures of firm condition and performance, market-based measures of risk ad returns, analyst coverage and expectations, proxies for managerial ability and contracting, and ownership structure. These antecedent firm characteristics are all measured using the most recent annual, quarterly, or monthly data from a prior period. Univariate analyses allow for the maximum number of observations to be used, while multivariate analyses test only the variables that are most populated in the data. I explain the variables of interest below.

4.1 Antecedents: financial condition and performance variables

The firm's financial condition is described using size (*ASSETS* and *MKVAL*), leverage (*LEV*), and liquidity (*CASH* and *INTAN*). The importance of firm size as a firm attribute is straightforward. Prior studies observe that targets tend to be smaller firms than non-targets (Hasbrouck, 1985; Palepu, 1986; Morck, et al., 1988; Ambrose and Megginson, 1992; Powell, 1997; Cornett, et al., 2011). However, it is unclear whether smaller, more volatile firms are more likely to find themselves in a situation needing to review strategic alternatives, or smaller firms are easier to sell, because a smaller target means less

financing for bidders to procure and easier post-transaction integration. Another reason firm size could be influential in the M&A sale process is that in larger firms, ownership is more dispersed, leading to a free-rider problem because many minor shareholders are unlikely to devote resources to pressure management enforce valuation maximization.

Firms burdened by high levels of debt and low liquidity may be more likely to seek a strategic out and monetize shareholder value by getting acquired. The firm's leverage (*LEV*) may be an important attribute to look at since greater debt pushes the manager to undertake risky but highly profitable actions, reflects monitoring by bondholders, and beyond some point, threatens the firm with bankruptcy and reorganization costs (Jensen and Meckling, 1976). An extremely high level of debt may lead firms to seek a sale as a way to get financial resources from an acquirer and avoid more painful alternatives like bankruptcy or restructuring (Pastena and Ruland, 1986; Amit, Livnat, and Zarowin, 1989). On the other hand, an extremely low level of debt may signal adverse selection problems, managerial incompetence, and hence be associated with takeover likelihood.

The proportion of assets that are liquid cash (*CASH*) may be a motive takeover due to the 'growth-resource imbalance' in the target (Palepu, 1986; Powell, 1997). For example, high growth firms with low resources (i.e., low liquidity and high leverage) may be ideal targets for bidders with the opposite imbalance (i.e., low growth prospects, but high liquidity and low leverage). In addition, the proportion of assets that are intangible (*INTAN*) provide another view of a firm's financial condition, since firms with high leverage, low cash and cash equivalents, and a high level of intangibles may find themselves in a financial bind and thus seek strategic alternatives.

Several measures of expected and operating performance are used. *BTM* is the book-to-market ratio of common equity. I use the level of *BTM*, calculated using the most recent quarterly financial numbers, to capture investors' timely evaluation of the firm's growth prospects. I assume that the book value accurately reflects the firm's net assets, without distortion by extreme accounting choices, and that the market value prior to the strategic alternatives disclosure accurately values the firm as a going

concern under the current management, rather than the value with a change in control. Financial statement-based measures of performance include the change in quarterly earnings from the same quarter in the prior year ($\Delta EARN$), quarterly sales (*REV*), cash and accrual components of operating earnings (*CFO* and *ACC*), and cash flows from investing activities (*CFI*). *CFO* and *CFI* sum to free cash flow; Jensen's (1986) theory of the agency cost of free cash flow posits that managers will waste the firm's free cash flow in perquisites and negative NPV projects rather than return it to shareholders. Accordingly, these firms have low performance, low valuations, and are token takeover targets.

Annual employee growth (*EMPGR*) is another measure of operating performance. Employee growth is closely related to business operations and the health of a company, yet it does not rely on financial statement numbers or stock prices like the other performance measures. Furthermore, it reflects management's reaction to past events (i.e., changes in product demand) and assessment for the future (i.e., allowing for production increases or curtailments).

4.2 Antecedents: market, managers, and ownership variables

Fundamentals alone are unlikely to influence which firms seek strategic alternatives and which of those firms receive bids. The next set of variables encompasses the firm's market (risk, returns, and intermediaries), management, and ownership structure. Market beta (*BETA*) is calculated from the standard monthly return series using the Capital Asset Pricing Model. Prior 12-month returns (*RET*, market-demeaned) capture the market's evaluation of the firm's current and expected future profitability.

Analysts are a key market intermediary, and their forecasts of EPS growth (*EPSFORECAST*) and the number of analysts following the firm (*NUMANALYSTS*) are important variables that characterize the firm's future performance and visibility with respect to market intermediaries.

Managers' forecast error (*MANAGERFE*) proxies for the managerial ability of top executives. The signed forecast error measures their optimism or overconfidence about the performance of the company. The absolute forecast error (|*MANAGERFE*|) more directly relates to the manager's precision. Firms seeking strategic alternatives may have a low ability or overconfident managers, who led the firm

to where it now needs to seek strategic alternatives. Although financial leverage (*LEV*) is mainly interpreted as a measure of financial constraint and to describe capital structure, it may also be a proxy for managerial entrenchment, since entrenched managers increase leverage beyond the optimal point to inflate the voting power of their equity stakes (Harris and Raviv, 1988).[8]

The firm's ownership structure, comprised of institutional investors, activists, and insiders, may influence its strategic decision-making. Under classical governance theory (Edmans, 2014), external ownership monitors managers and directors so that they pursue shareholder objectives, like seeking strategic alternatives and pushing the firm to actually get acquired. Institutional investors controlling a large block of votes and activist hedge funds have been regarded as a monitoring mechanism due to the pressure they exert over management (e.g., Holmstrom and Kaplan, 2001; Edmans, 2014), but there is mixed empirical evidence whether they play an effective role in improving firm performance (Holderness, 2003). In the M&A setting, Holmstrom and Kaplan report that institutional investors were often the key sellers of larger blocks of shares in takeovers, giving them the ability to facilitate their preferred transaction. Shleifer and Vishny (1986) argue that takeovers are more likely to occur as shareholder control increases, and Cremers, Nair, and John (2009) and Ali, Kravet, and Li (2016) find a positive association between blockholders and takeover likelihood. The two measures of external ownership I use are *BLOCKHOLDERS* and *ACTIVIST*, which are the percentage of shares outstanding owned by institutional blockholders and activists, respectively. Even though activists are subset of institutional investors, I measure activist holdings separately because Brav, et al. (2008) find that activists are involved in turnaround situations.

According to Jensen and Meckling (1976), increased managerial ownership aligns the managers' interests with that of shareholders, to maximizing firm value and not squander wealth. Wong and O'Sullivan (2001) suggest that incumbent managers' ownership in the firm may influence their

[8] In contrast, Berger, Ofek, and Yermack (1997) find that leverage and managerial entrenchment are inversely related.

preference for a takeover when personal financial gains from a change in control outweigh the possible losses, especially job loss. Other corporate executives and directors may also align their business decisions with shareholders' interests as insider ownership increases. Since the board officially approves the decision to seek strategic alternatives, and managers, directors, and partners are all involved in the M&A sale process, a broader definition of insiders is appropriate. I measure *INSIDER* as the percentage of shares outstanding owned by the CEO, CFO, Chairman, Vice Chairman, directors, and partners.[9]

4.3 Characterizing firms that seek strategic alternatives while controlling for industries and years

To address the first research question, I compare the values of each attribute of the strategic alternatives firms with their peer firms from the same industry-years. It is important to differentiate between industry-wide and firm-specific characteristics that motivate a target firm to sell itself, because boards respond to industry consolidation trends and firm-specific problems. When deciding to sell the company, the board of directors and managers look at the other firms in the same industry to evaluate the performance of the company and may seek strategic alternatives when the firm underperforms its industry. On the other hand, when the whole industry is performing poorly, the company may be less inclined to undertake a strategic review of alternatives if it is not underperforming its industry peers. Because the contribution of this paper is to identify the firm-specific antecedents, the research design must control for industry and year fixed effects, to absorb broad market developments that influence a firm's decision to seek strategic alternatives and a firm's probability of receiving a bid.

The research design to answer the first research question controls for industry-varying and time-varying capital market developments (e.g. merger waves) by including a proxy for the demand for industry consolidation (*DEMAND*), or by insuring that the makeup of different industries and years are not driving the observed differences between the strategic alternatives group and peer group. Peer observations (*SA_DISC*=0 and *SA_LEAK*=0) are taken from the same FF 48 industry-years as the

[9] Role codes in the Thomson Reuters Insiders data are: CEO, CFO, CB, D, P, DO, H, OD, and VC.

SA_DISC=1 and *SA_LEAK*=1 observations, respectively. Then, each peer observation is assigned a weight, $0 \leq w_i \leq 1$, so that the proportions of FF 12 industries and years in the comparison peer group are the same as in the respective *SA* group (Hainmueller, 2012; Hainmueller and Xu, 2013).[10,11] Including fixed effects and using a comparison peer group comprised of the same industries and years essentially differences out potential correlated omitted variables that are fixed for industries and years (e.g., stock market driven acquisitions and market conditions that lead to demand for consolidation).

Figure 1 shows the distributions of industries and years. Panel A shows the similar distributions of the industries of the *SA*=1 strategic alternatives group and *SA*=0 peer group after weighting. Panel B shows the similar distributions of calendar years of the *SA*=1 group and *SA*=0 peer group after weighting. Similar figures for *SA_DISC* and *SA_LEAK* are omitted for the sake of brevity. The same industry and year distributions in the case and control groups should mitigate confounding effects of M&A merger waves and other industry- and time-varying market conditions (Andrade, Mitchell, and Stafford, 2001).

In the univariate analyses to address the first research question, mean values of aforementioned firm determinants are compared using *t*-tests: between the *SA_DISC*=1 observations and their *SA_DISC*=0 peers; and between the *SA_LEAK*=1 observations and their *SA_LEAK*=0 peers.

Following the prior literature on predicting takeover targets, my first probit regression estimates the probability of an event indicator variable as a function of the firm's antecedent characteristics.

$$SA\_DISC_{i,t} \text{ or } SA\_LEAK_{i,t} = \beta_0 + \sum_{k=1}^{8} \beta_k fundamentals_{i,t} + \sum_{k=9}^{10} \beta_k market_{i,y} + \beta_{11} ownership_{i,m} + \varepsilon_{i,t}$$

SA_DISC or *SA_LEAK* is modeled using the antecedent firm determinants described in sections 4.1 and 4.2. All determinants examined in the univariate analyses are included for multivariate analyses with

[10] This method of assigning weights to achieve balance on industry and year composition between two groups is an application of entropy balancing.

