

DOES REPUTATION MATTER? EVIDENCE FROM CROSS-BORDER M&AS

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## **Abstract**

Better firm reputation could lead acquirers to pay a premium for the target. Using a cross-country sample between 2007 and 2017, we examine how firm environmental, social, and governance related reputational risk affects acquisition premiums in cross-border mergers and acquisitions. We find that targets with worse reputations tend to have lower acquisition premiums in cross-border deals, and this relation remains robust after controlling for characteristics affecting the investment environment. Additionally, the difference in reputational risk between target and acquirer matters, and the acquirer is likely to pay less for a target that has a worse reputation than acquirer itself. In particular, we construct a signal-country analysis based on U.S. targets to further examine this transfer effect in the reputational capital and find a consistent negative association between the difference in reputational risk and acquisition premium. These results suggest that target's social performance is an important determinant of the merger performance, and they support the signaling theory that a firm's reputation could send a signal about its overall quality.

**Key Words:** reputational risk, cross-border acquisition premium, signaling theory.

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## Chapter 1: Introduction

Widespread literature that studies how corporate social responsibility (CSR) can influence a firm's success tends to focus on the meaning of responsible behaviors, rather than on the meaning of irresponsible behaviors. Previous studies, however, have demonstrated a significant influence from corporate social irresponsibility (CSI), arguing that companies acting in the socially irresponsible manner can bring negative consequences for themselves such as losing current and potential customers and investors (Elsbach & Sutton, 1992; Fombrun, 1996). According to a survey early this year, over 1,000 of top international companies report their greenhouse gas emissions and their emissions-reduction targets for next year's operations<sup>1</sup>. This reduction-wave suggests an increasing concern about reducing a company's CSI, indicating that the decrease in irresponsible behaviors could benefit firm value.

Environmental, social and governance (ESG) are three key criteria in measuring the sustainability and social impact of an investment, which have been widely used in CSR/CSI studies. In one of the initial studies on CSR, Carroll (1979) presented a model for testing firm's corporate social performance based on economic, legal and ethical responsibilities, where environmental issues were embedded in the economic and legal dimensions. Since then, the ESG issues have been widely discussed in CSR research (Gillan et al., 2010; Jo & Ma, 2012; Halbritter & Dorfleitner, 2015; Garciaa et al., 2017). Likewise, many researchers also examine the firm's irresponsible behaviors in the ESG domains (Oikonomou et al., 2012; Kölbel et al., 2017). As CSR's negative counterpart, CSI is conceptualized by stakeholder theory as an opposite force to CSR because of its negative impact on firm performance, including sales revenue losses, increased financial risks and capital costs (Lange & Washburn, 2012; Oikonomou, Brooks, & Pavelin, 2012). Moreover, as implied by the ratings from the KLD dataset, which have been used as the proxy for a firm's social performance by lots of CSR-related literature, firms can be simultaneously socially responsible and irresponsible. Regardless of that, many CSR studies have combined CSR and CSI into one single concept by using this dataset, failing to differentiate CSR from CSI (Strike et al., 2006; Lange & Washburn, 2012). Therefore, our focus is on how the firm's social irresponsibility could influence firm value and its financial performance.

Given the association between CSR and CSI, it is worth understanding how CSR affects firm value to further investigate the influence of CSI, and there has been a growing concern about

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<sup>1</sup> <https://www.greenbiz.com/article/how-get-suppliers-act-climate>

whether CSR would benefit firm value or not in the context of the acquisition premium. In M&As, acquirers typically face information asymmetry as targets often hide negative information about themselves. To help solve this problem, acquirers must use signals available to get additional information about targets' quality (Connelly et al., 2011). Meanwhile, targets have the intention to send out positive signals about themselves for a higher purchase price (Reuer et al., 2012). Literature has shown that CSR could convey those signals to mitigate the information asymmetry. Based on the work conducted by Fisman et al. (2006) that good CSR can act as a credible signal of firm trustworthiness in providing high-quality products, Lagas (2013) argues that targets with better CSR are likely to be taken over at higher premiums, suggesting that the target's CSR could be a powerful positive signal in M&As. Using U.S. public merger and acquisition deals from 1992 to 2013, Malik (2014) finds that the acquisition premium increases with target's CSR, and this association is stronger for high-CSR acquirers compared with low-CSR acquirers. Likewise, Choi et al. (2015) construct a sample of 215 cash-only U.S. acquisitions between 1995 and 2013 and report similar findings.

Instead of analyzing how a firm "doing good" could benefit its value, in this paper, we focus on how a firm "doing bad" could hurt its value, which is its socially irresponsible behaviors. Meanwhile, with the increasing complexity in cross-border M&As, international deals face more severe information asymmetry and riskier misvaluation compared with domestic activities. Therefore, we construct a sample of cross-border M&As announced between the period of 2007 and 2017 to examine the relationship between a firm's reputational risk and the cross-border acquisition premium. Many studies on the acquisition premium have applied signaling theory (Laamanen, 2007; Reuer et al., 2012; Schijven & Hitt, 2012), and our perspective is that the acquirer is willing to pay a premium for a target with a better reputation as it sends a positive signal about the target's quality. Although it is difficult to empirically measure a firm's reputation, we measure the reputational risk of ESG issues as the second-best solution. Thus, we collect the RepRisk data (RRI index), a proprietary algorithm developed by the RepRisk dataset that dynamically captures and quantifies a firm's reputational risk exposure related to ESG issues on a monthly basis since January 2007, and Peak RepRisk data (RRIP index), which equals the highest level of the RRI index over the last two years, as the proxy for the target's and acquirer's reputational risk. The RepRisk platform systematically screens thousands of information sources and collects negative news, controversies, and criticism about companies worldwide, including



activities that violate human rights, destruct environment and involve poor working conditions. Then, it uses a unique methodology to quantify a company's exposure to controversial ESG issues based on the severity of the content, the authority of the information sources and the frequency of the information (Cui et al., 2018).

The acquisition premium data is from Securities Data Corporation (SDC) database, which is the bid price as a percentage of the closing price of the target four weeks before the announcement. Our empirical results show that, the target with a better reputation is associated with a higher acquisition premium in cross-border deals, indicating that the signal associated with target's reputation plays a significant role in mitigating information asymmetry and, therefore, affects the acquisition premium. Additionally, we find that the difference in reputational risk between target and acquirer is significantly and negatively associated with the cross-border acquisition premium, even after controlling for firm level, deal level, and country level characteristics, which suggests a potential transfer effect in the reputational capital after the acquisition.

Our cross-country analysis, however, has some limitations as it is hard to control for the differences in the same industry across countries. Therefore, we conduct a single country study based on U.S. domestic and cross-border M&As to further examine the target reputation transferability. Again, we find a significantly negative relation between the difference in the reputational risk and the acquisition premium. The results support the idea that the acquirer is willing to pay more for a target that has a better reputation than itself.

Additionally, we further examine the impact of different investment environment on cross-border M&A premiums by controlling for the investment environment characteristics since cross-border acquisition premiums vary across countries due to this difference. The empirical results provide evidence that the negative association between firm's reputational risk and acquisition premium holds after controlling for investor protection, judicial efficiency, and accounting standards, and the investment environment indices are significantly and positively associated with acquisition premium in international M&As after controlling for firm/deal/country level characteristics.

Our paper belongs to the growing literature explaining the cross-country variation in social performances around the world. Recent studies show that better CSR is associated with better acquisition performances and higher acquisition premiums in both cross-border and domestic deals (Malik, 2014; Choi et al., 2015; Gomes & Marsat, 2017). Our study, instead, analyzes how a firm

doing irresponsibly destroys its value by focusing on its negative ESG issues. The results indicate that firm's worse ESG performance is associated with a lower premium in cross-border mergers and acquisitions.

The organization of the paper is as follows. Section 2 presents different arguments that link firm reputation to acquisition premium in cross-border M&As. Section 3 illustrates our data, methodology, and the empirical design. The empirical results are presented in Section 4. Section 5 summarizes and concludes.

## **Chapter 2: Literature Review and Hypotheses Development**

In M&A transactions, especially cross-border deals, acquirers typically have incomplete information about the target, making it harder for them to evaluate the company. To alleviate this problem, it is essential for acquirers to use signals available to get extra information about the target's quality. Given the importance of signals, many studies on acquisition premium have applied signaling theory.

### **2.1 Literature Review**

#### **2.1.1 Signaling theory and firm reputation**

Signaling theory is essentially concerned about examining the information asymmetry between the two parties. Spence's (1973) preliminary work on job market signaling illustrates that high-quality applicants can distinguish themselves from low-quality applicants through the observable and costly signal of higher education if this education is positively related to the unobservable productivity.

This work triggered a large amount of research applying signaling theory to selection scenarios, many of which have focused on how corporate social responsibility (CSR) could convey signals about one firm's quality. From capital benefits, Goss & Roberts (2011) examine the relationship between CSR and bank debt based on 3996 loans to U.S. firms and find that socially responsible firms pay less than firms that are less responsible, indicating a lower cost of debt for firms with better social responsibility. Likewise, Ye & Zhang (2011), using a sample of Chinese firms from 2007 to 2008, also find that improved corporate social responsibility reduces a firm's debt financing costs. Richardson et al. (2001) and Dhaliwal et al. (2011), on the other hand, demonstrate a negative relation between CSR and the cost of equity capital. From ethical theory's perspective, Chih, Shen & Kang (2008) conduct a cross-country study and illustrate that a greater committee

to CSR can help reduce earning smoothing and earnings losses avoidance. Kim et al. (2012) also demonstrate that firms are less likely to manipulate real operating activities and manage earnings through accruals when they are more socially responsible. Overall, CSR conveys information about a firm's quality and sends a positive signal to all stakeholders of its reputation (Linthicum et al., 2010).

