

# Analysis of payment methods in merger and acquisition deals within the United Kingdom

Akindele Babatunde Omotesho

*Department of Finance, University of Strathclyde Business School,  
Glasgow, UK, and*

Ayodeji Michael Obadire

*School of Finance and Professional Studies, Botswana Accountancy College,  
Gaborone, Botswana*

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## Abstract

**Purpose** – This study aims to examine the effects of payment methods used in mergers and acquisitions (M&A) conducted by UK companies spanning the period from 2007 to 2019.

**Design/methodology/approach** – The study used the estimated expected returns method to identify abnormal returns during the deal announcement period, applying event study analysis with both univariate and multivariate regression models to detect cumulative abnormal returns around the announcement timeframe.

**Findings** – The results show a short-term positive return increase for acquiring firms, controlling for deal-specific characteristics like target firm location and payment methods. The authors observed a preference for cash financing across domestic and cross-border transactions. Multivariate analysis revealed insignificance between payment methods and deal characteristics like cross-border acquisitions and diversification.

**Research limitations/implications** – The study's focus on publicly traded firms in the UK and the absence of a comparative analysis across different regions and markets limits the sample size and may impact the generalizability of findings.

**Practical implications** – The study proposes three practical implications. Firstly, firms should tailor payment methods to each transaction, aligning with strategic goals to optimize value and mitigate risks. Secondly, decision-makers must prioritize comprehensive due diligence and strategic alignment throughout M&A processes to enhance success and maximize synergies. Finally, analysing broader strategic contexts and regulatory landscapes when structuring transactions enables goal attainment, such as market expansion or value creation.

**Social implications** – The study's findings can promote transparency and accountability among corporate decision-makers in M&A transactions. Stakeholders can advocate for transparent decision-making processes, enhancing trust in corporate governance.

**Originality/value** – This study provides valuable insights into the impact of payment methods on shareholder value in M&A transactions involving UK companies, informing strategic decision-making and contributing to the understanding of corporate finance dynamics.

**Keywords** Mergers and acquisitions, Acquiring firms, Payment methods, Listed companies, Developed nations

**Paper type** Research paper



## 1. Introduction

Mergers and acquisitions (M&A) refer to corporate strategies involving the consolidation of two or more entities (Tanna and Yousef, 2019). According to Melnyk (2020), companies merge to form a new entity, pooling resources for enhanced efficiency. Acquisitions, on the other hand, involve one company absorbing another, either maintaining the acquired entity's identity or integrating its operations (Tanna and Yousef, 2019). Though characterized by a prominent level of business and operational risk, business organizations leverage M&As for several reasons including scaling business operations, optimizing management capacities, improving competitiveness in the markets and increasing profitability among others. The success of an M&A transaction hinges on meticulous planning, due diligence and seamless integration to capitalize on intended benefits while mitigating potential challenges.

M&As over the years, have presented a wide range of business opportunities for businesses across the world. M&As represent a major channel of allocating resources to business areas they are most needed and eliminating inefficient and ineffective managers. DePamphilis (2010) and Tanna and Yousef (2019) highlighted that the objective of M&As in the business world is to facilitate the optimization of the merged companies' assets for potential synergy for the markets to appropriately reward their shareholders.

M&A transactions have complex strategic implications for an acquiring company. This implies that the transaction process must be well thought out to achieve its objectives. Crucial factors that typically determine the nature and process of an M&A would include strategic rationales, tax implications, accounting treatment, integration plans and form of purchase considerations (Güven, 2020). The major methods of payment consideration in M&A transactions are share or stock exchange, cash or a mix of both.

The answer of payment method choice is one that is critical to the success of every M&A transaction. Melnyk (2020) and Güven (2020) highlighted the major drivers influencing the decision on payment method in a transaction including financial leverage, business cycle, stock market valuations, income tax exposures and interest rate movement. There are three types of payment methods: cash, stock and a combination of both.

Because of the liquidity nature of cash, this form of payment method tends to be the most often used. The acquiring firm can decide to either use its cash or borrow cash to finance the transaction. Although using cash has the advantage of no risk of control dilution, it can be extremely expensive. On the other hand, the stock payment method involves share exchange considerations. Often, acquiring firms use shares exchange to gain controlling interest in the target. While this is the most popular type of share payment method, others include exchange of intellectual properties, assets and royalties (Dutta *et al.*, 2013).

The combination of the stock and cash method derives its logic from the pecking order theory. Majluf and Myers (1984) explained that a company's managers tend to finance their business in the following order: internal sources, debt financing and equity financing. Furthermore, Bruner (2004) created a decision tree explaining payment methods choice and their impact on financing M&A transactions. Bruner (2004) explains that the form of payment in an M&A transaction has a direct impact on financing decisions. For the cash payment method, additional cash injections are not needed since there is no movement in liabilities or equity. Financing through a new issuance of stock, on the other hand, entails the acquirer releasing additional shares for sale on a stock exchange to obtain capital, enabling the acquisition of target company shares. This mode of financing leads to ownership dilution, resulting in a loss of control and susceptibility to external intervention, a phenomenon absent in the preceding financing methods.