[11] I use the Fama-French 48 industry classification and years to select the peer firms. While I would ideally use FF 48 industry and year for fixed effects and entropy balancing as well, my finite sample of 1,006 (SA_DISC), 151 (SA_LEAK), and 1,137 (SA) leads me to use FF 12 industry and year for fixed effects and entropy balancing.

several exceptions. Due to collinearity with other determinants, ln(*ASSETS*) and *CASH* are excluded. Due to not being statistically significant in univariate analyses, *CFI* and *EMPGR* are excluded. Due to the limited number of non-missing values, *EPSFORECAST*, *MANAGERFE, PARACHUTE*, *ACTIVIST,* and *INSIDER* are excluded. In one specification, a proxy for demand for M&A targets is included (*DEMAND*), to control for the possibility that managers anticipate industry consolidations which affects their decision to seek strategic alternatives.

4.5 Characterizing firms that receive bids

The second research question starts with the sample of 1,137 observations that are seeking strategic alternatives (*SA*=1) and investigates what attributes characterize the firms that receive bids. Table 1 shows that 44 percent of the self-selected firms receive bids within one year, and 51 percent within 2 years. While it is straightforward to assume that M&A offers received within one year after the announcement or media leak date are the result of the same strategic alternatives initiative, it is relatively less straightforward to attribute the receipt of offers in future years to the same strategic alternatives initiative. Firm characteristics measured at the time of the announcement or leak also become stale information with time. Therefore, I focus on bids received within one year. The univariate analysis uses *t*-tests to compare firm attributes of observations that subsequently receive bids (*BID1YR*=1) versus those that do not (*BID1YR* =0).

In the second probit regression, the probability of receiving a bid (*BID1YR*) is modeled using antecedent firm determinants with the same aforementioned excluded variables.

$$BID1YR_{i,t} = \beta_0 + \sum_{k=1}^{8} \beta_k fundamentals_{i,t} + \sum_{k=9}^{10} \beta_k market_{i,y} + \beta_{11} ownership_{i,m} + \varepsilon_{i,t}$$

In one specification, a proxy for all other omitted traits that might affect firm value and future outcomes is included as the control variable *3DAYRET*. The three-day return is measured around the announcement or media leak date and captures any omitted or unobservable factors, because the market assesses the likelihood of a takeover and the expected target valuation premium in the announcement reaction.

5. Results

5.1 Determinants of firms seeking strategic alternatives (Research question 1)

The starting point of these findings is to acknowledge the heterogeneity in firm attributes and that this study characterizes the typical attributes of the typical firm that is seeking strategic alternatives. Table 2's univariate analyses reveal how firms seeking strategic alternatives differ from their peer firms, one variable at a time. Firm attributes likely also drive the method of disclosure, and the number of voluntary disclosures of strategic alternatives dominate medial leaks in the overall SA sample; thus, separate analyses are carried out for *SA_DISC* and *SA_LEAK*, and only the common determinants of *SA_DISC* and *SA_LEAK* are interpreted as the determinants of seeking strategic alternatives.

I first discuss the results that are unique to *SA_DISC* or *SA_LEAK*, which provide evidence about why firm news is disseminated through certain information channels. In Panel A, firms voluntarily disclosing strategic alternatives (*SA_DISC*=1) are smaller firms. They have higher *BTM*, reflecting lower opportunities. They are underperforming firms with lower Δ*EARN*, *CFO*, and *ACC*. They have higher *CFI*, which is consistent with lower *ACC* when firms invest less in net operating assets. They have lower analyst following, which is consistent with the use of voluntary disclosure to close the information asymmetry gap when other channels like information intermediaries are lacking. Insider ownership is also lower, suggesting weaker contracting with managers and directors. This supports the story that the lack of aligned incentives led these firms to their current unhealthy state, so now they need to seek strategic alternatives. They choose to disclose the news in order to transmit the information in an otherwise poor information environment. In this univariate analysis, they do not differ from their peers in terms of CAPM beta and activist ownership.

In Panel B, firms that experienced media leaks of strategic alternatives have higher *CFO* and greater analyst following than their peers, which suggests that firms with greater visibility in the analyst community are more likely to have their news leaked. They have lower activist ownership than their

peers (weakly significant). They do not differ from their peer firms with respect to Δ*EARN*, *CFO*, and *ACC*.

Taken together, the univariate evidence in Table 2 common to *SA_DISC* and *SA_LEAK* shows that firms seeking strategic alternatives have higher leverage, greater illiquidity (lower *CASH* and higher *INTAN*), and lower *REV*, which is consistent with financial and core operational problems. Their prior 12-month returns are more negative and analyst EPS growth forecasts are lower, suggesting that the market's, including analysts', assessment of the firm's future is dire. However, they have more golden parachute provisions and higher blockholder ownership, which suggests that displacing manager's job loss disutility and providing more monitoring pressure may play a role in pushing managers to seek strategic alternatives to maximize shareholder value. Despite the robust literature on the role of activists and managerial ownership on reducing agency costs, I cannot conclude that activist ownership or that insider ownership distinguishes firms that seek strategic alternatives, since statistically significant differences are not found for neither *SA_DISC* nor *SA_LEAK*.

The univariate tests of differences in means do not control for other confounding sources of heterogeneity; for example, many of the firm characteristics are related to firm size. Therefore, multivariate evidence is provided by the probit regressions. Probit regressions utilize only the well-populated variables to preserve sample size. Variables that may pose multicollinearity problems with other variables are excluded: *ASSETS* and *CASH*, as seen in the correlation matrix (Table 3).

Table 4 Panel A presents the results of modeling the probability of disclosing strategic alternatives (*SA_DISC*). Column 1 presents the results of estimation while controlling for demand for M&A targets in industries experiencing consolidation; column 2 presents the marginal effects; column 3 presents the results of estimation with fixed effects; and column 4 presents the marginal effects. Panel B presents the results for modeling media leaks of strategic alternatives (*SA_LEAK*). Results are generally consistent with the univariate analyses. First, I highlight the differences between the probit *SA_DISC* and *SA_LEAK* results; then, I highlight their common determinants. Firms that voluntarily

disclose strategic alternatives are smaller, have lower growth prospects (higher *BTM*), and weakly lower market beta. The McFadden pseudo R^2 of the *SA_DISC* model is 7.7% without fixed effects or 8.4% with fixed effects. The untabulated likelihood ratio (LR) Chi-square test statistic, which tests that all the parameters in the model are simultaneously equal to zero, is 365.3 or 544.7, for the specification with or without fixed effects. To compare, Powell's (1997, Table 3) main probit model has a McFadden pseudo R^2 of 1.49% without fixed effects, and Palepu (1986, Table 3) reports likelihood ratio (LR) Chi-squared test statistics between 47.78 and 72.32.

In contrast, in Panel B, firms with media leaks of strategic alternatives are larger, have weakly higher intangibles, but are not distinguished from peers by their *BTM* nor market beta. The McFadden pseudo R^2 of the *SA_LEAK* model is 11.6% without fixed effects and 13.4% with fixed effects. Consistent with the interpretation of the univariate analyses partitioning on *SA_DISC* and *SA_LEAK*, these probit results reveal the roles of voluntary disclosure and media leaks serving different types of firms.

What both groups of firms seeking strategic alternatives have in common are higher leverage, lower changes in earnings and revenues, lower prior stock returns, and higher blockholder ownership. The common determinants of seeking strategic alternatives provide evidence that a general motive for selling firms is to resolve their financial problems, consistent with the target bankruptcy avoidance hypothesis of Pastena and Ruland (1986) and Amit, Livnat, and Zarowin (1989). The debt overhang problem, while it may reduce agency costs, is nonetheless a threat to the firm's stand-alone vitality, so greater leverage is a contributing factor. This financial problem appears to be compounded by the fact that these firms do not have promising core operations, measured by changes in earnings and revenues, for an operational turnaround as a stand-alone company and thus leads these firms to seek a strategic solution. Their negative prior stock returns also reflect this negative sentiment. The presence of golden parachutes and blockholders appear to be effective corporate governance mechanisms in getting these firms to take action by reviewing strategic alternatives. By volitionally taking the first step of the M&A

sale process, these firms are exhibiting self-discipline when faced with financial and performance issues in the presence of good corporate governance qualities. In contrast to the disciplining theory of mergers (Morck, Shleifer, and Vishny, 1988), a novel interpretation of this evidence suggests that poorly performing firms do not need an acquirer to be disciplined; rather, they appear to discipline themselves by seeking strategic alternatives.

5.2 Determinants of receiving a bid (Research question 2)

In this subsection, results uncover what firm characteristics are associated with a higher probability of receiving bids. The subsequent tests start with the 1,137 observations that seek strategic alternatives (*SA*=1), and identify the distinguishing attributes between those that receive bids (*BID1YR*=1) versus those that do not (*BID1YR*=0).

Table 5 presents univariate *t*-tests, partitioning on *BID1YR*. Firms receiving bids have higher market capitalizations, greater growth prospects (lower *BTM*), and less cash. Although they have less cash, this potential need for cash provides an opportunity for a buyer to step in and provide capital resources to a target firm that otherwise has promising operations and investments in place. They have stronger operating performance, exhibited by $\Delta EARN$, *REV*, *CFO*, and *ACC*. The core operations of actual target firms are better, and they have higher investments in operating assets. Firms that are viewed favorably by the stock market are more likely to be actual targets: they have less market risk and better prior stock price returns. Finally, actual targets have greater blockholder ownership than non-targets.

When controlling for multiple firm antecedents, Table 6 presents findings that are generally consistent with the univariate findings. Firms with better growth opportunities, changes in earnings (weak significance), and cash flows from operations have a greater probability of receiving a bid. Market beta is decreasing and blockholder ownership is increasing in the probability of receiving a bid. Within the full set of specified firm attributes, market capitalization, revenues, and prior stock returns appear to not have a significant effect on the selection of bid recipients. The McFadden pseudo R^2 of this model

is 7.3%, or 7.9% when additionally controlling for the three-day announcement or media leak return (*3DAYRET*).

The announcement return at the time of the disclosure or media leak (*3DAYRET*) provides an opportunity to control for "unobservable" characteristics that the market observes. The market reaction prices in the estimated gains from a takeover, more specifically, the likelihood of a takeover and the premium to stockholders. When *3DAYRET* is included in the model, it is statistically significant as expected; the positive and significant coefficient on *3DAYRET* shows that the market partially prices the likelihood of receiving a bid in the future at the time of the disclosure or media leak. Yet, the coefficient estimates on the previously-specified firm attributes are generally unchanged, except *ΔEARN* is no longer statistically significant. The pseudo R^2 increases modestly to 7.9%. The modest changes provide confidence that there is no serious correlated omitted variable problem.

5.3 Two processes within one broadly-defined target selection process

The self-selection to seek strategic alternatives and the selection of target firms to receive bids appear to be two distinct selection processes that prior papers have entangled. For the most part, the determinants of the two processes are distinctly different. While firms seeking strategic alternatives are relatively unhealthy firms, those that receive bids are relatively healthier and appear more promising.