As most studies examine how a firm being socially responsible sends a positive signal about its overall quality, our research focuses on the negative influence of a firm's irresponsible behaviors. Similar to the positive influences from socially responsible behaviors, negative effects from socially irresponsible manners, such as environmental destruction or poor labor conditions, may threaten the firm's social license to operate, and further worry investors about its future growth. A growing body of literature documents that irresponsible behaviors could detract from the firm value (Luo & Bhattacharya, 2009; Jo & Na, 2012; Gregory et al., 2014). Also, existing analyses investigating stakeholders' and consumers' reactions to socially irresponsible behaviors, including moral outrage and righteous anger, demonstrate that those negative feelings can create negative company image (Lindenmeier et al., 2012; Grappi et al., 2013b) and motivate consumer boycott (Braunsberger and Buckler 2011; Cronin et al. 2012) and negative attitudes toward the company (Grappi et al., 2013a, b). Overall, a corporation will lose trust and social legitimacy if it is seen as being irresponsible (Price & Sun, 2017).

Compared with company's "good" behaviors, "bad" behaviors, however, seem to bring more dramatic and negative influences to the firm value. The stock market has seemed to be relatively more sensitive to bad news than to good news as behavioral psychology suggests that a bad shock can correct the market's over-optimism. For example, in the UK stock market, the stock prices of many stocks continued to decline significantly after reporting bad news<sup>2</sup>. Veronesi (1999) introduces a dynamic equilibrium model to examine how the stock market reacts differently to good news and bad news. Using the equilibrium price function, he demonstrates that the stock market overreacts to bad news in good times, which is further developed by Conrad et al. (2002). Their study, based on a sample of annual earnings announcements between 1988 and 1998, confirms that the stock price of individual firms responds more dramatically to bad news in good times, and the level of response rises with the market level. They argue that, compared with good news, which is already anticipated by the market, the bad news is more surprising, leading to a

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<sup>2</sup> <https://www.sharesmagazine.co.uk/article/is-the-stock-market-over-reacting-to-bad-news-with-large-share-price-declines>

larger negative stock return. Therefore, consistent with previous work, our perspective is that when a firm acts irresponsibly and is criticized by the media, its firm value will be hurt more strongly than the benefits that good behaviors could bring to it.

Regarding the firm's irresponsible manners, the media can influence the reputational capital of firms by generating public scrutiny to discipline firms' actions (Baloria et al., 2018). Therefore, our study measures a firm's reputational risk based on the RepRisk data. Launched in 2007, the RepRisk ESG Platform monitors the environmental, social and corporate governance (ESG) risk exposure of companies worldwide by systematically capturing negative incidents, criticism and controversies on a daily basis from over 80,000 media, stakeholders and third-party sources, including all major print and online media, NGOs, regulators, news sites, governmental agencies and social media<sup>3</sup>. The data collected, covering 28 ESG issues, such as activities involve human rights violations, poor working conditions, corruption, and environmental destruction, is then used to calculate the ESG-related reputational risk exposure score, RepRisk Index (RRI), which is considered an indicator of one firm's reputational risk (Cui et al., 2018).

Considering the importance of the reputational capital, Gloßne (2017) investigates the relationship between the ESG risk exposure and long-run stock return of firms located in the U.S. and Europe based on the RepRisk data from 2009 to 2016, and finds that value-weighted portfolios of U.S. firms and European firms that have ESG issue history face significant negative abnormal stock return. He explains that firms with higher ESG risks usually have weaker operating performances and more negative earnings surprises. Therefore, they experience more negative earnings announcement returns than other competitors. Li & Wu (2017) also use the RepRisk data to measure the ESG impact for public and private firms globally between 2007 and 2015 to examine whether CSR engagements could generate real societal benefits. Their findings show that private firms can reduce the negative influence from their ESG controversies by increasing their CSR engagements. In general, reputational capital is an important intangible asset, through which firms can signal their key characteristics to stakeholders (Fombrun & Shanley, 1990), and the increase in ESG incident issues could signal more serious problems about one firm.

### **2.1.2 Cross-border acquisition premium**

The quick development of globalization has dramatically increased the volume of cross-border M&A deals. In 1997, there were only about 2,000 cross-border M&A deals, worth

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<sup>3</sup> <https://www.reprisk.com/our-approach>

approximately \$163 billion, while in 2017, the international M&A market reported \$1.17 trillion in value.

The booming M&A market has received considerable attention from researchers, but comparatively less literature has investigated in the cross-border acquisition premium. The widely used definition of acquisition premium suggests that premium is an overpayment for acquirers as it consumes the expected synergies that would be achieved after the transaction (Sirower, 1997). Acquirers, however, continue to pay approximately 20-30 percent of the total transaction value as the premium (Laamanen, 2007). For example, the premium that paid by U.S firms is on average 30% to 50% of the target market values during the past three decades (Hayward & Hambrick, 1997). To find out the characteristics of cross-border acquisition premium, Rossi & Volpin (2004) conduct a cross-country analysis on international M&A deals by examining the differences in laws and regulations across countries. Their results show that premium is higher in countries with higher shareholder protection, although those are driven by the U.S. and UK firms. There are two reasons for the positive relation between the acquisition premium and shareholder protection. Firstly, the cost of capital is relatively reduced in those countries. Secondly, diffuse ownership is more common for countries with higher shareholder protection, leading to the free-rider problem during the acquisition, which forces bidders in those countries to pay a higher premium than otherwise (Grossman & Hart, 1980). Also, to test whether premium measures the private benefits of control, they include the difference in shareholder protection between acquirer and target and find insignificant results, suggesting that premium is a proxy for the total premium available to all shareholders, not for personal gains. This insignificant result also indicates that there is no much difference in premiums between acquires from countries with better shareholder protection and acquirers from countries with worse shareholder protection.

According to a survey conducted by McKinsey, institutional investors are willing to pay more for companies with better corporate governance, and the level of premium varies across countries (Newell & Wilson, 2002). Consistent with this result, Starks & Wei (2013), using 371 cross-border mergers of U.S. targets between 1980 and 1998, find a significantly negative relation between the acquisition premium and the quality of the foreign acquirer's governance for stock deals. They argue that this is because acquirers want to compensate target shareholders for the future exposure to inferior corporate governance. Interestingly, the key assumption of their findings is that the U.S. firms have superior corporate governance practices than other countries,

which corresponds to the U.S./UK driving factor concluded by Rossi & Volpin (2004) to some extent.

With the upward trend in M&As, the use of investment bankers in acquisitions has increased simultaneously. Between 1981 and 2002, the use of investment banks in M&As increased from 78% in 1981 to 88% in 1999 (Porrini, 2006). In 2007, when the M&A market experienced the most recent peak, 85% of these deals were advised by investment banks, generating about \$39.7 billion in advisory fees<sup>4</sup>. This calls attention to the question of whether hiring investment banks could benefit the firm or not during the M&A negotiation process and leads to different empirical discussions. With their advisory roles, investment banks are expected to help negotiate acquisition premiums (Eccles and Crane, 1988; Haunschild, 1994). As the acquisition premium is the difference between the estimated firm value and the actual price paid to acquire the target, any premium that is more than what the acquirer needs to pay to secure the deal should be considered too much if the markets are efficient with no information asymmetry. Through investment banks' expert knowledge and skills, they can affect the acquisition premiums during the acquisition process. Targets hire advisors to get a higher premium while acquirers hire bankers to negotiate for a lower premium. However, due to the contingent fee structure, acquirers' investment bankers could be motivated to increase acquisition premium for self-interest, which might mislead acquirers to end up paying beyond the reasonable amount. Therefore, there is a potential interest conflict between the acquirers and their investment bankers. Considering this dilemma, prior studies have questioned the role of advisories on acquisition premium, demonstrating that contingent contracts create conflicts of interest between the investment bank and the firm (McLaughlin, 1990; Kesner et al., 1994).

### **2.1.3 Signaling theory in cross-border acquisition premium**

Due to the information asymmetry between the target and acquirer, both parties are motivated to use signals available to maximize their profits. On the one hand, acquirers must use signals that could provide additional information about the target to avoid mispricing the deal (Connelly et al., 2011). On the other hand, targets are likely to send out positive signals to maximize its purchase price (Akerlof, 1970; Reuer et al., 2012). Therefore, several M&A studies focus on signaling theory with its implications of being able to reduce information asymmetries. Based on U.S. domestic acquisitions, Laamanen (2007) finds that R&D capitals and R&D growth

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<sup>4</sup> Source: Thomson Financial SDC.

rates could be signals about a technology-based target's prospect that can be detected by acquirers. He reports a significant positive relation between acquisition premium and R&D capitals/growth rates. Additionally, he finds that there is a significant negative association between acquisition premium and target's market-to-book ratio, the reason being that targets whose market values are significantly above their book values are believed to be overvalued, which are less likely to gain additional growth that an acquirer can realistically expect after the acquisition. Therefore, the premium is lower. Reuer et al. (2012), instead, look at this problem from the point of view of a target's interrelationship with others, and suggest that acquirers are willing to pay more for an IPO target affiliated with prominent underwriters, venture capitalists, and alliance partners.