Several studies indicate that payment methods on M&A deals have a significant impact on returns before and after the announcement of the transaction. For instance,

Song and Walking (1993) noted a surge of 20%–40% increase in the target's firm values while Huurenkamp (2020) showed +20.04% cumulative average abnormal returns (AAR) during the  $-1/+30$  event period. In contrast, Andrade *et al.* (2001) noted a negative return of between  $-2\%$  and  $-3\%$  within a few days surrounding the transaction announcement while Fuller *et al.* (2002) found that acquiring firms had materially negative average returns when buying public target companies. Hirshleifer (1995) quoted four key factors that influence selection of payment methods in M&A transactions. The four key factors include tax benefits of equity; value of equity in restricting overpayment; cheapness of equity for overvalued bidder and finally exploitation of the target's information through equity financing.

These contradictory findings underscore the complexity of M&A dynamics, particularly in developed markets. This study's significance lies in its investigation into whether similar patterns can be observed within the UK market. Specifically, it addresses how different payment methods influence M&A transaction returns in developed economies, using the UK as a case study.

More so, the significant research gap in the study of payment methods in M&A deals is the predominant emphasis on the financial aspects of these transactions and the challenge of identifying a "successful" M&A transaction. Meglio and Risberg (2010) asserted that this might stem from the wide array of measurement tools available to researchers, leading to inconsistent results. Additionally, existing literature on M&A has focused primarily on the short-term value gained by shareholders of target companies due to the premium paid during acquisition. However, this focus reveals that acquiring firms often do not achieve long-term profitability, highlighting a significant gap regarding short-term value creation within the context of UK companies. This study aims to bridge this gap by examining the short-term impacts on acquiring firms and the influence of payment methods in the UK's M&A landscape.

By addressing this research question via the proposed hypotheses, this study contributes valuable insights into the understanding of M&A dynamics within the UK market context. The study sheds light on the factors influencing transaction outcomes and the effectiveness of various payment strategies and offer practical recommendations for firms and policymakers involved in M&A activities, helping to optimize decision-making processes and enhance deal performance. Following the brief introduction, the rest of the paper is organized as follows: literature review, methodology, empirical discussion of results and, finally, the conclusion and recommendations.

## 2. Literature review and hypothesis formulation

### 2.1 Conceptual and empirical understanding of mergers and acquisitions

2.1.1 *Nature of acquisition.* The two forms of business growth are organic growth and inorganic growth. Organic growth is the growth derived from internal expansions such as operations, financial and staffing (Austin, 2020). Inorganic growth, on the other hand, is achieved through acquisitions, mergers and other forms of external takeovers (Bhattacharya *et al.*, 2021). The inorganic growth strategy helps acquiring firms explore other markets and expand their balance sheets. However, this strategy comes with downsides including agency conflicts and synergies problems.

Jensen (1986) highlighted that managers of an acquiring firm can view a potential merger or acquisition as a good move while its shareholders may have a divergent view. For example, Royal Dutch Ahold's managers were reported to have acted in their interest and not in the interest of its shareholders when the company acquired its competitors (De Jong *et al.*, 2005). This in the long run affected the returns of Royal Dutch Ahold, as the company did not have long-term plans for the acquisitions. De Jong *et al.* (2005) posited that inorganic

growth strategy does not necessarily increase shareholder's value, especially when there are no long-term business aspirations for the target firms.

In previous empirical studies, the target firm's country appears to have a significant impact on acquisitions' returns. [Dutta et al. \(2013\)](#) posited managers' preference for cross-border acquisitions over domestic acquisitions due to the strict take-over regulations, higher relative size of transactions and increased concentration of ownership. The research, however, does not explain if given the same characteristics for domestic acquisitions, the results would be different. On the flip side, [Moeller and Schlingemann \(2005\)](#) noted insignificant differences between domestic and cross-border acquisitions:

*H1.* Announcement of an M&A transaction will increase shareholder's value of the acquiring firm on a short-term.

*2.1.2 Payment methods in mergers and acquisitions deals.* [Keynes \(1936\)](#) is reputed to have postulated the notion that excess cash in a company enables the organization to invest in projects considered valuable for a long time. [Harford \(1999\)](#) noted that when an acquirer has excess cash in the bank, it is highly likely to make a significant decision on acquisition of a target in line with its business objectives. However, [Jensen \(1986\)](#) concluded that such a motive tends to lead to the unprofitability of the acquisitions.

There has been no consensus on whether financial leverage plays a part in determining payment method choice in acquisitions. While [Kanungo \(2021\)](#), [Brailsford et al. \(2002\)](#), [Martin \(1996\)](#) and [Friend and Lang \(1988\)](#) refute claims of leverage impacting cash payment method decisions, [Klitzka, He and Schiereck \(2022\)](#), [Kim and Sorensen \(1986\)](#) and [Faccio and Masulis \(2005\)](#) presented that a company's leverage position and size determines whether acquisitions are funded by cash or not. In addition, [Yang et al. \(2017\)](#) posit strong evidence of the positive effect of liquidity ratio (primarily cash ratio) of the acquirer on selecting cash as payment method for acquisitions in China.

In determining the likelihood of selecting stock as a preferred payment method, the relative target size appears to be a common consideration in various empirical studies. For instance, [Grigorieva and Fomenko \(2012\)](#) examined 825 M&A transactions in the BRICS countries and concluded that the size of the target is a major determinant factor for choosing stock as a payment method. Similarly, [Al-Khasawneh et al. \(2020\)](#), [Yang et al. \(2017\)](#) and [Zhang \(2003\)](#) found that the target's relative size significantly influences the payment method in M&A transactions in China and the UK.