The only two firm attributes that explain both the probability of seeking strategic alternatives and the probability of receiving bids appear to be less cash (univariate evidence only) and greater blockholder ownership (univariate and multivariate evidence). Cash is excluded from the probit analyses due to strong correlations with other regression covariates. Nonetheless, the univariate evidence is consistent with desperate firms with less cash needing to seek a strategic out, and also presenting an opportunity for bidders to provide needed cash resources to an otherwise promising target. Blockholder presence is not only increasing the probability of seeking strategic alternatives, but is also higher in firms that subsequently receive a bid. One interpretation of the results is that blockholders monitor and provide pressure to managers and directors at the onset of the preliminary sale process, to start evaluating

strategic alternatives, and further along the sale process. Managers and directors may be pressured by large institutional investors to schedule and pursue management meetings with potential bidders until one or more offers are received. These findings are consistent with institutional shareholders advocating for maximizing shareholder wealth via strategic alternatives and also seeking to ensure that a bid is received.

To provide evidence that the takeaways from my study could not be inferred from modeling takeover targets that receive a bid in one step, a probit equation models *BID1YR* on firm covariates in Table 7. This test also provides confidence that the results in previous tables are not due to this paper using different industries and years in my sample, but from using firms seeking strategic alternatives, which is conceptually different from firms that receive bids and whose takeovers are complete. Like my previous probit tests, I include fixed effects to difference out potential correlated omitted variables that are fixed for industries and years (e.g., market conditions and demand for consolidation). This analysis is subject to the named concerns of prior literature, yet the purpose of it is to show that using a sample of strategic alternatives to model two selection processes provides different empirical insights than using a sample of ex-post targets to model one selection process; the new insights are not due to using a different sample period or variations of variable calculations compared to prior papers. Column 1 shows that target firms compared to non-targets in the same industry-years have are more undervalued (greater *BTM*), have greater financial constraints (higher *LEV*), do not have statistically different cash flow performance (*CFO*) and market risk (*BETA*). As in prior literature, the evidence is not conclusive about the role of profitability or performance; the coefficient on the accrual component of earnings (*ACC*) is negative while the coefficient on earnings growth ($\Delta EARN$) is positive.

The takeaways gained from separately modeling the two processes suggest that we observe desperate target firms receiving merger bids *not* because bidders prefer to acquire firms with lower growth prospects and higher leverage, but because firms with lower growth prospects and higher leverage are more likely to seek strategic alternatives! Making inferences solely from Table 7 would

cause one to conclude that cash flow performance and market risk are not important explanatory variables, whereas the cleaner research design in Tables 5 and 6 suggest that bidders appear to prefer firms with greater cash flows and lower market risk based on Table 6. Finally, target firms have significantly greater external institutional ownership (*BLOCKHOLDER*) than non-targets, and this is likely because institutional ownership is an important determinant for the target firm at *both* stages: when it's seeking strategic alternatives and when it receives a bid. While I cannot statistically compare pseudo R^2s across tables using different samples, it is nonetheless interesting to note that the pseudo R^2 of the one-step model in Table 7 (2.2%) is much smaller than the pseudo R^2s from modeling the two processes separately in Tables 4 and 6 (range 7.7-13.4% and 7.3-7.9%, respectively).

5.4 Robustness check using a modified peer comparison sample

A limitation of my sample construction is that I can only identify a finite number of firms that are seeking strategic alternatives, whereas ideally, I would be able to identify all of them. Some firms that seek strategic alternatives but whose reviews are not publicly observable will be miscategorized into the respective peer comparison group (*SA_DISC*=0 and/or *SA_LEAK*=0). While having undercover *SA* firms in the comparison group is likely to lessen any differences between the observed *SA* group and comparison group and hence, understate my results, nonetheless, I conduct an alternate estimate of differences in firm attributes using the modified comparison samples. I remove all targets of friendly bids from the peer group, because presumably these firms could have been seeking strategic alternatives without being publicly observed. Then, I repeat the analysis in Table 2 using this modified peer group (untabulated), and results are consistent. Minute changes include the difference in *INTAN* between voluntary disclosers (*SA_DISC*=1) and their modified peer group, which becomes more significant (*p*-value=0.049). The difference in *REV* between medial leaked companies (*SA_LEAK*=1) and their modified peer group becomes less significant (p-value=0.111); and the difference in *ACTIVIST* becomes more significant (*p*-value=0.047).

6. Conclusion

The strategic alternatives sample provides a different perspective from which to analyze prospective targets' motives for engaging in M&A. Analyzing firms that seek strategic alternatives tells us something new about potential target firms, including those that do not become actual targets, by receiving a bid. In contrast to prior studies that describe the characteristics of targets that receive a bid (e.g., Hasbrouck, 1985) or of targets of completed deals (e.g., Palepu, 1986; Morck, Schliefer, and Vishny, 1988, 1989), this study identifies the attributes of firms that announce that they are seeking to be acquired, regardless of whether a bid is received. Then, from the sample of firms seeking strategic alternatives, this study identifies the distinguishing attributes of firms that do receive bids.

A limitation of the *ex-post* target samples used by prior studies is that they are unlikely to solely reflect target motives for M&A because they also reflect bidders' selections of targets. Studying targets of completed deals introduces a sample bias from comingling the selection of targets (both self-selection and by buyers) with the selection by regulators and shareholders (for shareholder approval). In contrast, the observed choice to undergo a review of strategic alternatives reflects the pure volition of the selling firm, in the absence of any acquirer's motive. The first main contribution of this study is exploiting the unique sample of firms seeking strategic alternatives to uncover the antecedent attributes of the typical firm that wants to be sold, including those that fail to receive a bid.

The second main contribution is to model the broadly-defined "target selection" process as two distinct selection processes, following two research questions. The first research question is why certain firms seek strategic alternatives. Based on the common determinants of both disclosed and leaked strategic alternatives, the typical firm that is seeking strategic alternatives has financing and liquidity constraints (such as greater leverage and intangibles, but less cash) and lower operating performance. Yet the presence of golden parachutes and greater institutional ownership also increases the probability of seeking strategic alternatives. Taken together, firms seeking strategic alternatives appear to be firms

that face financial and liquidity problems, have bleak expectations of an operational turnaround, but have effective corporate governance in place to push the managers and directors to action.

Due to the identification of firms seeking strategic alternatives through two different sources (voluntary corporate disclosures and media leaks), differences between firms using the two information channels can be analyzed to understand the different roles of voluntary disclosure and involuntary media leaks in transmitting information. Firms that disclose their strategic reviews tend to be smaller, less visible firms that need to publicly address their poor performance with a public announcement. On the other hand, firms that have their strategic reviews leaked have higher visibility within the analyst investment community and have greater market capitalizations.

The second research question addresses why certain firms that explore strategic alternatives are successful and actually receive bids. Firms that receive bids have greater growth opportunities and past operating performance. They have less cash, but this does not appear to deter bidders, and may actually provide an investment opportunity for bidders. Lower market risk also increases the probability of a bid, suggesting that this is a desirable attribute of targets. Lastly, blockholder ownership increases the probability of receiving a bid. The influence of external blockholders at both stages of the process supports that notion that large shareholders improve the efficiency of the market for corporate control and this is one channel through which they improve firm value (Shleifer and Vishny, 1986).

Modeling both selection processes using a common set of firm attributes contributes to the literature's extant interest in the characteristics of target firms and refines our understanding of target selection. I show that the differing firm attributes that are important factors at each of the two selection processes (self-selection for strategic alternatives and selection to receive a merger bid) cannot be uncovered by modeling targets versus non-targets in one step. Moreover, the finding of a generally non-overlapping set of determinants supports the two selection processes as being distinct from one another.

References

Agrawal, A. and J.F. Jaffe. 2003. Do takeover targets underperform? Evidence from operating and stock returns. *Journal of Financial and Quantitative Analysis* 38 (4), 721-746.

Aktas, N., E. de Bodt and R. Roll. 2010. Negotiations under the threat of an auction. *Journal of Financial Economics* 98: 241-255.

Ali, A., T. Kravet, and B. Li. 2016. Accounting profitability and takeover likelihood. Working paper.

Ambrose, B.W. and W.L. Megginson. 1992. The role of asset structure, ownership structure, and takeover defenses in determining acquisition likelihood. *Journal of Finance & Quantitative Analysis* 27, 575–589.

Amit, R., J. Livnat, and P. Zarowin. 1989. A classification of mergers and acquisitions by motives: Analysis of market responses. *Contemporary Accounting Research* 6 (1), 143-158.

Andrade, G., M. Mitchell, and E. Stafford. 2001. New evidence and perspectives on mergers. *Journal of Economic Perspectives* 15 (2), 103-120.

Asquith, P. 1983. Merger bids, uncertainty, and stockholder returns. *Journal of Financial Economics* 11, 51-83.

Berger, P.G., E. Ofek, and D.L. Yermack. 1997. Managerial entrenchment and capital structure decisisons. *The Journal of Finance* 52 (4), 1411-1438.

Brav, A. W. Jiang, F. Partnoy, and R. Thomas. 2008. Hedge fund activism, corporate governance, and firm performance. *The Journal of Finance* 63 (4), 1729-1775.

Boone, A.L. and J.H. Mulherin. 2007. How are firms sold? *Journal of Finance* 62 (2), 847-875.

---------- and ----------. 2008. Do auctions induce a winner's curse? New evidence from the corporate takeover market. *Journal of Financial Economics* 89 (1), 1-19.

Cornett, M.M., B. Tanyeri, and H. Tehranian. 2011. The effect of merger anticipation on bidder and target firm announcement period returns. *Journal of Corporate Finance* 17, 595-611.

Cremers, K.J.M., V.B. Nair, and K. John. 2009. Takeovers and the cross-section of returns. *The Review of Financial Studies* 22 (4), 1409-1445.

Edmans, A. 2014. Blockholders and corporate governance. *Annual Review of Financial Economics* 6, 23-50.

Fidrmuc, J.P. and C. Xia. 2017. M&A deal initiation and managerial motivation. *Journal of Corporate Finance* 46, in press.

Hainmueller, J. 2012. Entropy balancing for causal effects: A multivariate reweighting method to produce balanced samples in observational studies. *Political Analysis* 20 (1), 25–46.

Hainmueller, J. and Y. Xu. 2013. Ebalance: A Stata package for entropy balancing. *Journal of Statistical Software* 54 (7).

Harris, M. and A. Raviv A. 1988. Corporate control contests and capital structure. *Journal of Financial Economics* 20, 55-86.

Hasbrouck, J. 1985. The characteristics of takeover targets q and other measures. *Journal of Banking and Finance* 9, 351-362.

Healy, P.M., A.P. Hutton, and K.G. Palepu. 1999. Stock performance and intermediation changes surrounding sustained increases in disclosure. *Contemporary Accounting Research* 16 (3), 485-520.

