Chapter 5 Summary and Conclusion

5.1. Summary of the study

The exchange ratios, especially in a stock for stock merger, are usually determined by the level of reported earnings of both acquiring and acquired firms in M&As transactions. If acquiring firms have higher level of earnings, they can merge target firms with fewer stocks to avoid the problem of equity dilution. Similarly, acquired firms can get more stocks from acquiring firms to maximize their shareholders wealth if they have higher level of earnings. Therefore, we investigate the degree of earnings management in Taiwan’s financial institutions before announcing M&As transactions. By focusing on fourteen financial holding companies in Taiwan, we further examine if exchange ratios are really affected by manipulated earnings and if investors can detect these earnings manipulations before M&As announcements.

From empirical results in Chapter 4, we find (1) that the degree of earnings management is much higher in the period prior to M&As announcements given financial institutions in Taiwan are used to manipulating earnings at usual times, (2) that those financial institutions with higher degree of earnings management indeed get more favorable exchange ratios within M&As transactions relative to those with lower degree of earnings management for both acquiring and acquired companies, and (3) that investors will not punish those financial institutions obtaining better exchange ratios by manipulating reported earnings in the market since they can’t see through managers’ tricks when we focus on the sample of Taiwan’s banking industry. In stead, cumulative abnormal returns for firms with higher degree of earnings manipulations are a little more than firms with lower degree of
earnings management, indicating that investors care only about the number of shares they can get immediately after the completion of mergers but not the synergies within M&As transactions.

5.2. Suggestions for further research

With the severe competition in global, more and more M&As activities are expected to be announced in all industries worldwide. Moreover, a stock for stock merger determined by reported earnings of both acquiring and acquired firms is the most common method for M&As. Therefore, researches hereafter can use data from different industries besides banking to investigate if it is a consistent phenomenon that managers also have incentives to manage earnings prior to M&As announcements in different industries.

In detecting earnings manipulation, although the Jones model already provides good explaining ability by US data, further researches still can use data in Taiwan to find stronger supports in this model, or to further modify it according to the situation in Taiwan. Similarly, the Larson-Godenes model can be modified by considering the nature of industry, which can be proxied by industry-specific risk, for the following researches.