However, this consensus is not universal. [Martin \(1996\)](#) reported a contrasting view regarding the impact of the relative size of the target on the choice of payment method. In his research, Martin explained that the predictor variable was not significant at the 5% level of significance in his regression analysis. [Ghosh and Ruland \(2002\)](#) also shared a similar view with Martin, challenging the importance of target size as a determinant in payment method selection.

These discrepancies underpin the complexity of factors influencing payment method choices in M&A transactions. While several studies affirm the significance of target size, the contrary findings by Martin and Ghosh and Ruland suggest that other variables and contextual factors may also play critical roles. This divergence calls for a more nuanced investigation into the determinants of payment methods, considering the potential influence of market conditions, regulatory environments and firm-specific characteristics.

Another major area of research determining the choice of payment methods is the control hypothesis. [Yin \(2001\)](#) defines control as the guardianship and possession of decisive power or influence over a company's operational management and other policies. The control hypothesis hinges on the notion that shareholders' hesitation to lose control of the company

(via shares dilution) would make managers less likely to issue stocks as financing methods in M&A transactions.

Stulz (1988) concluded that the greater the control power of a company's majority shareholders, the more likely the acquiring firm is to select cash as the transaction's payment method. This view is supported by Martin (1996), Yook *et al.* (1999) and Amihud *et al.* (1990), who found an inverse relationship between control and the use of stock as financing in the USA. Martin (1996) further explained that managers do not seem to be concerned about control dilution at very high or low levels of ownership control. However, he highlighted the possibility of managers losing control of the firm at the middle range of ownership control.

These findings suggest a general consensus on the relationship between shareholder control and payment methods in M&A transactions. However, the nuance in Martin's (1996) observation about varying levels of ownership control introduces complexity. While high and low levels of control do not significantly impact managers' financing choices, the middle range poses a unique challenge. This inconsistency indicates that while control is a critical factor, its influence may vary depending on the specific ownership structure of the firm. This highlights the need for further research to explore the conditions under which control considerations significantly affect payment method choices, and its impact on shareholders' value in different market environments and ownership contexts:

H2. The payment method used in financing a transaction has an impact on shareholder's value on a short-term.

*2.1.3 Abnormal returns in mergers and acquisitions.* One major expectation for companies leveraging M&A is the hope to generate specified returns in line with their business objectives. Loukianova *et al.* (2017) noted that abnormal returns are often based on the expected synergies of a merger or acquisition. Lang and Stulz (1994) explored the change in stock market values by contrasting the targets' Tobin's Q ratio, defined as the total market value of a target over the target's assets replacement cost. They pointed out that recently merged or acquired targets generally had lower Tobin's Q relative to their unmerged or unacquired peers.

Draper and Paudyal (1999) analysed a sample of the UK acquiring companies between 1988 and 1996. Their research findings indicate that cash acquirers do not experience significant abnormal returns during the event period, whereas stock acquirers encounter significant negative returns. These results align with the earlier findings of Travlos (1987). However, the contrasting perspectives on returns highlight the complexity of predicting M&A outcomes based on payment methods alone.

Huang and Walking (1987) noted a positive cumulative abnormal return (CAR) of 23.4% for target firms during a -50/-1 event study window. Similarly, Eckbo (1983) and Carvalho and Camargos (2013) found positive CARs for target firms during the -1/+10 and -10/+10 event windows, respectively. Conversely, Graham *et al.* (2002) took a different approach by further studying the impact on returns around the announcement dates and long-term postannouncement event windows. They discovered a 3% AAR two years after the announcement, followed by a decline of 7% afterwards. These mixed findings suggest that the timing and duration of event windows significantly influence the observed abnormal returns, necessitating a more nuanced approach to analysing M&A performance.

Some empirical studies find that most conglomerates are priced at discounts, resulting in billions of dollars in market value being eroded. Lins and Servaes (1999) discovered that M&A transactions in Japan and the UK were priced at a discount of 10% and 5% of market value, respectively. The study also suggested that differences in corporate governance of international targets affected the value of M&A transactions. This highlights the importance

of considering governance structures when evaluating M&A deals, particularly in cross-border contexts.

Berger and Ofek (1995) noted an average decline of 13% to 15% in shareholders' value of acquiring firms between 1986 and 1991, primarily due to cross-subsidization and overinvestment. Gugler *et al.* (2003) highlighted that 50% of US mergers reported negative CAR in the years following the merger. Meeks (1977) and Salant *et al.* (1983) revealed that 43% of merged firms globally reported lower profits compared to comparable firms that were not merged. These findings underpin the risks associated with M&A activities and the potential for value destruction, emphasizing the need for rigorous due diligence and strategic alignment to mitigate these risks. The discrepancies in the literature indicate that while M&A can offer significant returns under certain conditions, there is considerable variability in outcomes, reflecting the complex and multifaceted nature of these transactions:

H3. Stock financing is preferable than other payment methods in M&A transactions.