Holmstrom, B. and S.N. Kaplan. 2001. Corporate governance and merger activity in the United States: Making sense of the 1980s and 1990s. *Journal of Economic Perspectives* 15 (2), 121-144.

Jensen, M.C. 1986. Agency costs of free cash flow, corporate finance, and takeovers. *The American Economic Review Proceedings* 76 (2), 323-329.

Jensen, M.C. and W.H. Meckling. 1976. Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of Financial Economics* 3, 305-360.

Malmendier, U., M.M. Opp, and F. Saidi. 2016. Target revaluation after failed takeover attempts: Cash versus stock. *Journal of Financial Economics* 119 (1), 92-106.

Marquardt, C. and E. Zur. 2015. The role of accounting quality in the M&A market. *Management Science* 61 (3), 604-623.

Morck, R., A. Shleifer, and R.W. Vishny. 1988. Characteristics of hostile and friendly takeovers. In Auerbach, A.J., ed. *Corporate Takeovers: Causes and Consequences*. Chicago: University of Chicago Press.

Morck, R., A. Shleifer, and R.W. Vishny. 1989. Alternative mechanisms for corporate control. *The American Economic Review* 79 (4), 842-852.

Palepu, K. 1986. Predicting takeover targets: A methodological and empirical analysis. *Journal of Accounting and Economics* 8, 3-35.

Pastena, V. and W. Ruland. 1986. The merger/bankruptcy alternative. *The Accounting Review* 61 (2), 288-301.

Powell, R.G. 1997. Modelling takeover likelihood. *Journal of Business Finance & Accounting* 24 (7-8), 1009-1030.

Ravenscraft, D.J. and F.M. Scherer. 1987. *Mergers, Sell-offs and Economic Efficiency*. Washington, DC: The Brookings Institution.

Rhodes-Kropf, M. and D.T. Robinson. 2008. The market for mergers and the boundaries of the firm. *The Journal of Finance* 63 (3), 1169-1211.

Shleifer, A. and R.W. Vishny. 1986. Large shareholders and corporate control. *Journal of Political Economy* 94 (3), 461-488.

---------- and ----------. 1988. Value-maximization and the acquisition process. *Journal of Economic Perspectives* 2, 7-20.

Wong, P. and N. O'Sullivan. 2001. The determinants and consequences of abandoned takeovers. *Journal of Economic Surveys* 15 (2), 145-186.

Zha, J. 2016. Voluntary disclosure of strategic alternatives: A cost-benefit analysis. Doctoral dissertation, University of California, Berkeley.

Zha Giedt, J. 2017. Economic consequences of announcing strategic alternatives. Working paper.

APPENDIX 1 (continued on the next page)

Examples of Firms Seeking Strategic Alternatives

Panel A: Angie's List, Inc.'s media leak

A Report Says Angie's List Might Sell Itself And Now Its Stock Is Surging

BUSINESS INSIDER

By Myles Udland

October 1, 2014

Shares of Angie's List were up as much as 22% in pre-market trade on Wednesday after a report by The Financial Times' Ed Hammond said the company has hired bankers to, "help it explore strategic options, including a possible sale of the business."

Angie's List in an online review service, sort of like Yelp, but requires members to register and pay a yearly fee for the service.

Earlier this week, Angie's List announced a new $85 million credit agreement with TCW Asset Management.

Year-to-date, shares of Angie's List, which has been the subject of negative commentary from short-selling blogs like Citron Research in the past, are down 57% excluding Wednesday's pre-market rally.

Over the last year, the stock has fallen more than 70%.

APPENDIX 1 (continued)

Panel B: Conn’s, Inc.’s corporate disclosure

Conn’s Exploring Strategic Alternatives

BUSINESS WIRE

October 6, 2014

Conn's, Inc. (NASDAQ:CONN), today announced that its Board of Directors authorized management to explore a full range of strategic alternatives for the Company to enhance value for stockholders, including, but not limited to, a sale of the Company, separating its retail and credit businesses or slowing store openings and returning capital to investors. The Company has engaged BofA Merrill Lynch as financial advisor and Vinson & Elkins LLP as legal counsel to assist in the process.

"Our strategic initiatives remain on track with new store openings and the penetration of new geographic markets, and we remain committed to our current strategic plan," stated Theodore M. Wright, Conn's chairman and chief executive officer. "We are extremely proud of what our Conn's team has accomplished. While we remain confident in the Company's future prospects and have ample capital and liquidity to execute our business plan, we have decided to conduct a strategic review and explore options to accelerate the realization of value for our stockholders," said Mr. Wright.

Mr. Wright further noted, "We remain fully committed to continuing to meet the needs of our customers, attracting and retaining world-class talent, driving sales and operating margins, executing our store opening plans and serving the interests of all of our stockholders, irrespective of the outcome of this process."

APPENDIX 2 (continued on the next page)

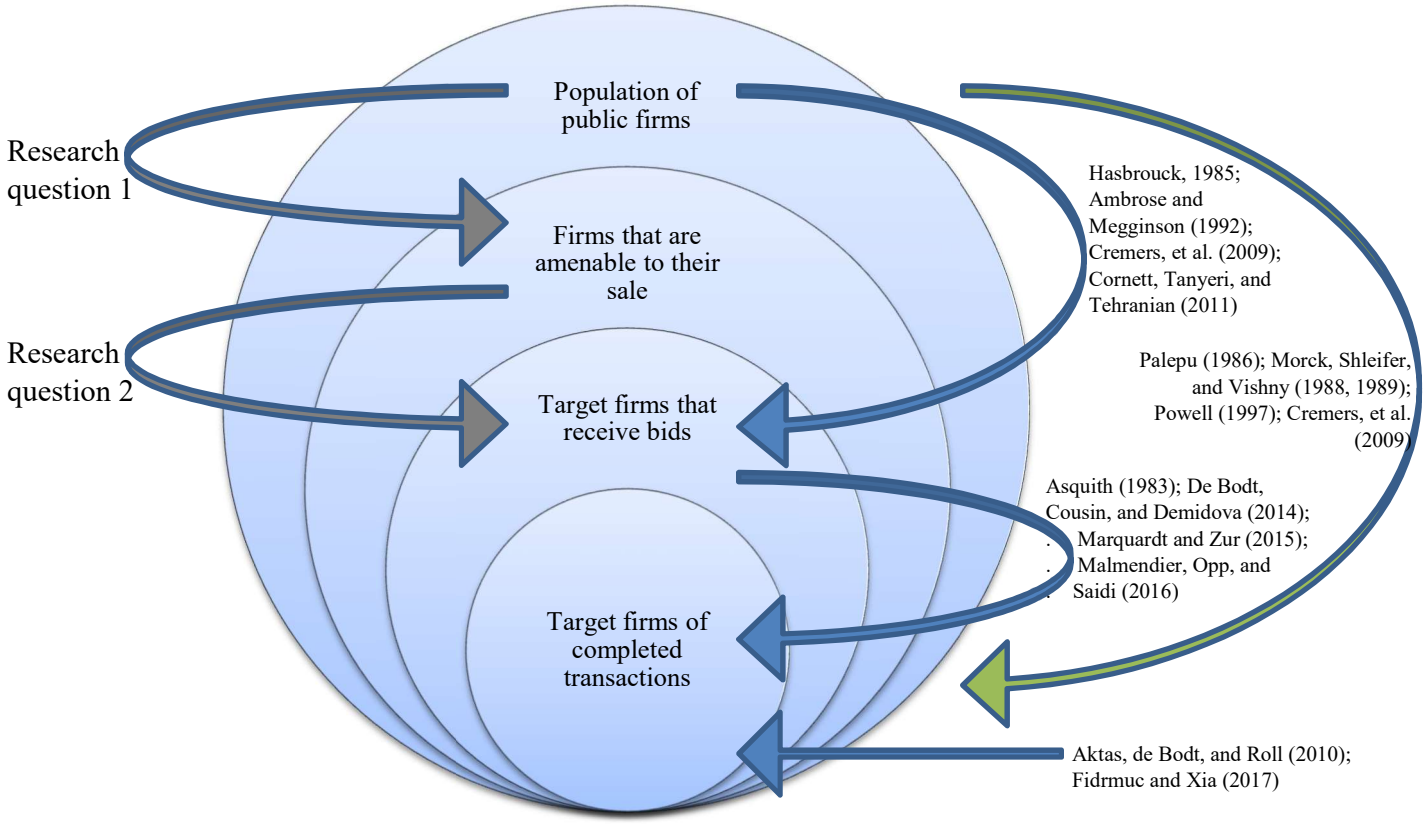
Variable Definitions

Strategic alternatives indicator variables	
$SA_{i,t}$	=1 if firm *i* is seeking strategic alternatives in year *t*, identified by its corporate disclosure or a media leak, and =0 for its peer firms in the same FF 48 industry-year. A firm with both leaked and disclosed strategic alternatives is only counted once.
$SA\_LEAK_{i,t}$	=1 if firm *i* is seeking strategic alternatives in year *t*, identified by a media leak, and =0 for its peer firms in the same FF 48 industry-year.
$SA\_DISC_{i,t}$	=1 if firm *i* is seeking strategic alternatives in year *t*, identified by its corporate disclosure, and =0 for its peer firms in the same FF 48 industry-year.
Receipt of a bid indicator variable	
$BID1YR_{i,t}$	=1 if firm *i* is seeking strategic alternatives and receives a bid within one year. =0 if firm *i* is seeking strategic alternatives but does not receive a bid.
Fundamentals	
$ASSETS_{i,q}$	Total assets of firm *i* at the most recent quarter-end *q* before the corporate disclosure or media leak. Source: Compustat
$MKVAL_{i,q}$	Market value of firm *i*'s common equity at the most recent quarter-end *q*, calculated as *PRCC_F * CSHO*. Source: Compustat
$MTB_{i,q}$	Market-to-book ratio of firm *i* at the most recent quarter-end *q*, calculated as market value of common equity divided by the book value of common equity. Source: Compustat
$LEV_{i,q}$	Leverage of firm *i* at the most recent quarter-end *q*, calculated as total liabilities divided by total assets. Source: Compustat
$CASH_{i,q}$	Cash and cash equivalents of firm *i* at the most recent quarter-end *q* before the corporate disclosure or media leak, scaled by total assets. Source: Compustat
$INTAN_{i,q}$	Intangible assets of firm *i* at the most recent quarter-end *q* before the corporate disclosure or media leak, scaled by total assets. Source: Compustat
$\Delta EARN_{i,q}$	Year-over-year change in quarterly earnings, calculated as $NI_{i,q} + XINT_{i,q} - (NI_{i,q-4} + XINT_{i,q-4})$, divided by average total assets. Source: Compustat
$REV_{i,q}$	Quarterly sales revenue of firm *i* for the most recent quarter *q* before the corporate disclosure or media leak, calculated as total revenues divided by average total assets. Source: Compustat
$CFO_{i,q}$	Quarterly cash flows from operations of firm *i* for the most recent quarter *q* before the corporate disclosure or media leak, scaled by average total assets. Source: Compustat
$CFI_{i,q}$	Quarterly cash flows from investing activities of firm *i* for the most recent quarter *q*, calculated as *IVNCF* scaled by average total assets. Source: Compustat
$ACC_{i,q}$	Quarterly operating accruals of firm *i* for the most recent quarter *q*, calculated as $(\Delta AT - \Delta CHE) - (\Delta LT - \Delta LCT - \Delta DLT)$, divided by