As one of the firms' most important intangible assets, reputational capital has been considered helpful in reducing information asymmetry (Cui et al., 2018) as it can signal additional information about firms to avoid adverse selection, and theories suggest that spending on CSR may help improve corporate reputation (Brown & Dacin, 1997). Therefore, a firm's CSR has become a tool to determine reputable companies (Aksak et al., 2016). By testing the relationship between the acquisition premium and target's social performance based on a sample of U.S. domestic acquisitions, Malik (2014) and Choi et al. (2015) find that there is a positive relation between the premium paid by acquirers and targets' CSR, indicating that the information on a target's CSR rating scores can send a positive signal about the target firm. Inspired by their work, Gomes and Marsat (2017), using the data provided by Thomson Reuters ASSET4 as the proxy for firm's CSR, examine the impact of CSR performance in the context of cross-border acquisition premium, and demonstrate that targets' CSR performance is positively associated with the acquisition premiums, consistent with previous literature.

## **2.2 Hypothesis Development**

Following the literature review, it should be clear that cross-border M&A involves additional complexity and risks due to the differences in culture, investment environment and regulations. However, in a similar vein, cross-border deals feature similar, or even more severe information asymmetries as acquirers need to navigate the differences in corporate governance, cultures, languages and accounting standards, as well as the hindrance of geographic distance (Ellis et al., 2011; Ahern et al., 2011; Erel et al., 2012). These factors make it more difficult for acquirers to accurately estimate the value and risks of the targets in cross-border transactions. Hence, acquirers involved in international deals should be more motivated to grasp available signals for additional

information, and target's reputational risk is one of the factors that we believe could affect target's valuation and attractiveness, which should be observed in the form of the acquisition premium.

This signaling effect from a firm's reputation, however, could influence the firm's stock price in both positive and negative ways. Due to the bad brand image, it is possible that one firm's stock price might suffer significant drop when some serious incidents happen, leading to the increase in the acquisition premium as the stock price is in the denominator when calculating the acquisition premium. Our perspective is that, the decrease in the stock price can't compensate for the more dramatic decrease in the estimated firm value after the severe controversies, suggesting a negative association between the reputational risk and the acquisition premium. Companies that seek mergers and acquisitions are motivated by the synergies expected after the transaction, and corporate reputation could serve as a transferable synergy-enhancing asset (Brandtzæg, 2014). Therefore, targets with higher reputational risks are expected to provide lower reputational synergies after the acquisition, decreasing the valuation of the targets. Bendixen, Bukasa & Abratt (2004), for example, demonstrate that high brand equity could yield a price premium. Therefore, we formally state our prediction in the following hypothesis:

*H1: Target's reputational risk is negatively associated with the acquisition premium in cross-border M&As.*

Additionally, it is worth noting that if targets have less reputational risk than acquirers themselves, it is likely that acquirers are willing to pay more for those targets as a way to improve their corporate brand image after the transaction. This reputation transferability is more critical in international deals as the foreign acquirer can benefit from the good reputation and existing customers of the local target, mitigating the uncertainty caused by the differences in culture, legal system and corporate governance. Accordingly, the transfer of good reputation from the target could result in a more favorable attitude from local consumers toward a cross-border acquisition (Fong et al., 2013). Using a sample of 124 acquiring companies in 29 countries, Barua (2017) suggests that acquirers should take target's corporate reputation into consideration since this can lead to a high degree of corporate brand architecture, which in return will increase acquirer's market share, sales growth, and profitability after the transaction, resulting a relatively higher premium for targets with a better reputation. Another possible reason is that, for targets, it might be more efficient for them to be acquired by other better firms than to try to fix their existing problems alone. In this case, the targets are willing to accept a lower purchase price as an exchange



for the financial support from acquirers with better reputation after the transaction. Thus, we propose the following hypothesis:

*H2: The difference between the target's reputational risk and acquirer's reputational risk is negatively associated with the acquisition premium in cross-border M&As.*

## **Chapter 3: Data Description**

### **3.1 Data Selection**

Our sample contains cross-border mergers and acquisitions announced between January 1st, 2007 and December 31st, 2017, completed as of February 1st, 2018, and reported by SDC Platinum, a database from Thomson Financial. The sample period is limited by the availability of our data from the RepRisk dataset for measuring a firm's reputational risk as RepRisk's data history spans back to January 2007. Since we focus on the target that could clearly and completely affect its acquirer through its reputation, we only include acquisitions when acquirers obtain 100% of targets' shares after the transaction. The sample excludes firms in the utilities and financial sectors, consistent with prior studies because of the historically regulated nature of the two industries as well as the dramatic regulatory changes that occurred during our sample period (for example, the regulatory responses to the subprime crisis in 2009). Moreover, financial firms are typically highly leveraged, which do not have the same meanings as for non-financial firms. Therefore, we exclude those firms to ensure that skewed financial fundamentals do not drive our results.

The availability of empirical measures of firm reputational risk from the RepRisk dataset limits our set to 36 countries. The preliminary sample from SDC includes 770 deals, and the excluded deals represent about 72% of the original dataset in number and 27% in value.

Appendix describes the variables we use in this paper and specifies their sources. These variables can be classified into three broad categories. The first set is at the country level, including a dummy for the legal origin of each country and proxies for investment environment. The second category measures characteristics at the individual deal level, such as the premium paid, the means of payment, the number of advisors involved in the transaction, and the transaction volume, etc. Our third set of variables is at the firm level, and this covers target's industry information and target's size, which is the market capitalization of the target four weeks before the announcement of the deal in US\$ million.

### 3.2 Dependent Variable

Acquisition premium is widely defined by the previous literature as the bid price as a percentage of the closing price of the target four weeks before the announcement (Rau & Vermaelen, 1998; Rossi & Vopin, 2004; Reuer et al., 2012; Qiu et al., 2014). Following Rossi & Vopin (2004)'s work, we use the natural logarithm of premium in percentage as our dependent variable.

Table 3.1 presents all the variables' statistic properties of our sample. The number of cross-border mergers and acquisitions is 219. The mean of the dependent variable,  $\text{Lnpremium4week}$ , is appropriately 3.344 with a standard deviation of 1.109 while the average RRIP for all the target companies is 20.37 with a standard deviation of 17.96. We also include the summary statistics for the premium in percentage, and the mean of it is 42.08% while the standard deviation of it is 41.92. Starks & Wei (2013) report a mean of cross-border premium in percentage as 36.47% and Gomes and Marsat (2017) demonstrate the average cross-border premium in percentage as 32.1%, similar to our results.

In Table 3.2, we sort the data on M&A activity by target country, including the average volume, the average premium paid by acquirers for each country and the percentage of each country's cross-border M&As in value. Obviously, different countries play different roles in the global M&A market. For instance, the U.S. has the highest volume among all the other countries, representing 39.73% in deal number and 52.54% in deal value of the whole sample. Regarding premiums, New Zealand has the highest premium compared with others while target from Switzerland, instead, received the lowest premium in our sample. To eliminate the possible influences from the outliers, we conduct a separate robustness test without countries that have extremely high premiums (New Zealand and Japan) and countries that have extremely low premiums (Switzerland). The results are reported in Table 4.9.

**Table 3.1: Variable Summary Statistics**

This table presents the summary statistics of the major dependent and independent variables. The primary dependent variable, premium is measured by natural logarithm of bid price as a percentage of the closing price of the target four weeks before the announcement. In our regressions, we adjust two of these variables using natural logarithms including: the deal value and the target size.

	<i>MEAN</i>	<i>STDEV</i>	<i>MIN</i>	<i>MEDIAN</i>	<i>MAX</i>	<i>N</i>
<b><i>Premium</i></b>						
<i>Premium4week(percentage)</i>	42.08	41.92	0.22	35.59	510.1	219
<i>Lnpremium4week</i>	3.344	1.109	-1.51	3.54	6.23	219
<b><i>Firm-level Variables</i></b>						
<i>Target RRIP</i>	20.37	17.96	0	25	68	219
<i>Acquirer RRIP</i>	29.12	18.72	0	32	74	176
<i>Difference in RRIP</i>	-9.528	20.31	-69	0	57	176
<i>Horizontal</i>	0.644	0.48	0	1	1	219
<i>Lntargetequity</i>	7.306	1.843	-0.21	7.41	11.54	219
<b><i>Deal-level Variables</i></b>						
<i>Lndv</i>	6.839	2.193	-2.98	7.16	11.53	219
<i>Cashdeal</i>	0.731	0.445	0	1	1	219
<i>Hostile</i>	0.0137	0.117	0	0	1	219
<i>Tender</i>	0.475	0.501	0	0	1	219
<i>Contested</i>	0.0731	0.261	0	0	1	219
<i>Crossborder</i>	0.282	0.451	0	0	1	241
<i>Targetadvisor</i>	1.557	1.062	0	1	7	219
<i>Acquireradvisor</i>	1.712	1.308	0	1	8	219
<b><i>Country-level Variables</i></b>						
<i>Targetlo</i>	0.735	0.442	0	1	1	219
<i>Acquirerlo</i>	0.47	0.5	0	0	1	219
<i>ADRI</i>	4.211	1.231	0	5	5	213
<i>ANTI</i>	3.627	0.868	1	3.5	5	217
<i>Enforcement</i>	9.474	1.128	5	10	10	213
<i>Accounting</i>	69.41	11.31	0	71	83	213

**Table 3.2: Observation and Average Premium by Country**

Summary statistics on the sample of individual cross-border M&A deals sorted by target country announced between January 1<sup>st</sup>, 2007 and December 31<sup>st</sup>, 2017. Premium is natural logarithm of the bid price as a percentage of the closing price of the target four weeks before the announcement.