## 2.2 Theoretical motivation

This study is grounded on three relevant theories that explain the payment dynamics of M&A transactions. The underpinning theories are the agency theory, information asymmetry and signalling theory. The review of these theories shed light on and provided insight into the complex dynamics of M&A.

The agency theory of Ross (1973), proposes that an agency relationship emerges when one party represents another, known as the principal or stakeholder, while the other party acts on their behalf. This representation typically occurs in companies where management, including the board of directors, represents shareholders (Obadire *et al.*, 2022). Jensen and Meckling (2019) extended this theory, asserting that optimal outcomes for principals are achieved when they incur agency costs. Agents, often not aligned with shareholders' interests, can be incentivized to better serve shareholders through these costs. By establishing agency costs, the relationship between principal and agent is bound, fostering optimal results. Agency theory is relevant in the context of M&A deals as it addresses the relationship between the principals (shareholders) and agents (management). In M&A transactions, the choice of payment method can be influenced by the alignment of interests between shareholders and management. For instance, cash payments may be preferred to mitigate agency problems, ensuring that management acts in the best interest of shareholders. Allen *et al.* (2022) further added that to encourage managers to give their best possible effort, their compensation is often tied to the value that they add to the firm.

Information asymmetry is a critical factor in M&A deals, where the buyer and seller may have different levels of information. According to Song *et al.* (2021), the information asymmetry perspective posits that stock market investors do not have access to all the information that the acquirers' manager has about their firms and the targets. In situations characterized by information asymmetry, providing cash payments sends a favourable signal to the market. Conversely, in public deals, using stock payments tends to have a detrimental effect on the valuation of the company as the acquiring company believes its stock is undervalued (Majluf and Myers, 1984). Regardless, acquirers are motivated to opt for stock financing in situations of high information asymmetry regarding the target company. This will enable them to enhance their market integration by fostering improved customer-supplier relationships post-transaction.

Moreover, Luijckx Sam (2021) highlighted that signalling theory in the M&A landscape essentially builds on the notion that when there is a lot of information asymmetry in the market, there is a distinction between high-quality and low-quality senders. This distinction arises because signals incur costs, limiting the number of senders capable of transmitting signals due to the associated expenses (Bergh *et al.*, 2014). As such, signalling theory

suggests that the method of payment can act as a signal, conveying information about the acquiring firm's confidence in the deal. Understanding these theories helps in selecting payment methods that minimize information asymmetry and convey favourable signals.

### 3. Methodology

#### 3.1 Data, sample and models

This study investigates significant acquisitions announced and executed between 2007 and 2019, exclusively involving UK-based companies as acquiring entities. Data was sourced from the UK M&A transactions database within the Department of Accounting and Finance at Strathclyde Business School. The sample selection criteria encompassed several parameters: transactions occurring within the specified timeframe; deals classified as "completed"; acquisition funding via cash, stock or a combination thereof; a minimum deal value of £1m; and the acquirer being either publicly listed or privately held within the UK. The data set comprises 200 samples, capturing various transaction characteristics such as market capitalization, payment method, deal value, deal structure, target firm's geographic operations and announcement date.

The methodology used to detect the presence or absence of abnormal returns surrounding the deal announcement period is the event study method. This method was first used by [Fama et al. \(1969\)](#) to explain stock price reactions to information availability in the market. [Khotari and Warner \(2006\)](#) explains that an event study aims to test the behaviour of return for a given sample with similar events pattern. The event study method is particularly suitable as the enormity of abnormal returns performance provides a basis to explore the reaction of the event (abnormal returns) on target's shareholders.

#### 3.2 Event study method

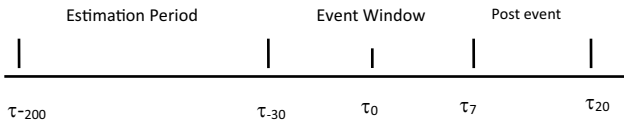
While it is difficult to trace the exact origin of the event study methodology, the first empirical research on the subject was conducted in 1933 by James Dolley. [Dolley \(1933\)](#), in his research, scrutinized stock price reactions to 95 sample stock splits between 1921 and 1931. Recent studies have estimated the event window based on performance metrics and length of the event study. [Barber and Lyon \(1994\)](#) highlighted that beyond examining the scope of stock market impact and reactions, the event method also measures other business-level effects such as operational and financial performance.

The event study method has grown in its relevance across several disciplines including finance, econometrics, marketing, statistics and engineering. [Kothari and Warner \(2007\)](#) conducted an analysis of 500 companies and their event studies' properties. They discovered the event studies properties were contrasting based on sample companies' characteristics and time length. [Corrado \(2011\)](#) assessed disparities in short-term event windows to adjust for event-based volatility and nonnormality adjustment while [Binder \(1998\)](#) and [MacKinlay \(1997\)](#) explored the use of event study method in finance, detailing the procedures for regression analysis and its interpretations.

The event-study method can be categorized into short-term study and long-term study. [MacKinlay \(1997\)](#) and [Brown and Warner \(1985\)](#) defined short-term event study method as a maximum event window length of 40 days while [Lyon et al. \(1999\)](#) explained that long-term event studies aim at identifying abnormal returns between one to eight years. [Kothari and Warner \(2007\)](#) have, however, highlighted the huge limitations of long-term event study such as low reliability and difficulty in results interpretation. This has also been supported by [Brown and Warner \(1985\)](#) and [Lyon et al. \(1999\)](#).