	average total assets. Source: Compustat
$EMPGR_{i,y}$	Annual change in number of employees at the most recent year-end y before the corporate disclosure or media leak, calculated as ($EMP_{i,y}$ – $EMP_{i,y-1}$) / $EMP_{i,y-1}$. Source: Compustat
Market and Analyst	
$BETA_{i,y}$	CAPM beta estimated at the firm-year level using monthly observations of firm i's returns during years y-2, y-1, and y, where at least 10 observations are required for estimation: $(ret_{i,m} - r_m^f) = \alpha_{i,m} + \beta_{i,y}(r_m^{mkt} - r_m^f) + \varepsilon_{i,m}$ Source: CRSP and Ken French's website
$RET_{i,y}$	12-month market-demeaned buy-and-hold returns ending with the month prior to the corporate disclosure or media leak. 12-month buy-and-hold CRSP value-weighted returns over the same period are subtracted. Source: CRSP
$EPSFORECAST_{i,m}$	Consensus analysts' forecasted EPS growth for firm i at month m, calculated as (*consensus EPS estimate*$_{i,m}$ – *actual*$_{i,m-12}$) / *actual*$_{i,m-12}$. Source: IBES Estimates
$NUMANALYSTS_{i,m}$	Number of analysts following firm i at month m, calculated as the number of earnings forecasts used in determining the consensus estimate for fiscal year earnings. Source: IBES Estimates
Manager	
$MANAGERFE_{i,m}$	Managers' forecast error, calculated as (*manager's EPS forecast*$_{i,m}$ – *actual EPS*) / *actual EPS*. Source: IBES Guidance
$\lvert MANAGERFE_{i,m} \rvert$	Absolute value of managers' forecast error. Source: IBES Guidance
$PARACHUTE_{i,m}$	Presence of golden parachute provision. Source: Risk Metrics Governance
Ownership	
$BLOCKHOLDER_{i,m}$	Institutional blockholders' ownership as a percent of shares outstanding, by asset managers with $100+ million AUM and 5%+ ownership, for firm i at the end of the most recent month m before the corporate disclosure or media leak. Source: Thomson Reuters Institutional Holdings
$ACTIVIST_{i,m}$	Activists' ownership as a percent of shares outstanding, from 13-D filings for firm i at the end of the most recent month m before the corporate disclosure or media leak. Source: Audit Analytics
$INSIDER_{i,m}$	Insiders' shares held in firm i at the end of month m, as a percent of shares outstanding. Insiders are the CEO; Chairman of the Board; Director; CFO; General Counsel; Partner; Director and Beneficial Owner; Officer Director and Beneficial Owner; Officer and Director; and Vice Chairman. Source: Thomson Reuters Insider Filing Data
Other	
$3DAYRET_{i,t}$	The 3-day buy-and-hold return surrounding the corporate disclosure or media leak date. Source: CRSP
$DEMAND_{i,y}$	Proxy for demand for consolidation in firm i's industry and year y, calculated as the number of acquired firms in that FF48 industry-year divided by the number of firms in that FF48 industry-year. Source: CRSP delisting codes

EXHIBIT 1

Target Selection Processes

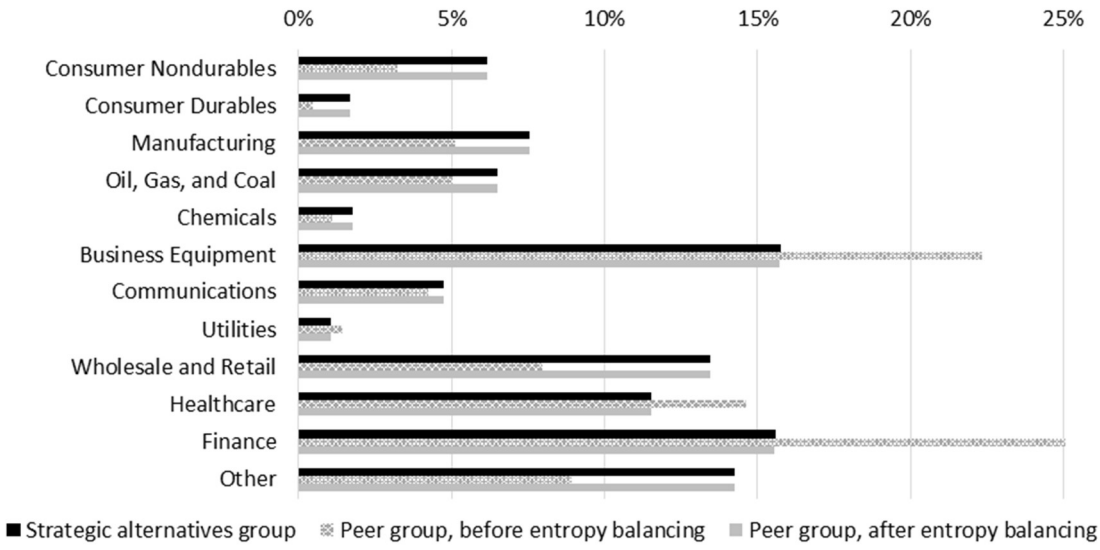


Notes: This exhibit summarizes the various samples and subsamples used by the literature to describe target selection. The arrows on the right show the comparisons that prior studies have made. The two arrows on the left show the two selection processes described in this paper. This conceptual representation of target selection would not apply to hostile takeovers, which are rare in my post-1990 sample period (Andrade, et al., 2001).

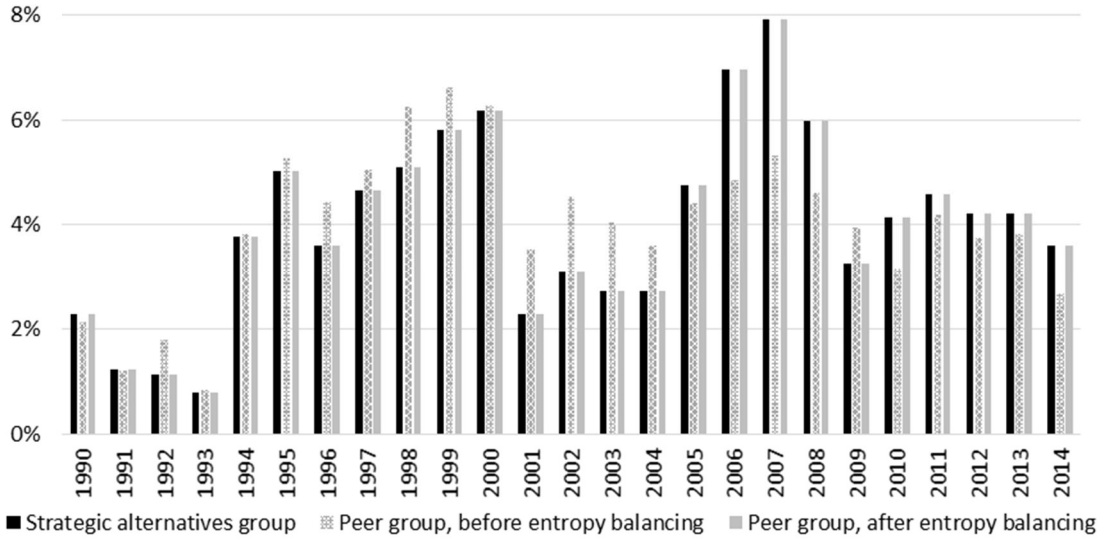
FIGURE 1

Industry and Year Distributions

Panel A: Industry distributions of firms seeking strategic alternatives and their peer firms



Panel B: Year distributions of firms seeking strategic alternatives and their peer firms

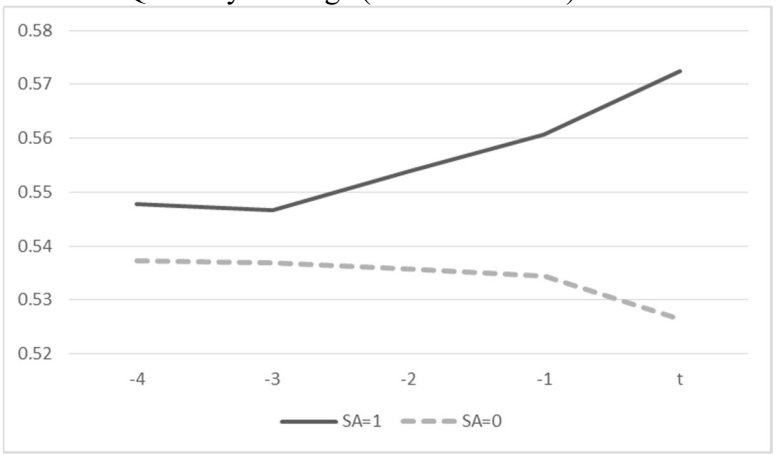


Notes: Panel A depicts the Fama-French 12 distributions of firms that seek strategic alternatives (*SA*=1) identified by corporate disclosures and media leaks (black bars), their peer firms before balancing industries and years (patterned bars), and the peer firms after balancing (grey bars). Panel B depicts the year distributions. Peer firms (*SA*=0) are selected from the same FF 48 industry years as the *SA*=1 observations. Entropy balancing assigns a weight to each peer observation so that the peer group's proportions of FF 12 industries and years are the same as those of the strategic alternatives group.