Country	Deal Value				Premium	
	Number of Deals	Numbers (%)	Mean	Proportion (%)	Mean	Std. Dev
Australia	12	5.48	1210.45	1.46	3.62	0.87
Austria	1	0.46	1756.99	0.18	1.79	0.00
Belgium	3	1.37	4705.95	1.42	1.86	1.81
Bermuda	1	0.46	3017.31	0.30	4.12	0.00
Brazil	5	2.28	2110.39	1.06	3.24	0.63
Canada	11	5.02	2071.64	2.28	3.36	1.75
China	1	0.46	843.27	0.08	3.11	0.00
Colombia	1	0.46	13.79	0.00	0.10	0.00
Denmark	2	0.91	3610.56	0.72	3.19	0.95
Finland	4	1.83	793.21	0.32	2.14	2.48
France	9	4.11	785.96	0.71	3.13	1.11
Germany	7	3.20	779.97	0.55	3.07	1.01
Gibraltar	1	0.46	1623.55	0.16	4.16	0.00
Greece	2	0.91	190.36	0.04	1.92	1.42
Hong Kong	4	1.83	6522.25	2.62	3.54	0.41
India	2	0.91	194.22	0.04	3.79	0.77
Ireland-Rep	2	0.91	27095.30	5.43	3.16	0.41
Israel	3	1.37	5517.37	1.66	3.79	0.53
Italy	2	0.91	733.08	0.15	1.83	1.98
Japan	2	0.91	2843.43	0.57	4.72	0.17
Netherlands	4	1.83	6555.96	2.63	2.91	0.70
New Zealand	1	0.46	608.94	0.06	4.76	0.00
Nigeria	1	0.46	124.10	0.01	3.54	0.00
Norway	5	2.28	469.74	0.24	2.88	2.03
Pakistan	1	0.46	329.74	0.03	0.76	0.00
Poland	2	0.91	6.74	0.00	2.81	1.57
Russian Fed	1	0.46	1375.67	0.14	4.67	0.00
Singapore	6	2.74	954.93	0.57	3.60	0.57
South Africa	4	1.83	5937.54	2.38	2.89	1.02
Spain	1	0.46	1583.00	0.16	3.43	0.00
Sri Lanka	1	0.46	0.05	0.00	2.22	0.00
Sweden	4	1.83	2200.10	0.88	3.54	0.89
Switzerland	1	0.46	47.56	0.00	-0.53	0.00
Taiwan	1	0.46	202.06	0.02	2.85	0.00
United Kingdom	24	10.96	8552.40	20.58	3.54	0.86
United States	87	39.73	6022.83	52.54	3.57	0.80
Total	219					
World Average			4553.89		3.34	1.11

### 3.3 Test Variable

To measure a firm's reputational risk, we collect our reputational risk exposure score using data from the RepRisk platform, a dataset that focuses on risk-related data for all companies across the world that have been exposed to ESG risks. RepRisk, with the coverage of 28 ESG issues and 45 ESG topics, collects and analyzes negative incidents, criticism, and controversies from thousands of sources on a daily basis. Those collected data is then converted to a monthly-updated score, the RRI index, for each company through a unique methodology. This data is uniquely suitable for our study for two reasons. Firstly, different from KLD database that only focuses on publicly traded U.S. companies, the RepRisk platform provides access to ESG-related reputational risk exposure score for companies from different countries including emerging and frontier markets, helping us to get a broader sample for our cross-country study. Secondly, KLD indices are frequently based on subjective analyst ratings and self-reported documents, which might lead to biased results. The RepRisk dataset, in contrast, uses an approach that allows for a more frequent and objective assessment of ESG impact on each firm over time, giving us a more comprehensive understanding of one firm's reputational risk exposure. More importantly, the data provided by RepRisk look at similar information as KLD database does, which has been widely used for CSR study that monitors a firm's social responsibility. This enables us to relate our study to previous CSR literature for theoretical support and insights. Some literature, such as Gomes and Marsat (2017), uses the rating score provided by Thomson Reuters ASSET4 as the proxy for a firm's social performance. This database is based on data provided by ASSET4, a leading global ESG score provider, and the ratings are derived from 226 Key Performance Indicators. However, as ASSET4 data measure the socially responsible and irresponsible manners through one combined score reflecting the overall social performance of firms, it does not match our major research purpose, which is to concentrate on the influence from socially irresponsible behaviors. Furthermore, ASSET4 is aimed at examining environmental, social and governance dimensions separately, a feature that is not necessary for our study. In addition, both KLD database and ASSET4 database are mainly based on company reports, filings and their websites, which are more likely to be manipulated and biased than sources such as public media, stakeholder, and third-party information where RepRisk collects data from. Therefore, we eventually decide to focus on the RepRisk data.

Two major RepRisk indices have been used in prior literature, the peak RRI index and current RRI index. The peak RepRisk Index (RRIP) is equal to the highest level of the RRI index over the last two years, a proxy for overall ESG and business risk exposure, and is recommended by RepRisk when analyzing and comparing firms along with their ESG risk exposure. Current RRI index, instead, is a monthly-updated data that denotes the current risk level of a company related to its ESG issues. The index ranges from 0 to 100, and a higher number is associated with higher ESG risk exposure. When an ESG issue happens, the index of a firm accordingly increases based on the severity, the reach and the novelty of the issue and the intensity of the news about the firm (Gloßne, 2017). If there is no negative news, the index will decay over time according to some strict rules.

Our study, with the purpose of having a thorough understanding of a firm's ESG risk exposure, focuses on the RRIP index for two reasons. First of all, as one firm's viable and heavily practiced growth strategy, M&A activity requires a significant amount of time for preparation and negotiation, which is more sophisticated in the context of cross-border M&A due to higher information asymmetry and significant country differences. De Beaufort & Lempereur (2003) demonstrate that lack of trustworthy contracts and information exchange between the acquirer and target partially lead to M&A failures in cross-border deals, indicating the importance of understanding the factors that influence effective negotiation process. Ahammad et al. (2016), for example, provide an empirical examination of those factors and find that communication, national cultural distance and organizational cultural differences affect the negotiation process. Due to the uncertainty, the merger decision could be time-consuming. Thus, the current value of one firm's RRI score around the announcement date can't completely describe how this risk exposure affects the M&A transaction during the negotiation process. Secondly, the RRIP index is a proxy for a firm's overall ESG related reputational risk exposure, which is the main metric used in analyzing the risk exposure of a company according to RepRisk's methodology. Therefore, this data perfectly suits our analysis among different companies regarding their ESG risk exposure.

### **3.4 Firm, Country, and Deal Characteristics**

Following Rossi & Volpin (2004)'s work on the determinants of cross-border acquisition premium, we add three different levels of control variables to capture firm differences and cross-country differences.

Firm-level characteristics include the industry difference between target and acquirer, which equals one if they belong to the same industry at the two-digit SIC-code level, and size, which is the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. At the country level, the set of variables include the legal origin of the target country and acquirer country, which is equal to 1 if it is a common law system and zero otherwise. Rossi & Volpin (2004) find a significant positive association between cross-border acquisition premium and shareholder protection of target country. However, due to the lack of data for shareholder protection, we decide to use legal origin at the target country level as the proxy for investor protection instead. Since La Porta et al. (1998) published a study on the effects of legal origin on shareholder protection and found that countries with a common law origin are associated with a higher level of shareholder protection, a lot of studies have invested in this topic and report similar empirical results (La Porta et al., 2008; Fagernas et al., 2009; Acheson et al., 2016). More specifically, Ciobanu (2015) examines how the legal origin of a state can influence M&As through an international M&A sample from 30 different countries, and he finds that the legal system actually impacts the control premium and the overall M&A market.

To further examine the effect of different investment environment on international M&As, we conduct additional analysis by examining the investment environment that is measured by investor protection, accounting standards, and judicial efficiency. Bris and Cabolis (2008), using a sample of 506 acquisitions from 39 target countries, find that acquisition premium is higher for firms from countries with better shareholder protection and accounting standards. They argue that acquirers with a higher accounting standard and shareholder protection are more likely to improve the corporate governance of the targets after the deal, which can help increase the target's value in the long run. Thus, they are willing to pay more for the target. However, due to the highly correlated nature of these variables, putting all variables in one regression might cause estimation problems (Kennedy, 2003). Therefore, we reveal the relationship between the investment environment index and the cross-border acquisition premium by adding one index to our model each time while controlling for other firm-level, country-level and deal-level characteristics in the meantime.

