Motivating Takeover Bids

A Problem

- Consider the case of Acme widgets, badly mismanaged
  - Profits are $\pi^*$
  - Shares are selling at $40

The Opportunity

- Offer to pay existing shareholders $60
  - Existing shareholders make money.
  - You make money.

The Fly in the Ointment

<table>
<thead>
<tr>
<th>Shareholder Decision</th>
<th>Tender Offer</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Successful</td>
</tr>
<tr>
<td>Tender</td>
<td>$60</td>
</tr>
<tr>
<td>Don’t Tender</td>
<td>$80</td>
</tr>
</tbody>
</table>
Some Suggestions

• How then do we allow bidders to profit?

• Treat tendered and non-tendered shares differently.
  – Shares sell for $40; properly managed, worth $80.
  – Offer $80 for first 51% of shares and then buy the rest at $40.

Not legal under US Securities Law

Some Suggestions

• Let bidders profit from the first 5% of the shares.
  – Secretly buy the first 5% at $40 and then make intentions public.
Some Suggestions

Let bidders profit from the first 5% of the shares.
– This is the edge in American Law
– The effect is to reduce the incentives for takeovers.

©2004 Charles W. Upton