In recent years ([Singh et al., 2024](#); [Yousaf et al., 2022](#)), two main changes have evolved in the event study methodology; the use of intraday and daily returns instead of the typical monthly return data, which leads to a more precise abnormal returns calculations and secondly, the sophistication of estimating abnormal returns and its statistical importance.

The event window study for this paper is displayed below:



where:

- $\tau_{-200}$  = beginning of sample period;
- $\tau_{-30}$  = beginning of event study window;
- $\tau_0$  = event day;
- $\tau_7$  = end of event study window; and
- $\tau_{20}$  = end of sample period.

In this study, the returns between  $-30/+7$  event window have been examined to compute the CARs. The basis for the event window estimation is based on [Dyckman et al. \(1984\)](#) who noted that reducing event window estimation period indicates a positive impact on the identification of abnormal returns.

To evaluate short-term effects, returns within  $+5/-5$  and  $+3/-3$  windows have also been examined. These two alternative windows were selected based on three factors: the level of abnormal returns, significant abnormal trading activities and abnormal intraday volatility, as proposed by [Krivin et al. \(2003\)](#). To enhance the robustness of the test, it is generally acceptable to include alternative event study windows. For example, [Thirumalai and Sinha \(2011\)](#) and [Kalaignanam et al. \(2013\)](#) adopted six event windows each to assess the reactivity of their results. Additionally, other researchers such as [Modi et al. \(2015\)](#), [Zhao et al. \(2013\)](#) and [Girotra et al. \(2007\)](#) examined at least two event windows in their studies, with sample sizes ranging from 132 to 223.

### 3.3 Estimating expected returns model

This study uses the market model to observe the presence of abnormal returns. [Pettengill and Clark \(2001\)](#) logically explained that the application of the model would typically result in expected returns estimate bias and consequently, lead to biased estimates of abnormal returns. The market model highlights the variation between the expected returns and actual returns in normal market conditions. Parameters of the market model are estimated using the observations from the event window period.

A security expected return of a firm is defined as:

$$R_{it} = \alpha + \beta R_{mt} + \varepsilon_{it} \quad (1)$$

where:

- $R_{it}$  = return on target company;
- $R_{mt}$  = return on the market;
- $\alpha$  and  $\beta$  = market mode parameters; and
- $\varepsilon_{it}$  = error term.

The abnormal return, calculated as actual returns minus expected returns, is as follows:

$$A_{it} = R_{it} - (\alpha + \beta R_{mt}) \quad (2)$$

### 3.4 Aggregation and statistical tests of mean excess returns

The aggregation of abnormal returns is estimated using cross-sectional data (sample firms and event window period) on a daily basis. [Brown and Warner \(1985\)](#) summarized the daily estimation of the ARRs as follows:

$$\bar{A}_t = \frac{1}{N} \sum_{i=1}^{N_t} A_{i,t} \quad (3)$$

where:

$A$  = abnormal returns; and

$N$  = number of sample securities.

To calculate the statistical significance test of abnormal returns ( $t$ -test), the formula below is used:

$$T = \frac{\bar{A}_t}{S(\bar{A}_t)} \quad (4)$$

The CAR is then estimated as:

$$CAR_t = \bar{A} + CAR_{t-1} \quad (5)$$

To investigate the significance of CAR across the event window ( $\tau_{-30}$  to  $\tau_7$ ), the estimation of the test statistic is computed as:

$$T = \frac{\sum_{t=-30}^{+7} \bar{A}_t}{\left( \sum_{t=-30}^{+7} S^2(\bar{A}_t) \right)^{1/2}} \quad (6)$$

The calculated  $t$ -statistic for any given period in the event study window is given as:

$$\left( \sum_{i=1}^{N_t} A_{it} \right) \cdot (N_t)^{-1/2} \quad (7)$$

## 4. Empirical findings and discussions

### 4.1 Descriptive statistics

Table 1 below presents the summary descriptive statistics for the acquiring firm and payment methods used in financing sample M&A transactions.

Table 1 presents descriptive statistics pertaining to M&A transactions categorized by payment method (cash, stock, mixed) within a specific event window extending from  $-30$  to  $+7$  days relative to the announcement date. Each payment method category is delineated by the number of transactions ( $n$ ) and provides insights into various metrics' mean and median values. For instance, in terms of acquiring firm characteristics, the table showcases the mean and median market capitalization values in million dollars for each payment method. Additionally, the market-to-book value ratio, indicating the relationship between a company's market value and its book value, is delineated across the payment method categories.

These insights shed light on the financial stature and valuation metrics of acquiring firms associated with different payment methods. Furthermore, the table outlines key deal characteristics such as the relative size of the deal, presented as mean and median percentages in relation to the acquiring firm's market capitalization. This offers an understanding of the significance of M&A transactions relative to the acquiring firms' overall market value. Moreover, market performance metrics, including daily return and abnormal return, provide valuable insights into the stock price movements of acquiring firms during the event window.