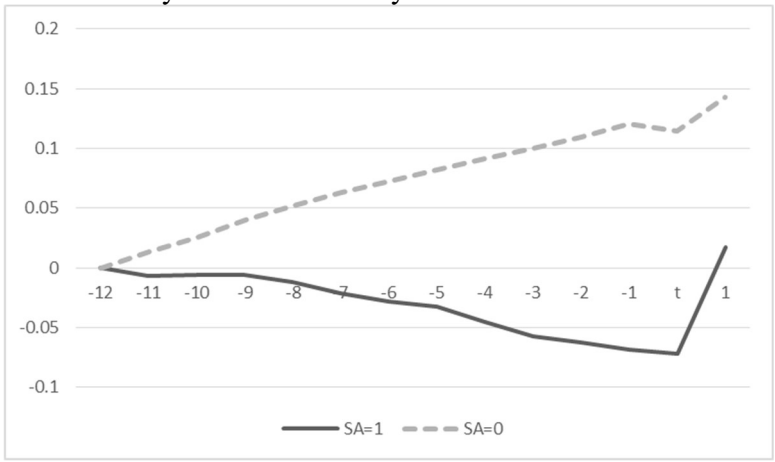
FIGURE 2

Antecedent Characteristics of Firms Seeking Strategic Alternatives vs. Their Peers

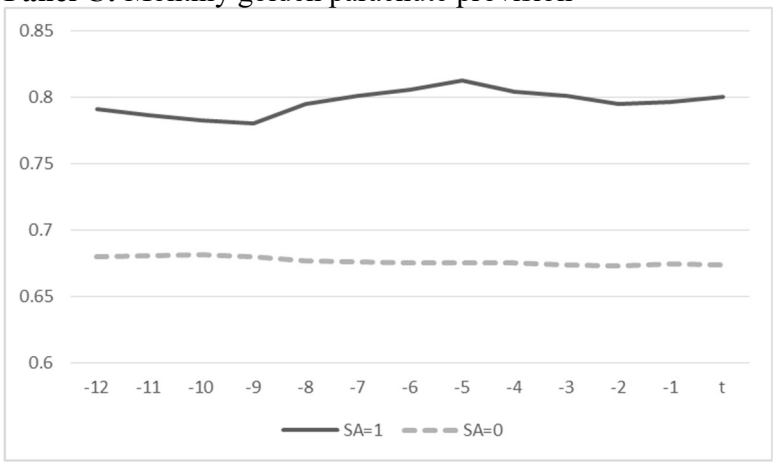
Panel A: Quarterly leverage (liabilities/assets)



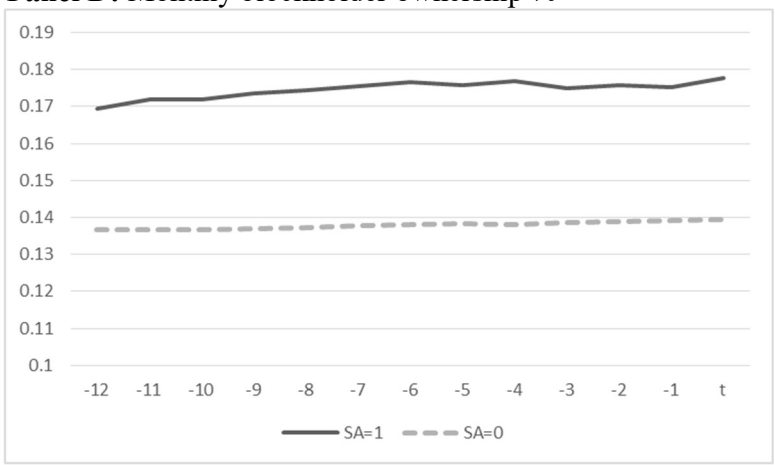
Panel B: Buy-and-hold monthly returns



Panel C: Monthly golden parachute provision



Panel D: Monthly blockholder ownership %

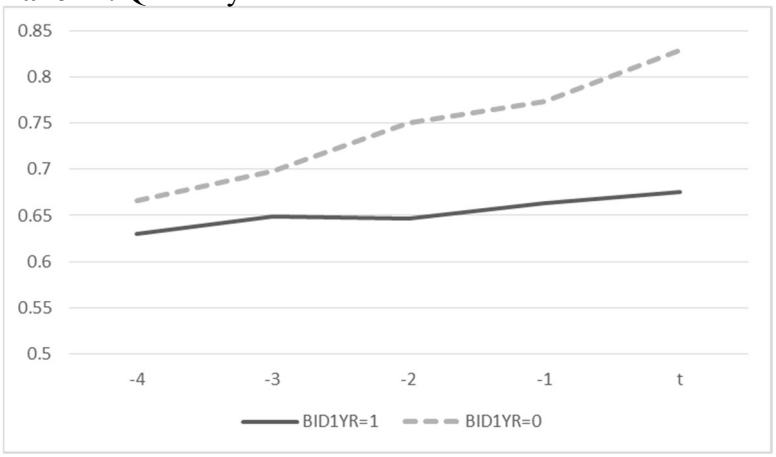


Notes: This figure presents the mean values of selected quarterly and monthly antecedent firm characteristics before the strategic alternatives event date. The solid line represents the strategic alternatives group (*SA*=1) and the dashed line represents the industry-and-year-balanced peer group (*SA*=0). *t* is the most recent quarter or month before *SA*.

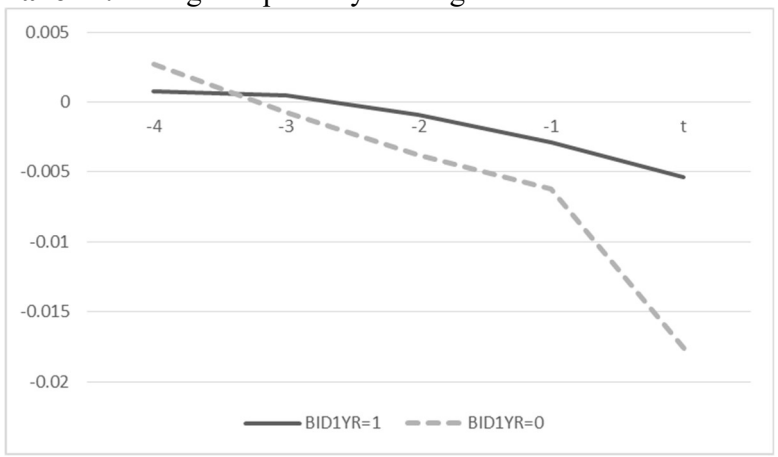
FIGURE 3

Antecedent Characteristics of Firms that Receive Bids vs. Firms that Do Not Receive Bids

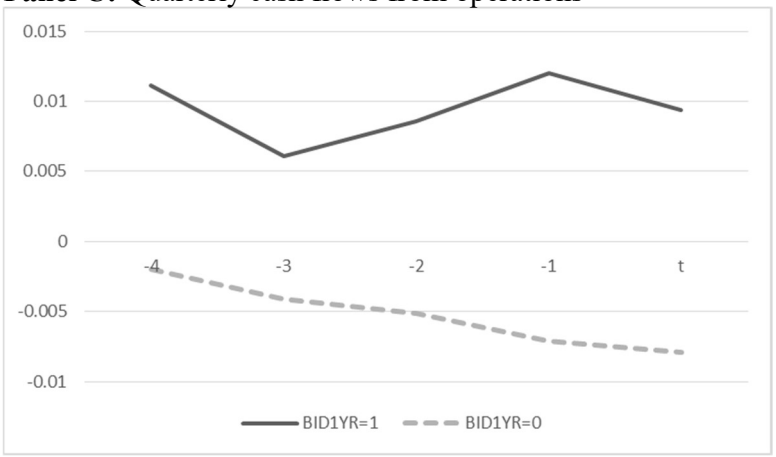
Panel A: Quarterly book-to-market



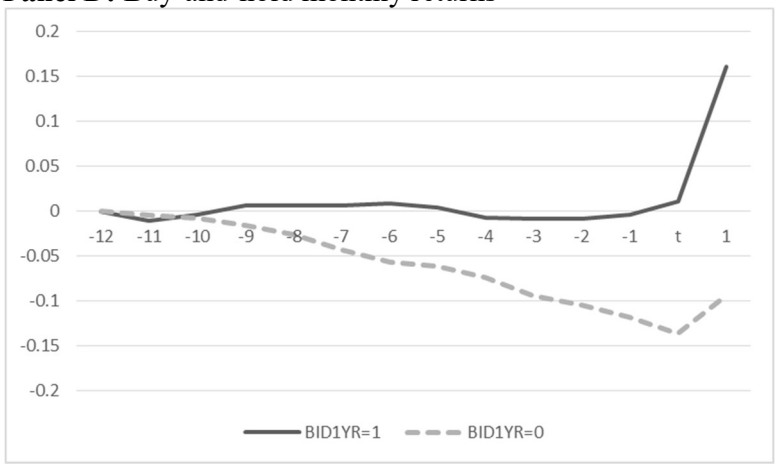
Panel B: Change in quarterly earnings



Panel C: Quarterly cash flows from operations



Panel D: Buy-and-hold monthly returns



Notes: This figure presents the mean values selected quarterly and monthly antecedent firm characteristics before the strategic alternatives event date. The solid line represents the observations in the strategic alternatives group that receive bids (*SA*=1 & *BID1YR*=1) and the dashed line represents those that do not receive bids (*SA*=1 & *BID1YR*=0). *t* is the most recent quarter or month before *SA*.

TABLE 1

Sample and Subsamples

Corporate disclosures of strategic alternatives *SA_DISC*=1	Media leaks of strategic alternatives *SA_LEAK*=1	Total observations of strategic alternatives *SA*=1
1,006	151	1,137
Observations that receive bid(s) within one year *SA_DISC*=1 & *BID1YR*=1	Observations that receive bid(s) within one year *SA_LEAK*=1 & *BID1YR*=1	Observations that receive bid(s) within one year *SA* =1 & *BID1YR*=1
435 43.2%	77 50.1%	497 43.7%
Observations that receive bid(s) within two years *SA_DISC*=1 & *BID2YR*=1	Observations that receive bid(s) within two years *SA_LEAK*=1 & *BID2YR*=1	Observations that receive bid(s) within two years *SA*=1 & *BID2YR*=1
510 50.7%	87 57.6%	581 51.1%

Notes: This table describes the sample and pertinent subsamples used in this study. Of the 1,006 corporate disclosures (*SA_DISC*=1) and 151 media leaks (*SA_LEAK*=1), 20 observations experience both and thus are only counted once for a total of 1,137 observations (*SA*=1).