The last category measures characteristics at individual deal level, including the number of target's and acquirer's advisors involved in the transaction, the logarithm of the transaction volume, a dummy variable (cash offer) that equals one if it is a cash deal and zero otherwise, a dummy

variable (hostile bid) that equals one if the deal is hostile and zero otherwise, a dummy variable (tender offer) that equals one if the deal is a tender offer and zero otherwise; and a dummy variable (contested bid) that equals one if the number of bidders is larger than one and zero otherwise. The use of advisors in M&As has been studied by many researchers recently. Through their advisory roles, investment banks can affect the acquisition premiums for both acquirers and targets during the acquisition negotiation process. Since there is a lack of resources to complete deals, targets and acquirers need investment bankers for their professional knowledge and skills. For targets, they hire bankers to get the highest premium while for acquirers, they need bankers to negotiate for the lowest premium during the transaction. However, as bankers' fees are a percentage of the acquisition premium, acquirers' investment bankers may increase acquisition premium to get higher fees. Therefore, there is potential interest conflict between acquirers and investment bankers. Studies have questioned the role of advisories on acquisition transactions, demonstrating that there might be misalignment, and hence conflict of interest between banker and firm due to the contingent contracts (McLaughlin, 1990; Kesner et al., 1994).

## **Chapter 4: Results**

### **4.1 Main Regression**

Table 4.1 presents the Pearson correlation matrix for the variables discussed in the previous section. Consistent with our expectation, the Pearson correlation between the acquisition premium and target RRIP is significantly negative, -0.15. Similarly, the acquisition premium is negatively correlated with the difference in reputational risk between the target and acquirer, -0.27, which confirms our expectation that acquirers are more likely to pay less for targets with a worse reputation than themselves, indicating a potential transfer effect in the intangible asset, that is, reputation building here, after the acquisition.

Deal value, which is the logarithm of the transaction volume, is significantly and positively correlated with acquisition premium, 0.16. Kim & Canina (2013), using a property-level dataset, reports similar significantly positive correlation between deal value and acquisition premium, suggesting that acquisition premium increases with the deal size. Target legal origin, which equals one if it is a common law system and zero if it is a civil law system, is positively and significantly correlated with acquisition premium, 0.3, consistent with the results found by Rossi & Volpin (2004). Interestingly, there is a significantly positive correlation between the use of advisory from



**Table 4.1: Pearson Correlation Matrix**

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	
(1) Lnpremium4week	1																		
(2) Target RRIP	-0.15**	1																	
(3) Difference in RRIP	0.27***	0.53***	1																
(4) Horizontal	0.08	0.04	-0.03	1															
(5) Lntargetequity	0.005	0.1	-0.12	0.13**	1														
(6) Lndv	0.16**	-0.04	-0.22***	0.08	0.9***	1													
(7) Cashdeal	0.07	-0.09	-0.1	-0.11	-0.24***	-0.2***	1												
(8) Hostile	-0.07	0.03	0.08	-0.08	0.06	0.05	0.07	1											
(9) Tender	0.09	0.02	0.09	0.04	-0.23***	-0.33***	0.15**	0.12*	1										
(10) Contested	0.104	-0.04	-0.02	0.14**	-0.03	0.04	0.01	-0.03	0.12*	1									
(11) Targetadvisor	0.2***	-0.08	-0.25***	-0.04	0.44***	0.53***	-0.2***	-0.06	-0.14**	0.07	1								
(12) Acquirerdvisor	0.1	0.122*	-0.01	0.03	0.51***	0.52***	0.25***	-0.03	-0.08	0.06	0.46***	1							
(13) Targetlo	0.3***	-0.15**	-0.13*	0.03	0.06	0.3***	0.22***	0.07	-0.40***	0.13*	0.13*	0.03	1						
(14) Acquirerlo	0.12*	-0.14**	-0.19**	-0.04	-0.12*	-0.01	-0.05	-0.03	-0.16**	0.12*	-0.003	-0.11	0.32***	1					
(15) ADRI	0.3***	-0.2***	-0.2***	-0.01	0.013	0.27***	0.18***	0.044	-0.31***	0.13*	0.11	0.05	0.83***	0.27***	1				
(16) ANTI	0.11*	0.02	0.16**	0.17**	-0.08	-0.07	-0.06	0.05	0.06	0.02	0.12*	0.13*	0.17**	0.13**	0.13*	1			
(17) Enforcement	0.23***	-0.2***	-0.2**	-0.002	0.09	0.27***	0.11	0.056	-0.05	0.12*	0.15**	0.07	0.4***	0.14**	0.34***	0.2***	1		
(18) Accounting	0.2***	-0.2***	-0.11	-0.06	-0.01	0.13*	0.13*	0.056	0.09	0.09	0.19***	0.06	0.18***	-0.01	0.3***	0.02	0.5***	1	

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.

the target's side and the acquisition premium, 0.2. Previous literature has reported mixed results regarding how hiring the advisory might affect the acquisition premium, and our correlation coefficient supports the idea that the cross-border acquisition premium is positively correlated with the use of advisory.

To gain insights into the relation between one firm's reputational risk and the takeover premium in cross-border M&As, we run fix-effects regressions, which examine the association between target's reputational risk and the acquisition premium as shown in Table 4.2. We use the sample of cross-border transactions to analyze how the target's reputational risk might influence the acquisition premium by estimating the following specification:

$$\text{Log}(\text{Premium}) = \alpha + \beta \text{Target RRIP} + \gamma X + \varepsilon \quad (4.1)$$

where X refers to a set of control variables including the logarithm of the transaction volume, horizontal dummy, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million, cash deal dummy, hostile deal dummy, tender offer dummy, contested deal dummy, the number of target's and acquirer's advisor and target's legal origin.

In column 1, we find that the target's reputational risk is negatively correlated with the acquisition premium. An increase in the level of RRIP by one point is associated with a 0.012 decrease in the logarithm of the premium, which translates into an average decrease of 1.2% in the premium. More specifically, the standardized beta coefficient (not shown) for target's RRIP is -0.19, indicating that one-point increase in target RRIP's standard deviations leads to approximately 0.19 decrease in the premium's standard deviations, which is more economically significant compared to the standardized beta coefficient of deal size, 0.18. The coefficient of the value of the deal is positive and significant. That is, larger deals are associated with higher premiums when using transaction value as the proxy for deal size. Similar to our results, Loderer and Martin (1990), argue that acquirers are more likely to overpay for bigger targets on average because acquirer managers could be fascinated by these large acquisitions for the publicity they attract. Moreover, top executives may pay a higher premium for large firms for the high private benefits that are often provided by large deals (Grinstein & Hribar, 2004; Harford & Li, 2007).

In column 2, we add deal-level dummy variables for hostile bid, tender offer and contested deal. The results on target RRIP and deal value do not change, and now tender offer is significantly

**Table 4.2: OLS Regression of Target RRIP on Cross-Border Acquisition Premium**

The table presents the results of seven OLS regressions for the sample of cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target four weeks before the announcement. Independent variable is target RRIP, which is equal to the highest level of the RRI over the last two years. The control variable at the cross-country level is target legal origin, a dummy variable that equals one if the country has common law system. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; hostile deal, a dummy variable that equals one if the deal is hostile and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Target RRIP	-0.012** (-2.59)	-0.011** (-2.53)	-0.01** (-2.41)	-0.01* (-1.69)	-0.013*** (-2.7)	-0.012** (-2.53)	-0.008* (-1.78)
Horizontal			0.15 (0.85)	0.11 (0.66)		0.20 (1.08)	0.13 (0.78)
Target size					0.04 (0.92)	-0.035 (-0.65)	-0.01 (-0.17)
Deal value	0.094*** (2.51)	0.13*** (3.13)	0.09* (1.77)	0.06 (1.32)			
Cash deal			0.27 (1.48)	0.01 (0.08)		0.23 (1.29)	-0.01 (-0.07)
Hostile deal		-0.98 (-1.48)	-0.81 (-1.2)	-1.23* (-1.88)	-0.80 (-1.17)	-0.49 (-0.72)	-1.05 (-1.59)
Tender offer		0.35** (2.10)	0.30* (1.76)	0.61*** (3.46)	0.19 (1.18)	0.16 (1.00)	0.54*** (3.06)
Contested deal		0.23 (0.79)	0.17 (0.56)	-0.07 (-0.24)	0.33 (1.1)	0.2 (0.65)	-0.06 (-0.19)
Target advisor			0.13 (1.47)	0.12 (1.48)		0.20** (2.2)	0.16* (1.94)
Acquirer advisor			0.05 (0.64)	0.04 (0.62)		0.11 (1.57)	0.08 (1.2)
Target legal origin				0.87*** (4.25)			0.90*** (4.37)
$R^2$	0.1095	0.1408	0.1631	0.2350	0.1019	0.1514	0.2281
$N$ observations	219	219	219	219	219	219	219
F-Statistic	1.37	1.54*	1.50*	2.27***	1.06	1.38	2.18***
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.

positive. We interpret this finding as evidence of the free-rider theory, which is, the acquirer in a tender offer needs to pay a higher premium to persuade the target shareholders to tender their shares. Our contested deal variable, however, is not significantly positive as other literature has reported. This might be because, when a firm's reputational risk is taken into consideration, the competition for targets won't necessarily affect the premium as one firm can distinguish itself from other competitors through its better reputation.

