Valuation Effect of Institutional Ownership: The Case of Corporate Takeovers

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February 2005

ABSTRACT

We examine the relation between institutional ownership in acquiring firms and their post takeover stock performance. We find that negative long-run abnormal returns appear to decline (in economic and statistical terms) as the extent and persistence of institutional ownership increase, after accounting for the size, book-to-market and method of payment effects. Given the unusually high uncertainty surrounding takeovers, such evidence implies that the degree of short sale constraints serves as an important determinant of acquiring firms’ short-run overpricing (Miller, 1977). It appears that the presence of institutions mitigates and in most cases eliminates, through effective arbitrage, any short-run overpricing that may be responsible for the long-run underperformance of acquirers, preserving in this way efficiency in the takeover markets.

JEL classification: G14; G20; G34.

Keywords: Institutional Ownership; Corporate Takeovers; Mergers and Acquisitions; Short Sale Constraints; Abnormal Returns.

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We would like to thank Abhay Abhyankar, Phil Arbour, John Doukas, Dimitris Petmezas, and seminar participants at the 2004 French Finance Association (AFFI) Meeting and Durham Business School for comments on previous drafts of this paper.

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