TABLE 2 (continued on the next page)

Firms that Seek Strategic Alternatives vs. Their Peers

Panel A: Firms seeking strategic alternatives identified by corporate disclosures versus their industry-year peer firms

	Firms seeking strategic alternatives Corporate disclosures				Industry-year peer firms				Difference in means
	N	Mean (a)	SD	Median	N	Mean (b)	SD	Median	*P*-value (a) ≠ (b)
Fundamentals									
$ASSETS_{i,q}$	1,006	1,112	3,556	215	67,355	3,225	13,174	268	***
$MKVAL_{i,q}$	1,006	597	1,739	113	67,355	2,155	6,800	217	***
$BTM_{i,q}$	1,006	0.794	0.857	0.627	67,355	0.610	0.622	0.480	***
$LEV_{i,q}$	1,006	0.570	0.282	0.563	67,355	0.525	0.276	0.517	***
$CASH_{i,q}$	1,006	0.152	0.205	0.061	67,355	0.183	0.229	0.079	***
$INTAN_{i,q}$	1,006	0.085	0.169	0.000	67,355	0.075	0.154	0.000	*
$\Delta EARN_{i,q}$	1,006	-0.014	0.082	-0.002	67,355	0.000	0.072	0.001	***
$REV_{i,q}$	964	0.248	0.216	0.197	57,931	0.271	0.228	0.220	***
$CFO_{i,q}$	1,006	-0.003	0.073	0.007	67,355	0.006	0.066	0.011	***
$CFI_{i,q}$	1,006	-0.013	0.059	-0.008	67,355	-0.023	0.067	-0.011	***
$ACC_{i,q}$	1,006	-0.008	0.105	-0.000	67,355	0.012	0.098	0.007	***
$EMPGR_{i,y}$	950	0.084	0.470	0.000	59,037	0.136	0.451	0.041	***
Market									
$BETA_{i,y}$	1,006	1.123	1.000	0.993	67,355	1.167	1.030	1.035	.
$RET_{i,y}$	1,006	-0.213	0.529	-0.283	67,355	-0.006	0.612	-0.083	***
$EPSFORECAST_{i,m}$	581	0.238	1.607	0.091	35,062	0.406	1.495	0.154	**
$NUMANALYSTS_{i,m}$	658	4.941	4.880	3.000	40,820	6.692	6.396	4.000	***
Manager									
$MANAGERFE_{i,m}$	334	0.834	1.899	0.119	20,553	0.406	1.459	0.002	***
$\lvert MANAGERFE_{i,m} \rvert$	334	0.959	1.893	0.219	20,553	0.598	1.482	0.111	***
$PARACHUTE_{i,m}$	161	0.789	0.409	1.000	12,930	0.662	0.473	1.000	***
Ownership									
$BLOCKHOLDER_{i,m}$	847	0.170	0.157	0.141	51,061	0.136	0.142	0.099	***
$ACTIVIST_{i,m}$	378	0.181	0.182	0.113	16,542	0.189	0.219	0.098	.
$INSIDER_{i,m}$	800	0.092	0.178	0.019	54,040	0.115	0.206	0.026	***

Panel B: Firms seeking strategic alternatives identified by media leaks versus their industry-year peer firms

	Firms seeking strategic alternatives Media leaks				Industry-year peer firms				Difference in means
	N	Mean (a)	SD	Median	N	Mean (b)	SD	Median	*P*-value (a) ≠ (b)
Fundamentals									
$ASSETS_{i,q}$	151	6,385	19,526	1,642	20,583	5,306	19,024	478	.
$MKVAL_{i,q}$	151	2,534	3,248	1,515	20,583	3,290	9,372	370	***
$BTM_{i,q}$	151	0.542	0.534	0.430	20,583	0.630	0.670	0.481	**
$LEV_{i,q}$	151	0.601	0.254	0.589	20,583	0.551	0.290	0.529	**
$CASH_{i,q}$	151	0.174	0.187	0.103	20,583	0.226	0.252	0.115	***
$INTAN_{i,q}$	151	0.206	0.231	0.092	20,583	0.137	0.194	0.029	***
$\Delta EARN_{i,q}$	151	0.002	0.045	0.000	20,583	0.002	0.073	0.000	.
$REV_{i,q}$	135	0.229	0.186	0.172	14,264	0.256	0.216	0.200	*
$CFO_{i,q}$	151	0.015	0.055	0.016	20,583	0.005	0.065	0.009	**
$CFI_{i,q}$	151	-0.015	0.033	-0.010	20,583	-0.018	0.061	-0.009	.
$ACC_{i,q}$	151	0.009	0.074	0.004	20,583	0.007	0.085	0.004	.
$EMPGR_{i,y}$	149	0.069	0.235	0.026	17,965	0.091	0.333	0.030	.
Market									
$BETA_{i,y}$	151	1.248	0.919	1.156	20,583	1.208	0.954	1.096	.
$RET_{i,y}$	151	-0.046	0.454	-0.103	20,583	0.021	0.553	-0.047	*
$EPSFORECAST_{i,m}$	140	0.059	1.115	0.066	12,070	0.289	1.443	0.119	**
$NUMANALYSTS_{i,m}$	145	11.283	7.583	10.000	13,876	7.586	6.948	5.000	***
Manager									
$MANAGERFE_{i,m}$	88	0.389	1.380	0.012	6,976	0.388	1.409	0.000	.
$\lvert MANAGERFE_{i,m} \rvert$	88	0.476	1.366	0.088	6,976	0.560	1.440	0.099	.
$PARACHUTE_{i,m}$	72	0.833	0.375	1.000	4,090	0.753	0.431	1.000	*
Ownership									
$BLOCKHOLDER_{i,m}$	141	0.223	0.149	0.210	16,350	0.161	0.151	0.130	***
$ACTIVIST_{i,m}$	80	0.147	0.171	0.094	8,319	0.184	0.213	0.096	*
$INSIDER_{i,m}$	141	0.066	0.154	0.010	16,547	0.085	0.159	0.020	.

Notes: Panel A presents summary statistics for firms that disclosed strategic alternatives (*SA_DISC*=1) and their FF 48 industry-year peers (*SA_DISC*=0). Panel B presents summary statistics for firms that experienced leaked strategic alternatives (*SA_LEAK*=1) and their FF 48 industry-year peers *(SA_LEAK*=0). The right-most column in each panel presents *t*-tests of the differences in means between the two groups. ***, ** and * denote statistical significance at the 1, 5 and 10 percent levels, respectively, from two-tailed *t*-tests. See Appendix 2 for variable definitions.

TABLE 3

Correlation Matrix

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)
(1) ln($MKVAL_{i,q}$)		-0.28***	0.04***	-0.06***	0.22***	0.01***	-0.13***	0.24***	0.10***	0.04***	0.08***	0.18***	-0.01	**0.68*****	0.19***	-0.18***
(2) $BTM_{i,q}$	**-0.28*****		-0.05***	-0.18***	-0.06***	-0.01***	-0.05***	0.06***	-0.06***	-0.09***	-0.08***	-0.20***	-0.06***	-0.15***	-0.01***	-0.03***
(3) $LEV_{i,q}$	0.04***	0.03***		**-0.47*****	-0.05***	0.02***	0.10***	0.01***	-0.08***	-0.08***	-0.15***	-0.04***	-0.02***	0.02***	-0.08***	-0.05***
(4) $CHE_{i,q}$	-0.03***	-0.27***	**-0.48*****		-0.08***	-0.01	-0.21***	**-0.28*****	-0.07***	0.03***	0.25***	0.05***	-0.02***	-0.06***	0.04***	0.01***
(5) $INTAN_{i,q}$	**0.27*****	0.00	0.03***	0.04***		0.02***	-0.06***	0.08***	-0.00	-0.03***	0.09***	0.01***	-0.01***	0.14***	0.19***	-0.10***
(6) $\Delta EARN_{i,q}$	0.07***	-0.09***	-0.01***	0.01	0.02***		0.08***	0.11***	0.16***	-0.09***	0.02***	0.10***	0.14***	0.01***	0.00	0.00
(7) $REV_{i,q}$	-0.11***	-0.06***	0.08***	-0.14***	0.01	0.15***		0.22***	0.02***	-0.00	-0.06***	0.06***	0.06***	-0.03***	-0.03***	0.15***
(8) $CFO_{i,q}$	**0.28*****	-0.02***	-0.05***	-0.12***	0.10***	0.18***	**0.26*****		-0.15***	-0.03***	-0.10***	0.11***	0.08***	0.19***	0.09***	0.03***
(9) $ACC_{i,q}$	0.10***	-0.09***	-0.07***	-0.08***	-0.05***	0.15***	0.04***	-0.22***		0.15***	-0.01***	0.10***	0.07***	0.01***	-0.01	0.04***
(10) $EMPGR_{i,y}$	0.13***	-0.17***	-0.11***	0.05***	-0.05***	-0.03***	0.02***	0.03***	0.19***		0.04***	0.02***	0.01	0.01	-0.03***	0.06***
(11) $BETA_{i,y}$	0.12***	-0.16***	-0.18***	**0.26*****	0.11***	0.02***	-0.03***	-0.05***	-0.01***	0.04***		0.04***	0.02***	0.03***	0.07***	-0.03***
(12) $RET_{i,y}$	**0.28*****	-0.22***	0.02***	-0.00	0.08***	0.22***	0.07***	0.17***	0.12***	0.05***	-0.05***		0.17***	0.03***	-0.01	0.04***
(13) $EPSFORECAST_{i,m}$	-0.01	-0.15***	-0.03***	0.02***	-0.03***	**0.38*****	0.14***	0.09***	0.09***	0.04***	0.05***	**0.25*****		-0.02***	-0.00	0.03***
(14) $NUMANALYST_{i,m}$	**0.68*****	-0.21***	0.01	0.01	0.15***	0.05***	0.00	0.23***	0.04***	0.10***	0.09***	0.08***	-0.02***		0.03***	-0.15***
(15) $BLOCKHOLDER_{i,m}$	**0.26*****	0.01	-0.09***	0.04***	0.18***	0.01***	0.00	0.13***	-0.01	0.00	0.11***	0.03***	-0.01	0.13***		-0.16***
(16) $INSIDER_{i,m}$	**-0.33*****	0.00	-0.06***	0.03***	-0.16***	0.02***	0.18***	-0.02***	0.06***	0.10***	-0.06***	0.03***	0.08***	**-0.28*****	-0.18***	

Notes: Pearson pairwise correlations are presented on the upper right, and Spearman rank pairwise correlations are presented on the lower left. See Appendix 2 for variable definitions. *** indicates correlations significant at the 1% level. Correlation coefficients with magnitudes greater than 0.25 are bolded.