In column 3 and 4, we include firm-level and country-level variables. The major result on target RRIP remains the same, with the absolute value of the standardized beta coefficient decreasing from -0.19 to -0.12 after adding other control variables. However, deal value loses its significance after adding the target's legal origin dummy. This finding suggests that the deal value variable is significant in Column 1, 2 and 3 only because it captures the difference in legal origin for different countries. More interestingly, the hostile bid becomes significantly negative after adding the target's legal origin dummy, indicating that in a hostile bid, acquirers are likely to pay less for the target when considering its legal system. This finding, different from the work by Schwert (2000) and Rossi & Volpin (2004) who demonstrate a positive relation between hostile bid and acquisition premium, suggests that target's legal origin aggravates the influence of hostile bid in cross-border M&As. The target legal origin variable is significantly and positively associated with the acquisition premium, consistent with previous literature, indicating a higher premium in countries with higher shareholder protection. The possible interpretation is that, since the acquisition premium measures the gain available to all target shareholders, the stronger shareholder protection helps reduce the cost of capital, and therefore increases the competition among bidders, leading to a higher premium. Moreover, Grossman & Hart (1980) illustrate the free-rider problem that is caused by higher shareholder protection, forcing bidders to overpay for the target.

In column 5, 6 and 7, we repeat the previous regressions using target size, which is the logarithm of the target's market capitalization four weeks before the announcement, as the proxy for transaction size instead of the deal value. Similar to our existing results, target RRIP is significantly and negatively associated with acquisition premium while target legal origin and tender offer are significantly and positively associated with acquisition premium. The absolute value of the standardized beta coefficient for target's RRIP increases from -0.12 to -0.13 when target size, instead of deal value, is included in the model, indicating the larger economic

significance of the target's reputational risk when controlling for target's market value. This time, after adding the target legal origin dummy variable, the number of advisors that target hired during the negotiation process becomes significant positive in column 7. Considering the expert knowledge and skills that investment bankers can offer to their clients, target and acquirers often employ investment bankers to negotiate premiums (Eccles & Crane, 1988; Haunschild, 1994). Literature has demonstrated mixed results on the association between acquisition premium and advisory due to the potential agency conflicts that could happen for acquirers (Hayward, 2003; Porrini 2006). But for targets, since investment bankers' fees are a percentage of the acquisition premiums, their advisories are more motivated to negotiate higher premiums for them.

In M&As, there're cases that target's management team joins and manages acquirer's company after the acquisition. Therefore, it is possible that the acquirer's reputation could affect the acquisition premium as well. Thus, we include the acquirer's reputational risk and acquirer's legal origin in our regressions by estimating the following specification:

$$\text{Log (Premium)} = \alpha + \beta \text{Target RRIP} + \gamma \text{Acquirer RRIP} + \delta X + \varepsilon \quad (4.2)$$

where  $X$  refers to a set of control variables including the logarithm of the transaction volume, horizontal dummy, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million, cash deal dummy, hostile deal dummy, tender offer dummy, contested deal dummy, the number of target's and acquirer's advisor, and target's and acquirer's legal origin.

Table 4.3 presents the regression results. Overall, the results remain the same as Table 4.2, with the only exception that hostile bid and the number of target advisory are no longer significant in column 6 and 7. This insignificant result on hostile bid suggests that this variable captures the difference between the target's reputational risk and the acquirer's reputational risk as well as the differences in the legal system between two countries. Concerning the role of target advisory, we interpret the findings as the evidence of the effect from the acquirer's reputation that helps reduce the information asymmetry between target and acquirer. When the information on acquirer's reputational risk is available for the target, it provides the target with additional information on acquirer's overall quality when negotiating the price, reducing the need for advisor's expert knowledge and skills.

**Table 4.3: OLS Regression of Target/Acquirer RRIP on Cross-Border Acquisition Premium**

The table presents the results of seven OLS regressions for the sample of cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target four weeks before the announcement. Independent variables are target/acquirer RRIP, which is equal to the highest level of the RRI over the last two years. The control variable at the cross-country level is target/acquirer legal origin, a dummy variable that equals one if the country has common law system. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; hostile deal, a dummy variable that equals one if the deal is hostile and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Target RRIP	-0.02*** (-3.53)	-0.019*** (-3.51)	-0.02*** (-3.32)	-0.02** (-2.84)	-0.02*** (-3.85)	-0.02*** (-3.59)	-0.02*** (-3.03)
Acquirer RRIP	0.01 (1.12)	0.01 (1.11)	0.005 (0.85)	0.01 (1.22)	0.01 (1.51)	0.01 (1.05)	0.01 (1.37)
Horizontal			-0.04 (-0.2)	-0.06 (-0.27)		-0.03 (-0.13)	-0.049 (-0.23)
Target size					0.03 (0.58)	-0.043 (-0.67)	-0.02 (-0.32)
Deal value	0.1** (2.34)	0.12*** (2.63)	0.09 (1.61)	0.06 (1.09)			
Cash deal			0.15 (0.72)	-0.07 (-0.30)		0.12 (0.56)	-0.10 (-0.45)
Hostile deal		0.31 (0.35)	0.44 (0.48)	0.30 (0.33)	0.56 (0.61)	0.87 (0.94)	0.53 (0.59)
Tender offer		0.32* (1.68)	0.29 (1.50)	0.6*** (2.88)	0.18 (0.95)	0.18 (0.95)	0.55** (2.63)
Contested deal		0.30 (0.88)	0.29 (0.82)	0.04 (0.12)	0.40 (1.16)	0.31 (0.9)	0.053 (0.15)
Target advisor			0.06 (0.56)	0.16 (0.60)		0.12 (1.18)	0.10 (0.97)
Acquirer advisor			0.06 (0.72)	0.07 (0.79)		0.13 (1.59)	0.11 (1.33)
Target legal origin				0.77*** (3.15)			0.81*** (3.34)
Acquirer legal origin				0.03 (0.15)			0.01 (0.07)
$R^2$	0.2365	0.2602	0.2678	0.3210	0.2269	0.2568	0.3158
$N$ observations	176	176	176	176	176	176	176
F-Statistic	1.78**	1.77**	1.57**	1.89***	1.48*	1.49*	1.85***
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.

Across both specifications, we find that the target's reputational risk, which is measured by the target RRIP index, is significantly and negatively associated with the acquisition premium in cross-border M&As, consistent with our first hypothesis that there is a negative relation between target's reputation risk and cross-border acquisition premium. The findings support our prediction that firm's reputational risk carries information that can send a negative signal to the M&A market, resulting in a lower acquisition premium paid by acquirers. Due to information asymmetry in cross-border M&As, acquirers seek available information to compensate for the higher uncertainty that comes from the differences in culture, legal systems, corporate governance and investment environment, and the analysis of target's social performance is an effective way to reduce information asymmetry and firm-specific risks.

Despite the insignificant relation between acquirer's reputational risk and acquisition premium, the differences in risk exposure between target and acquirer might play a role during the negotiation process; especially we study the targets that are completed owned by acquirers after the transaction. This ownership brings acquirer's the attention to reputation differences since reputational capital is one of the most important intangible assets, and M&A activity transfers target's intangible assets to the acquirer, which could benefit or hurt acquirer in the long run, depending on the quality of target's asset. This concern will influence the acquirer's valuation on target and affect the final premium. Therefore, our specification is:

$$\text{Log (Premium)} = \alpha + \beta(\text{Target RRIP} - \text{Acquirer RRIP}) + \gamma X + \varepsilon \quad (4.3)$$

where  $X$  refers to a set of control variables including the logarithm of the transaction volume, horizontal dummy, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million, cash deal dummy, hostile deal dummy, tender offer dummy, contested deal dummy, the number of target's and acquirer's advisor and target's and acquirer's legal origin.