**Table 1.** Descriptive statistics: mean, median and standard deviation of payment method

Acquiring firm	Descriptive statistics (-30/+7 event window)											
	Cash (n = 173)			Stock (n = 8)			Mixed (n = 19)			Total (n = 200)		
	Mean	Median	Mean	Median	Mean	Median	Mean	Median	Mean	Median	Mean	Median
Market capitalization (\$'m)	4,119	576	6,388	2,613	581	166	3,874	576				
Market-to-book value ratio	2.88	2.27	3.42	1.88	3.21	2.79	2.93	2.27				
Relative size of deal (%)	7	4	35	26	29	18	11	4				
Daily return (%)	0.18	0.10	0.01	-0.07	0.27	0.33	0.10	0.11				
Abnormal return (%)	1.14	-1.15	-0.11	-0.18	0.18	0.24	0.97	-0.98				
Payment method												
Daily return		Std dev (%)		Std dev (%)		Std dev (%)		Std dev (%)				
Abnormal return		1.04		0.96		0.69		0.20				
		0.26		0.91		0.68		0.24				

**Source:** Authors' compilation (2023)

By delineating these statistics across payment method categories, the table facilitates a comprehensive examination of how payment method choices may influence acquiring firms' financial profiles and market performance surrounding M&A announcements.

Table 1 reveals that the mean daily returns and CARs for acquiring firms are the highest when financed by a mix of cash and stock. This result, however, disagrees with Kling *et al.* (2013) who noted that mixed payment method poses a lower abnormal return than a cash payment method. It also shows that acquiring firms that use stock to finance an acquisition have higher average market-to-book value ratio, consistent with results from Faccio and Masulis (2005) and Martin (1996).

Also, as seen in Table 1, the standard deviation of returns is the highest when deals are financed by stock (daily return = 0.96%, abnormal return = 0.91%). This implies that an acquiring company with a high-risk appetite, indicated by the standard deviation, is more likely to finance the acquisition of a target wholly by stock. Hansen (1987) explains that the tendency of acquiring firms to use stock is based on the fact that target shareholders are typically forced to share post-acquisition losses if the target is overvalued. This risk-sharing mechanism can make stock financing attractive for acquirers, especially in volatile market conditions.

The volatility arising from financing deals solely by issuing stock can be attributed to several factors. Integration risks, uncertainties in regulations, market sentiments and impacts on financial performance all contribute to increased volatility. Investors' perceptions play a critical role in determining the value of the acquirer's stock. If investors believe that an acquirer's stock is overvalued, there will likely be a significant downward movement in the share price following the M&A announcement. This reaction reflects concerns about potential overpayment and future dilution.

Additionally, Rostyslav (2020) noted that the issuance of new shares leads to dilution, causing the value of existing shares to drop. This dilution effect prompts investors to reassess their shareholdings considering the increased outstanding shares count. The reassessment can lead to sell-offs, further driving down the share price and adding to the overall volatility of the stock.

Speculators' behaviour adds another layer of volatility to stock-financed deals. Market participants often trade based on their anticipation of a deal's outcome, leading to price swings driven by speculation rather than fundamental analysis. Short-term trading and high-frequency trading reinforce these cyclical changes, making stock prices more volatile. This speculative activity can create significant price fluctuations in the short term, complicating the acquirer's efforts to stabilize the stock price post-acquisition. Critically, while stock financing allows companies to preserve cash and potentially share post-acquisition risks, the associated volatility can undermine investor confidence and long-term value creation (Rostyslav, 2020). Firms must carefully consider these trade-offs and implement strategies to manage market perceptions and integration risks effectively. Comprehensive communication with investors, transparent reporting and proactive risk management can help mitigate some of the adverse effects of stock-financed M&A transactions.

#### 4.2 Univariate analysis

The univariate analysis' goal is to interpret the relationship between payment methods and returns. This analysis aims to detect short-run value creation capacities for the acquiring firms during and after acquisitions. Table 2 shows the univariate analysis on the method of payment across the sample period (2007–2019) and summarizes the return patterns of sample acquiring firms across the three selected event windows. The average daily returns for the  $-3/+3$ ,  $-5/+5$  and  $-30/+7$  event windows are 0.30%, 0.22% and 0.10%, respectively. As seen in Table 2, the daily returns increased as the event window gets closer to the announcement date. This result is supported by Guven (2020) and Carvalho and Camargos (2013).

**Table 2.** Univariate analysis of the method of payment

Univariate analysis (2007–2019)				
Event window	Multiple R		R square	Adj. R square
-3/+3	0.02967		0.00088	-0.00417
-5/+5	0.02429		0.00059	-0.00446
-30/7	0.02766		0.00077	-0.00428
	Coefficients	Standard error	t-stat	p-value
-3/+3	-0.093200	0.223142	-0.417673	0.676639
-5/+5	-0.108895	0.318526	-0.341871	0.732811
-30/7	-0.00734	1.05897	-0.00693	0.99448
<i>Event window</i>	-3/+3	-5/+5	-30/7	
Average CAR (%)	-0.85	-0.82	-0.97	
Daily returns (%)	0.30	0.22	0.10	

**Source:** Authors' compilation (2023)

To test for the significance of payment method on M&A performance, we analysed the sample data using *t*-statistics. Our findings indicate that payment method is not significant across the three event windows: *t*-test values of -0.417673 (for -3 to +3 days), -0.341871 (for -5 to +5 days) and -0.00693 (for -30 to +7 days), all at the 5% significance level. This aligns with prior studies by [Yuan et al. \(2015\)](#) and [Huang and Walking \(1987\)](#), and leads to the rejection of *H2*, which posited that the choice of payment method affects short-term shareholder value in M&A transactions.