TABLE 4 (continued on the next page)

Modeling the Probability that the Firm Seeks Strategic Alternatives

Panel A: Strategic alternatives identified by corporate disclosures

	Dependent variable = $SA\_DISC_{i,t}$			
	Coefficients	Marginal Effects	Coefficients	Marginal Effects
	(1)	(2)	(3)	(4)
Intercept	0.113		N/A due	
	(0.897)		to F.E.	
ln($MKVAL_{i,q}$)	-0.121***	-0.044	-0.131***	-0.047
	(-6.950)		(-6.653)	
$BTM_{i,q}$	0.119***	0.044	0.134***	0.049
	(5.169)		(5.349)	
$LEV_{i,q}$	0.620***	0.226	0.631***	0.228
	(6.199)		(5.719)	
$INTAN_{i,q}$	0.277	0.101	0.309	0.112
	(1.518)		(1.294)	
$\Delta EARN_{i,q}$	-0.784***	-0.286	-0.842***	-0.305
	(-3.221)		(-2.944)	
$REV_{i,q}$	-0.411***	-0.150	-0.354**	-0.128
	(-2.642)		(-2.226)	
$CFO_{i,q}$	-0.213	-0.078	-0.337	-0.122
	(-0.600)		(-1.043)	
$ACC_{i,q}$	-0.259	-0.094	-0.320	-0.116
	(-1.239)		(-1.484)	
$BETA_{i,y}$	-0.046*	-0.017	-0.046*	-0.017
	(-1.699)		(-1.674)	
$RET_{i,y}$	-0.248***	-0.090	-0.251***	-0.091
	(-4.476)		(-4.852)	
$BLOCKHOLDER_{i,m}$	1.132***	0.413	1.217***	0.441
	(9.303)		(8.963)	
$DEMAND_{i,y}$	2.814***	1.026	N/A due	
	(2.863)		to F.E.	
Sample	Observations that disclosed strategic alternatives (*SA_DISC*=1) and their industry-year peers (*SA_DISC*=0)			
Fixed effects	No		FF 12 & year	
Clustered SEs	FF 48 & year		FF 48 & year	
Industry & year balancing	Yes		Yes	
Observations	44,248		44,248	
McFadden pseudo R^2	0.077		0.084	

Panel B: Strategic alternatives identified by media leaks

	Dependent variable = $SA\_LEAK_{i,t}$			
	Coefficients	Marginal Effects	Coefficients	Marginal Effects
	(1)	(2)	(3)	(4)
Intercept	-2.274***		N/A due	
	(-7.117)		to F.E.	
ln($MKVAL_{i,q}$)	0.203***	0.071	0.239***	0.081
	(4.100)		(4.300)	
$BTM_{i,q}$	0.062	0.021	0.014	0.005
	(0.531)		(0.112)	
$LEV_{i,q}$	0.623***	0.216	0.498**	0.169
	(3.440)		(2.369)	
$INTAN_{i,q}$	0.251	0.087	0.729*	0.248
	(0.748)		(1.696)	
$\Delta EARN_{i,q}$	-0.977**	-0.339	-0.896**	-0.304
	(-1.979)		(-2.176)	
$REV_{i,q}$	-0.424*	-0.147	-0.308	-0.105
	(-1.783)		(-0.875)	
$CFO_{i,q}$	0.273	0.095	0.066	0.023
	(0.348)		(0.094)	
$ACC_{i,q}$	0.337	0.117	0.276	0.094
	(0.591)		(0.364)	
$BETA_{i,y}$	-0.023	-0.008	0.004	0.001
	(-0.330)		(0.051)	
$RET_{i,y}$	-0.204	-0.071	-0.263*	-0.090
	(-1.569)		(-1.917)	
$BLOCKHOLDER_{i,m}$	1.539***	0.533	2.011***	0.684
	(4.320)		(4.424)	
$DEMAND_{i,y}$	8.407***	2.914	N/A due	
	(5.038)		to F.E.	
Sample	Observations with leaked strategic alternatives (*SA_LEAK*=1) and their industry-year peers (*SA_LEAK*=0)			
Fixed effects	No		FF 12 & year	
Clustered SEs	FF 48 & year		FF 48 & year	
Industry & year balancing	Yes		Yes	
Observations	11,317		11,269	
McFadden pseudo R^2	0.116		0.134	

Notes: This table presents probit regressions explaining the incidence of seeking strategic alternatives using firm attributes. Voluntary corporate disclosures of strategic alternatives (*SA_DISC*) is the dependent variable in Panel A. and media leaks of strategic alternatives (*SA_LEAK*) is the dependent variable in Panel B. The number of observations used in regressions is lower than the number of observations in the univariate analyses due to requiring non-missing variables. Standard errors are clustered by FF 48 industry and year. *Z*-statistics are in parentheses. ***, ** and * denote statistical significance at the 1, 5 and 10 percent levels, respectively, based on two-tailed tests. See Appendix 2 for variable definitions.

TABLE 5

Firms that Receive vs. Do Not Receive Bids

	Firms seeking strategic alternatives that receive bids				Firms seeking strategic alternatives that do not receive bids				Difference in means
	N	Mean (a)	SD	Median	N	Mean (b)	SD	Median	*P*-value (a) ≠ (b)
Fundamentals									
$ASSETS_{i,q}$	497	1,926	9,101	323	640	1,591	6,850	226	.
$MKVAL_{i,q}$	497	928	1,996	190	640	725	2,038	126	*
$BTM_{i,q}$	497	0.675	0.641	0.586	640	0.828	0.948	0.601	***
$LEV_{i,q}$	497	0.582	0.263	0.576	640	0.565	0.292	0.555	.
$CHE_{i,q}$	497	0.144	0.188	0.062	640	0.165	0.215	0.071	*
$INTAN_{i,q}$	497	0.099	0.182	0.000	640	0.099	0.182	0.000	.
$\Delta EARN_{i,q}$	497	-0.005	0.063	-0.000	640	-0.018	0.089	-0.003	***
$REV_{i,q}$	468	0.265	0.213	0.211	614	0.229	0.209	0.178	***
$CFO_{i,q}$	497	0.009	0.058	0.015	640	-0.008	0.079	0.005	***
$CFI_{i,q}$	497	-0.014	0.049	-0.010	640	-0.013	0.061	-0.007	.
$OPACC_{i,q}$	497	0.001	0.076	0.002	640	-0.012	0.116	-0.002	**
$EMPGR_{i,y}$	474	0.059	0.387	0.008	606	0.102	0.491	0.000	.
Market									
$BETA_{i,y}$	497	1.009	0.925	0.885	640	1.239	1.036	1.149	***
$RET_{i,y}$	497	-0.134	0.490	-0.178	640	-0.238	0.547	-0.317	***
$EPSFORECAST_{i,m}$	347	0.271	1.379	0.094	355	0.127	1.616	0.073	.
$NUMANALYSTS_{i,m}$	391	6.294	5.940	4.000	393	5.623	5.694	4.000	.
Manager									
$MANAGERFE_{i,m}$	186	0.651	1.616	0.057	225	0.774	1.870	0.104	.
$\lvert MANAGERFE_{i,m} \rvert$	186	0.762	1.582	0.156	225	0.901	1.883	0.194	.
$PARACHUTE_{i,m}$	121	0.793	0.407	1.000	104	0.808	0.396	1.000	.
Ownership									
$BLOCKHOLDER_{i,m}$	491	0.188	0.156	0.159	479	0.167	0.158	0.134	**
$ACTIVIST_{i,m}$	193	0.171	0.177	0.104	254	0.179	0.185	0.109	.
$INSIDERSHARES_{i,m}$	419	0.078	0.165	0.013	503	0.096	0.183	0.022	.

Notes: This table presents the antecedent characteristics of firms that receive versus do not receive M&A bids, from the sample of 1,137 firms that are seeking strategic alternatives (*SA*=1). The right-most column presents *t*-tests of the differences in means between the two groups. ***, ** and * denote statistical significance at the 1, 5 and 10 percent levels, respectively, from two-tailed *t*-tests. See Appendix 2 for variable definitions.

TABLE 6

Modeling the Probability that the Firm Receives a Bid

	Dependent variable = $BID1YR_{i,t}$			
	Coefficients	Marginal Effects	Coefficients	Marginal Effects
	(1)	(2)	(3)	(4)
ln($MKVAL_{i,q}$)	0.026	0.010	0.018	0.007
	(0.767)		(0.539)	
$BTM_{i,q}$	-0.096*	-0.035	-0.116**	-0.042
	(-1.649)		(-1.960)	
$LEV_{i,q}$	-0.012	-0.004	-0.019	-0.007
	(-0.057)		(-0.087)	
$INTAN_{i,q}$	-0.230	-0.084	-0.218	-0.080
	(-0.623)		(-0.562)	
$\Delta EARN_{i,q}$	1.133*	0.417	1.026	0.374
	(1.684)		(1.386)	
$REV_{i,q}$	0.428	0.158	0.420	0.153
	(1.472)		(1.458)	
$CFO_{i,q}$	1.284**	0.472	1.060*	0.387
	(2.314)		(1.832)	
$ACC_{i,q}$	0.146	0.054	0.069	0.025
	(0.303)		(0.138)	
$BETA_{i,y}$	-0.119***	-0.044	-0.110**	-0.040
	(-2.597)		(-2.371)	
$RET_{i,y}$	0.101	0.037	0.081	0.030
	(0.944)		(0.726)	
$BLOCKHOLDER_{i,m}$	0.658*	0.242	0.625*	0.228
	(1.862)		(1.711)	
$3DAYRET_{i,t}$			0.673**	0.246
			(2.131)	
Sample	Observations seeking strategic alternatives (SA=1)			
Fixed effects	FF 12 & year		FF 12 & year	
Clustered SEs	FF 48 & year		FF 48 & year	
Observations	920		920	
McFadden pseudo R^2	0.073		0.079	

Notes: This table presents results from probit regressions of an indicator variable, *BID1YR*, which =1 if the firm received a bid within one year, on firm attributes. The intercept is not presented due to the inclusion of fixed effects. The number of observations used in regressions is lower than the number of observations in the univariate analyses due to requiring non-missing variables. Standard errors are clustered by FF 48 industry and year. *Z*-statistics are in parentheses. ***, ** and * denote statistical significance at the 1, 5 and 10 percent levels, respectively, based on two-tailed tests. See Appendix 2 for variable definitions.

TABLE 7

Modeling the Probability that the Firm Receives a Bid from the Population

	Dependent variable = $BID1YR_{i,t}$	
	Coefficients	Marginal Effects
	(1)	(2)
ln($MKVAL_{i,q}$)	-0.035***	-0.006
	(-3.098)	
$BTM_{i,q}$	0.054*	0.009
	(1.803)	
$LEV_{i,q}$	0.170***	0.028
	(2.886)	
$INTAN_{i,q}$	0.276**	0.046
	(2.347)	
$\Delta EARN_{i,q}$	0.234***	0.039
	(2.592)	
$REV_{i,q}$	-0.003	-0.000
	(-0.033)	
$CFO_{i,q}$	-0.238	-0.040
	(-0.962)	
$ACC_{i,q}$	-0.479***	-0.080
	(-5.259)	
$BETA_{i,y}$	-0.020	-0.003
	(-1.398)	
$RET_{i,y}$	0.008	0.001
	(0.592)	
$BLOCKHOLDER_{i,m}$	0.581***	0.096
	(8.327)	
Sample	*SA*=1 observations and their *SA*=0 industry-year peers	
Fixed effects	FF 12 & year	
Clustered SEs	FF 48 & year	
Observations	46,153	
McFadden pseudo R^2	0.022	

Notes: This table presents results from the probit regression of an indicator variable, *BID1YR*, which =1 if the firm received a bid within one year, on firm attributes. The intercept is not presented due to the inclusion of fixed effects. Standard errors are clustered by FF 48 industry and year. *Z*-statistics are in parentheses. ***, ** and * denote statistical significance at the 1, 5 and 10 percent levels, respectively, based on two-tailed tests. See Appendix 2 for variable definitions. Instead of only using the *SA*=1 observations as in the previous table, this table uses the *SA*=1 and *SA*=0 observations.