As shown in Table 4.4, the regression results are consistent with our hypothesis. The difference in reputational risk between target and acquirer is significantly and negatively associated with the cross-border acquisition premium. That is, the acquirer is likely to pay less for a target if it has worse ESG-related reputation than acquirer itself, as expected. The standardized beta coefficient for the difference in reputational risks is -0.23, indicating a 0.23 decrease in premium's standard deviations when the standard deviations of the difference in reputational risks increase by 1. This finding supports the argument that the integration of intangible resources is

**Table 4.4: OLS Regression of the Difference in RRIP between Target and Acquirer on Cross-Border Acquisition Premium**

The table presents the results of seven OLS regressions for the sample of cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target four weeks before the announcement. Independent variable is the difference in RRIP index between target and acquirer. The control variable at the cross-country level is target/acquirer legal origin, a dummy variable that equals one if the country has common law system. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; hostile deal, a dummy variable that equals one if the deal is hostile and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Difference in RRIP	-0.013** (-2.77)	-0.013*** (-2.75)	-0.012** (-2.44)	-0.01** (-2.4)	-0.015*** (-3.25)	-0.01*** (-2.76)	-0.012** (-2.63)
Horizontal			-0.05 (-0.25)	-0.06 (-0.31)		-0.03 (-0.15)	-0.05 (-0.26)
Target size					0.01 (0.15)	-0.06 (-0.93)	-0.028 (-0.45)
Deal value	0.10** (2.17)	0.11** (2.47)	0.10* (1.76)	0.063 (1.14)			
Cash deal			0.16 (0.74)	-0.08 (-0.38)		0.12 (0.56)	-0.12 (-0.54)
Hostile deal		0.22 (0.24)	0.29 (0.31)	0.18 (0.20)	0.51 (0.55)	1.79 (0.84)	0.45 (0.50)
Tender offer		0.32* (1.66)	0.30 (1.54)	0.64*** (3.09)	0.17 (0.92)	0.17 (0.92)	0.58*** (2.79)
Contested deal		0.32 (0.93)	0.32 (0.90)	0.03 (0.09)	0.42 (1.2)	0.34 (0.97)	0.045 (0.13)
Target advisor			0.05 (0.48)	0.05 (0.56)		0.12 (1.21)	0.094 (0.97)
Acquirer advisor			0.02 (0.25)	0.04 (0.49)		0.11 (1.27)	0.089 (1.1)
Target legal origin				0.85*** (3.53)			0.89*** (3.73)
Acquirer legal origin				0.04 (0.19)			0.02 (0.1)
$R^2$	0.2129	0.2368	0.2416	0.3099	0.2053	0.2299	0.3046
$N$ observations	176	176	176	176	176	176	176
F-Statistic	1.62**	1.63**	1.42*	1.86***	1.36	1.33	1.82***
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.



vital for the successful post performance of M&As (Das & Teng, 2000). Through merger and acquisition, firms can access other firms' key capabilities and resources, and the Resource-Based View (RBV) suggests that integrating intangible resources, which are valuable, rare, inimitable and non-substitutable (VRIN), can contribute to a better post-performance for the acquirer (Sigera & Cahoonb, 2018). Compared with tangible assets, intangible assets are more difficult to develop and duplicate, making them more unique and heterogeneous. Regarding that, corporate reputation is identified as one of the most important strategic assets (Barnett et al., 2006). Although reputational asset is not easy to measure and integrate, based on three international M&As, Birkinshaw et al. (2000) introduce the two-sub processes to integrate intangible resources, including reputation integration, which is further developed by Sigera & Cahoonb (2018). They illustrate that reputation integration is slower than other asset integration and is usually undertaken after some acceptable performance is achieved. Our empirical results support this reputation-integration argument by showing that the difference in reputational risk exposure between target and acquirer influences the valuation of the target in cross-border M&As.

#### **4.2 Investment Environment Analysis**

Table 4.5 presents the regression results with each column revealing the relationship between one investment environment index and the acquisition premium while controlling for deal size, target size, horizontal industry, cash deal, tender offer, hostile deal, contested deal and the number of target's and acquirer's advisors.

Similar to our existing findings, the RRIP is significantly and negatively associated with acquisition premium in cross-border M&As after controlling for the investment environment characteristics, indicating a higher premium for the target with a better firm reputation after taking the investment environment into consideration. Column 1, 2, 5 and Column 6 measures the relation between ADRI and acquisition premium. Consistent with previous literature (Rossi & Volpin, 2004; Starks & Wei, 2013), ADRI is positively related to the premium, which indicates that, on average, targets from countries with better shareholder protection command higher cross-border M&A premiums than otherwise. Similarly, as reported in Column 3 and Column 7, there is a positive association between the efficiency and integrity of the legal environment and the acquisition premium, which is, however, less economically significant than ADRI. Regarding the accounting standards, it is only significantly and positively related to acquisition premium when target size is used as the proxy for transaction size.

**Table 4.5: OLS Regression of Target RRIP and Investment Environment Index on Cross-Border Acquisition****Premium**

The table presents the results of eight OLS regressions for the sample of cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target four weeks before the announcement. Independent variable is target RRIP, which is equal to the highest level of the RRI over the last two years. The control variables at the cross-country level are: target legal origin, a dummy variable that equals one if the country has common law system; proxies for investment environment, which include investor protection, accounting standards and judicial efficiency. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; hostile deal, a dummy variable that equals one if the deal is hostile and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Target RRIP	-0.01* (-1.66)	-0.01** (-2.57)	-0.01** (-2.16)	-0.01** (-2.27)	-0.01* (-1.70)	-0.01*** (2.72)	-0.01** (-2.15)	-0.01** (-2.31)
ADRI	0.27*** (3.73)				0.27*** (3.86)			
ANTI		0.22** (2.33)				0.19** (2.01)		
Enforcement			0.13* (1.85)				0.15** (2.13)	
Accounting				0.01 (1.57)				0.01* (1.72)
Target size					-0.02 (-0.4)	-0.02 (-0.31)	-0.04 (-0.82)	-0.04 (-0.76)
Horizontal	0.14 (0.81)	0.17 (0.97)	0.12 (0.66)	0.13 (0.73)	0.16 (0.95)	0.20 (1.16)	0.15 (0.86)	0.17 (0.94)
Deal value	0.05 (1.02)	0.11** (2.12)	0.06 (1.18)	0.07 (1.39)				
Cash deal	0.11 (0.57)	0.32* (1.78)	0.24 (1.3)	0.24 (1.29)	0.07 (0.39)	0.28 (1.54)	0.19 (1.05)	0.19 (1.03)
Hostile deal	-0.97 (-1.49)	-0.85 (-1.27)	-0.85 (-1.26)	-0.80 (-1.19)	-0.80 (-1.21)	-0.52 (-0.78)	-0.60 (-0.89)	-0.52 (-0.77)
Tender offer	0.49*** (2.8)	0.32* (1.79)	0.29* (1.7)	0.25 (1.44)	0.42** (2.43)	0.16 (0.99)	0.19 (1.14)	0.13 (0.79)
Contested deal	-0.07 (-0.23)	0.15 (0.49)	0.09 (0.28)	0.13 (0.42)	-0.07 (-0.22)	0.18 (0.57)	0.084 (0.27)	0.14 (0.44)
Target advisor	0.15* (1.77)	0.12 (1.32)	0.14 (1.57)	0.12 (1.39)	0.18** (2.19)	0.18** (2.08)	0.19** (2.11)	0.17* (1.96)
Acquirer advisor	0.03 (0.42)	0.012 (0.17)	0.04 (0.54)	0.04 (0.55)	0.07 (0.95)	0.08 (1.14)	0.09 (1.29)	0.10 (1.37)
$R^2$	0.2259	0.1908	0.1834	0.1792	0.2223	0.1729	0.1802	0.1732
$N$ observations	213	217	213	213	213	217	213	213
F-Statistic	2.18***	1.72**	1.68**	1.63**	2.14***	1.52*	1.64**	1.57**
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.

### 4.3 Robustness Tests

This subsection evaluates the alternative explanations for the findings reported in the paper. One concern with the transfer-in-reputational-asset statement is that, in cross-border M&As, the differences in culture, law, and regulation between two different countries might make it difficult to compare the reputational risk of firms from two countries since it is possible that one controversy that happens in country A is not considered controversial in country B. Moreover, prior literature has illustrated interesting findings towards U.S. targets in both domestic (Malik, 2014; Choi et al., 2015) and international M&As (Rossi & Volpin, 2004; Starks & Wei, 2013). Therefore, to address our concern, we construct a U.S. target-only subsample and replicate our previous analysis to evaluate the transfer theory.

Table 4.6 reports the coefficients of six OLS models derived from the specification 4.3 for U.S. target. Consistent with previous results from Table 4.4, the difference in RRIP between target and acquirer is significant and negative in all regressions, indicating a lower premium when the target has a worse reputation than the acquirer for U.S. targets. The standardized beta coefficient (not shown) for the difference is -0.16, indicating that one-point increase in the difference's standard deviations leads to approximately 0.16 decrease in the premium's standard deviations. Target size, this time, becomes significantly negative, that is, larger deals are associated with lower premiums when using target size as the proxy for deal size. Additionally, contested bids are associated with a 0.45 increase in the logarithm of premium, consistent with the view that premium is higher when there is competition among acquirers. Additionally, we report a significantly positive relation between the acquisition premium and cash deal for U.S. targets. Previous literature has reported mixed results on the influence of payment method on acquisition premium. Bowman et al. (2013), for example, find a significantly negative relation between cash deal and acquisition premium while Jory et al. (2016) and Gomes & Marsat (2017) find that cash deal is positively and significantly associated with acquisition premium. Schlingemann & Wu (2015), however, demonstrate no significant association between cash deal and acquisition premium. Our study illustrates that cash deal is associated with a higher acquisition premium in cross-border M&As for U.S. targets.