### 4.3 Multivariate analysis

The multivariate analysis explores the multinomial relationship of payment method in M&A, industry diversification, countries of target (domestic and cross-border) and nature of target (private or public).

From the analysis in [Table 3](#), the regression results are not significant at 5% for target listing, diversification, cross-border and method of payment (*t*-stat = 0.223261, -0.75014, 0.862044 and -0.34373) respectively. This is compatible with [Magnusson and Lindberg's \(2013\)](#) empirical results.

**Table 3.** Multivariate analysis of the method of payment

Multivariate analysis (2007–2019)				
Event window	Multiple R		R square	Adj. R square
-30/+7	0.091998		0.008464	-0.011876
Variables	Coefficients	Standard error	t-stat	p-value
Intercept	-0.04574	1.217162	-0.03758	0.970064
Target (public or private)	0.291147	1.304066	0.223261	0.823566
Diversification	-0.5963	0.794919	-0.75014	0.454075
Cross-border	0.683814	0.793247	0.862044	0.389722
Method of payment	-0.40351	1.173903	-0.34373	0.731418

**Source:** Authors' compilation (2023)

4.4 Return pattern around the -30/+7 event window

Figure 1 shows the average CAR and average daily returns of all sample stocks ( $n = 200$ ) between -30 and 7 trading days with the event day (0).

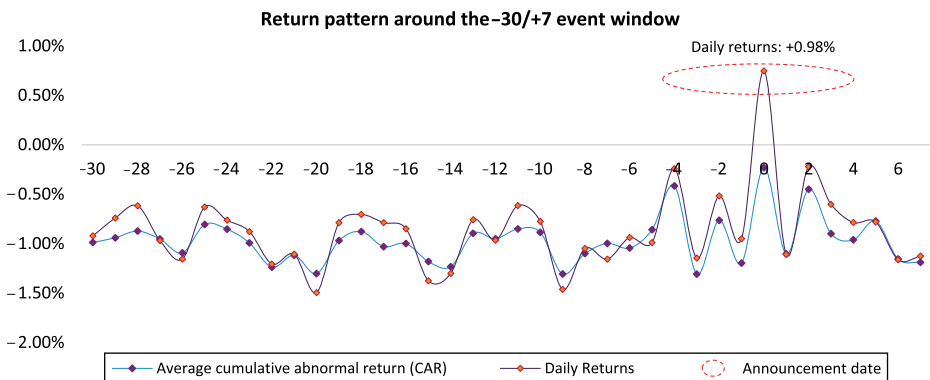
As illustrated in Figure 1, the announcement of an M&A transaction positively impacts shareholder value for acquiring firms. This finding supports *H1*. “The announcement of an M&A transaction will increase shareholder value of the acquiring firm in the short-term” and aligns with the research conducted by Dutta *et al.* (2013), Carvalho and Camargos (2013) and Magnusson and Lindberg (2013). On the announcement date (Day 0), the average daily return was +0.98%, representing the sole positive daily return observed across the event window.

Prior to the announcement date, the average cumulative abnormal rate recorded negative returns, averaging -1%. The announcement of the transaction saw a 297% increase in daily returns between the event day (0) and the day before (-1). A possible explanation for the increase is that during the announcement, the market reacts positively expressing potential in the transaction due to limited information. From the following day, the market adjusts gradually based on the availability of information. This leads to the fluctuations of returns, averaging +0.11% between Days 1 and 7.

4.5 Analysis of deal-specific characteristics

The study sample deals comprise 200 acquisitions made by publicly listed and private UK firms between 2007 and 2019. “Value of deal” is the total transaction value in British Pounds. “Market capitalization” is the value of acquirer before the announcement of the merger. “Relative deal size” is calculated as deal value divided by the acquiring firm’s market capitalization before merger. “Method of Payment” is a categorical variable dividing the sample data into deals funded by “stock only”, “cash only” or a “mix of both”. “Domestic/Cross-border” is a design variable representing the location of the target firms (i.e. within or outside the UK).

Based on the findings presented in Table 4, there is a significant preference for funding acquisitions of target firms using cash, regardless of the target’s location. Approximately 87% of the sampled transactions are entirely financed by cash, with around 4% financed



Source: Authors Compilation (2023)

Figure 1. Return pattern around the -30/+7 event window

solely by stock. This result is corroborated by [Eckbo et al. \(2018\)](#) and [De Bodt et al. \(2018\)](#), who noted that cash accounted for 70% of annual transaction financing between 2000 and 2014, with the remaining 30% involving stock and mixed methods combining cash and equity. These results refute *H3*, which posited that stock financing is preferable than other payment methods in M&A transactions.

The empirical results are in consonance across the different analyses. We also noted the absence of statistical significance between payment methods and acquiring firms' returns. This is consistent with [Yuan et al. \(2015\)](#) and [Huang and Walking \(1987\)](#). This result, however, disagrees with [Savor and Lu \(2009\)](#) and [Moeller et al. \(2004\)](#) who highlighted that the mean stock price reactions for acquiring firms during the M&A announcement are negative and statistically significant when the payment method is mixed or stock but positive and statistically insignificant when the payment method is cash.

The empirical analysis also shows a positive impact in shareholder's value on a short-term basis, which is congruous with [Dutta et al. \(2013\)](#) and [Magnusson and Lindberg \(2013\)](#). The average CAR for the three event windows (-3/+3, -5/+5 and -30/+7) aligns with the expected distribution patterns explained by [Brown and Warner \(1985\)](#).

**Table 4.** Deal-specific characteristics of sample data between 2007 and 2019

Characteristics	Criteria	No.	%
Value of deal (£)	Less than 10 m	60	30
	10m to 100 m	102	51
	100m to 500 m	28	14
	More than 500 m	10	5
Market capitalization (£)	Less than 100 m	27	14
	100m to 500 m	68	34
	500m to 1000 m	31	16
	More than 1000 m	74	37
Relative deal size	Less than 10	136	68
	10 to 30	48	24
	More than 30	16	8
Deal form	Acquisitions	133	67
	Merger	63	30
	Buyback	3	2
	Exchange offer	1	1
Method of payment	Cash	173	87
	Stock	8	4
	Mix of both	19	9
Target location	Domestic	111	56
	Cross-border	89	44
Domestic payment method	Cash	93	84
	Stock	6	11
	Mix of both	12	5
Cross-border payment method	Cash	80	90
	Stock	2	2
	Mix of both	7	8

**Source:** Authors' compilation (2023)

Finally, the multivariate analysis indicates that deal characteristics such as cross-border acquisitions, diversification and target listing are statistically insignificant with the payment method used in M&A transactions, in consonance with [Tanna and Yousef \(2019\)](#).

## 5. Conclusion, limitations and recommendations

While M&A drive corporate investment and restructuring, propelling a multi-billion-pound industry, their success rate often falls short of expectations. Despite anticipated synergies, many M&As underperform, prompting extensive research into the contributing factors. This existing body of literature explored the complexities of M&A success and unravels the intricate causes of failure. This paper examined more closely major acquisitions led by UK companies concluded between 2007 and 2019, exploring their impact and dynamics within the domestic business landscape. This analysis leverages 200 unique acquisitions, each characterized by detailed information such as market capitalization, payment method, deal value, structure, target company location and announcement date. The analysis used descriptive statistics, univariate and multivariate analyses as well as deal-specific characteristics. Each transaction covers company return and market return for a period of 221 days (-200/+20). The three event windows selected for the empirical analysis are -3/+3, -5/+5 and -30/+7.

The study suggests five practical implications and recommendations. These practical implications are substantial for M&A strategies and decision-making processes. Firstly, the observed preference for cash financing suggests that firms might achieve better short-term returns through cash transactions, regardless of whether the deal is domestic or cross-border. This insight can guide firms in selecting appropriate payment methods to optimize value. Secondly, the lack of significant impact of payment methods on deal characteristics underscores the importance of tailoring payment methods to align with strategic goals rather than adhering to a one-size-fits-all approach. By customizing payment strategies for each transaction, firms can better mitigate risks and enhance value creation.

Thirdly, the study highlights the need for comprehensive due diligence and strategic alignment throughout the M&A process. Decision makers should prioritize thorough assessments of potential synergies and strategic fit to maximize the success of the transaction. This approach not only enhances the likelihood of achieving desired outcomes but also ensures that the acquisition contributes positively to the firm's overall strategic objectives. Additionally, understanding the broader strategic contexts and regulatory landscapes when structuring transactions can facilitate market expansion and value creation. Firms that consider these factors are better positioned to navigate the complexities of M&A transactions and achieve their strategic goals effectively. This informed approach enables goal attainment, such as market expansion or value creation.

Finally, the study recommends that policymakers and researchers should continue to use rigorous empirical analysis frameworks, incorporating descriptive statistics, univariate and multivariate analyses and deal-specific characteristics. By leveraging comprehensive data sets and analytical techniques, policymakers and researchers can gain deeper insights into the drivers and implications of M&A activities, informing evidence-based policy interventions and corporate strategies to promote sustainable economic growth and value creation.

Despite the unique contributions emanating from the study, the study acknowledges the potential limitation of a smaller-than-ideal sample size. Despite the size of M&A deals in the UK, our focus on publicly traded firms restricts our results, potentially influencing the generalizability of the findings. Also, we were unable to test the impact of payment methods on M&A transactions of multiple developed economies as this study solely focused on the UK as a case study. Including a comparative analysis across different regions and markets

could provide more robust understanding of payment method impact on M&A transactions as well as enhance the generalizability of findings. Future studies should consider including a greater amount of study on emerging and under-developed economies.

Conclusively, this paper has not examined the long-term impact of M&A transactions on shareholder value. While our analysis provides valuable insights into short-term outcomes and immediate market reactions, it does not address how shareholders' values are being influenced over a long-time frame. Understanding long-term implications is crucial for comprehending the success and sustainability of M&A transactions. Future research should consider focusing on longitudinal studies that track shareholder value over several years post-acquisition.

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#### Further reading

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#### Corresponding author

Akindele Babatunde Omotesho can be contacted at: [akin.omotesho@gmail.com](mailto:akin.omotesho@gmail.com)