**Table 4.6: OLS Regression of the Difference in RRIP between Target and Acquirer for U.S. Subsample on Cross-Border Acquisition Premium**

The table presents the results of six OLS regressions for the U.S. target sample of both domestic and cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target four weeks before the announcement. Independent variable is the difference in RRIP index between U.S. target and acquirer. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; hostile deal, a dummy variable that equals one if the deal is hostile and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; cross-border, a dummy variable that equals one if the deal is cross border, and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)
Difference in RRIP	-0.01** (-2.24)	-0.01** (-2.27)	-0.01** (-2.35)	-0.01* (-1.93)	-0.01** (-2.44)	-0.01** (-2.48)
Horizontal						-0.05 (-0.33)
Target size			-0.07* (-1.71)	-0.044 (-0.94)	-0.11** (-2.16)	-0.12** (-2.34)
Deal value		-0.03 (-0.71)				
Cash deal				0.28* (1.83)	0.31** (2.09)	0.31** (2.02)
Hostile deal				-0.13 (-0.13)	0.33 (0.34)	0.45 (0.46)
Tender offer				0.09 (0.52)	0.13 (0.77)	0.08 (0.45)
Cross border	-0.02 (-0.15)	-0.03 (-0.19)	-0.04 (-0.24)	-0.11 (-0.72)	-0.16 (-1.09)	-0.15 (-1.01)
Contested deal						0.45* (1.7)
Public acquirer						0.014 (0.06)
Target advisor					0.17** (1.98)	0.16* (1.84)
Acquirer advisor					0.11* (1.72)	0.12* (1.87)
$R^2$	0.1053	0.1073	0.1172	0.1349	0.1676	0.1793
$N$ observations	241	241	241	241	241	241
F-Statistic	1.06	1.03	1.14	1.18	1.41**	1.37**
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.

Our results of the higher premiums for targets from countries with common-law traditions are consistent with previous studies (Rossi & Volpin, 2004). In those countries, however, the effect of firm reputation might be less pronounced than it is in civil-law countries because civil-law countries are associated with a lower level of shareholder protection, which are more likely to have corruption and human rights violations problems. Therefore, we focus on the interaction between the target's reputation building, that is, its RRIP, and target's legal origin.

As reported in Table 4.7, however, we fail to find any significant effects of the interaction term of target's RRIP and its legal origin after controlling for target's legal origin, indicating that RRIP is not dependent on legal origins. Therefore, the findings do not support the hypothesis about reputation building and country legal origin.

As a further robustness check, we estimate specification 4.1, 4.2 and 4.3 using RRI index as the proxy for a firm's reputational risk instead. Similar to the RRIP index, RRI is a proprietary algorithm developed by RepRisk that dynamically captures and quantifies reputational risk exposure related to ESG issues. Instead of focusing on the peak level of the firm's reputational risk exposure, RRI index provides an overview of the associations between a company and its ESG issues on a monthly basis.

We collect the RRI data that happens before the premium date from the RepRisk platform for each firm and replicate our analysis on the cross-country sample. Table 4.8 reports the results of eight regressions based on the specification 4.1, 4.2 and 4.3.

In specification 4.1, target RRI remains significantly negative until the target legal origin is included in the model, suggesting that the lower premium is a feature of the target's legal origin. The results are very similar to our primary empirical results of Table 4.2, Table 4.3 and Table 4.4. The significant negative relation between target's RRI, the difference in reputational risk between the target and acquirer, and the acquisition premium hold when we replace RRIP index with RRI index. Especially, when adding the acquirer's RRI index to the model, the insignificant coefficients of Target RRI in column 2 and 4 from Table 4.8 become significantly negative again.

To eliminate the possible influences from the outliers, we conduct another robustness test based on our previous cross-country sample but without countries with extremely high premiums (New Zealand and Japan) and countries with extremely low premiums (Switzerland), and the results are reported in Table 4.9. As we expected, the results remain basically the same as our

**Table 4.7: OLS Regression of Target RRIP and the Interaction between Target RRIP and Target Legal Origin on Cross-Border Acquisition Premium**

The table presents the results of six OLS regressions for the sample of cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target four weeks before the announcement. Independent variables are target RRIP, which is equal to the highest level of the RRI over the last two years, and the interaction term between target RRIP and target legal origin. The control variable at the cross-country level is target legal origin, a dummy variable that equals one if the country has common law system. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; hostile deal, a dummy variable that equals one if the deal is hostile and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)
Target RRIP	-0.02** (-3.47)	-0.02*** (-3.9)	-0.02*** (-3.70)	-0.01 (-1.18)	-0.01 (-0.91)	-0.01 (-0.99)
Target RRIP * target lo	0.014** (2.31)	0.019*** (3.04)	0.02*** (2.84)	-0.003 (-0.04)	-0.001 (-0.14)	-0.0005 (-0.06)
Horizontal			0.18 (1.04)			0.11 (0.64)
Deal value	0.07* (1.9)	0.11*** (2.79)	0.07 (1.38)	0.06* (1.67)	0.11*** (2.84)	0.06 (1.32)
Cash deal			0.13 (0.73)			0.014 (0.08)
Hostile deal		-1.21* (-1.84)	-0.98 (-1.48)		-1.43** (-2.24)	-1.23* (-1.87)
Tender offer		0.49*** (2.90)	0.44** (2.53)		0.66*** (3.79)	0.62*** (3.45)
Contested deal		0.10 (0.35)	0.04 (0.12)		-0.02 (-0.06)	-0.07 (-0.23)
Target advisor			0.13 (1.48)			0.12 (1.47)
Acquirer advisor			0.05 (0.64)			0.04 (0.62)
Target legal origin				0.58** (2.14)	0.90*** (3.24)	0.88*** (3.09)
$R^2$	0.1327	0.1795	0.1968	0.1523	0.2215	0.2350
$N$ observations	219	219	219	219	219	219
F-Statistic	1.60*	1.95***	1.81***	1.78**	2.41***	2.17***
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.

**Table 4.8: OLS Regression of Target RRI on Cross-Border Acquisition Premium**

The table presents the results of eight OLS regressions for the sample of cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target four weeks before the announcement. Independent variables include target RRI, which denotes the current level of media and stakeholder coverage of a company related to ESG issues, and the difference in RRI index between target and acquirer. The control variable at the cross-country level is target/acquirer legal origin, a dummy variable that equals one if the country has common law system. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; hostile deal, a dummy variable that equals one if the deal is hostile and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	Target RRI only				Target & Acquirer RRI		Difference in RRI	
Target RRI	-0.01* (-1.69)	-0.006 (-0.98)	-0.012* (-1.83)	-0.007 (-1.11)	-0.02* (-1.85)	-0.02** (-2.00)		
Acquirer RRI					0.01 (1.13)	0.01 (1.39)		
Difference in RRI							-0.01* (-1.76)	-0.012** (-2.05)
Horizontal	0.15 (0.87)	0.11 (0.65)	0.20 (1.11)	0.13 (0.78)	-0.01 (-0.07)	-0.002 (-0.01)	-0.015 (-0.07)	-0.001 (-0.01)
Target size			-0.034 (-0.63)	-0.01 (-0.16)		-0.02 (-0.34)		-0.03 (-0.48)
Deal value	0.09* (1.78)	0.065 (1.34)			0.065 (1.15)		0.064 (1.15)	
Cash deal	0.28 (1.54)	0.016 (0.09)	0.24 (1.35)	-0.01 (-0.06)	-0.02 (-0.1)	-0.06 (-0.27)	-0.05 (-0.21)	-0.08 (-0.38)
Hostile deal	-0.76 (-1.1)	-1.22* (-1.84)	-0.43 (-0.62)	-1.03 (-1.55)	0.42 (0.46)	0.7 (0.75)	0.34 (0.38)	0.65 (0.7)
Tender offer	0.28 (1.64)	0.62*** (3.44)	0.14 (0.88)	0.54*** (3.04)	0.57*** (2.65)	0.5** (2.36)	0.59*** (2.76)	0.51** (2.44)
Contested deal	0.16 (0.54)	-0.08 (-0.27)	0.19 (0.62)	-0.06 (-0.22)	0.02 (0.06)	0.03 (0.09)	0.02 (0.07)	0.04 (0.11)
Target advisor	0.14 (1.58)	0.13 (1.57)	0.2** (2.31)	0.17** (2.04)	0.1 (0.96)	0.13 (1.4)	0.1 (1.00)	0.14 (1.47)
Acquirer advisor	0.035 (0.48)	0.033 (0.47)	0.10 (1.41)	0.07 (1.06)	0.04 (0.5)	0.09 (1.04)	0.03 (0.32)	0.08 (0.93)
Target legal origin		0.9*** (4.38)		0.93*** (4.5)	0.76*** (3.04)	0.8*** (3.24)	0.8*** (3.3)	0.8*** (3.46)
Acquirer legal origin					0.1 (0.52)	0.09 (0.45)	0.11 (0.55)	0.09 (0.47)
$R^2$	0.1545	0.2275	0.1383	0.2203	0.3004	0.2944	0.2971	0.2917
$N$ observations	219	219	219	219	176	176	176	176
F-Statistic	1.37	2.17***	1.24	2.09***	1.72**	1.67**	1.75**	1.71**
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.

**Table 4.9: OLS Regression of Target RRIP on Cross-Border Acquisition Premium (Excluding Outliers)**

The table presents the results of six OLS regressions for the sample of cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target four weeks before the announcement. Independent variables include target RRIP, acquirer RRIP and the difference in RRIP between target and acquirer. The control variable at the cross-country level is target/acquirer legal origin, a dummy variable that equals one if the country has common law system. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; hostile deal, a dummy variable that equals one if the deal is hostile and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)
	Target RRIP only		Target & Acquirer RRIP		Difference in RRIP	
Target RRIP	-0.008*	-0.01***	-0.02***	-0.02***		
	(-1.9)	(-1.99)	(-2.88)	(-3.06)		
Acquirer RRIP			0.01	0.01		
			(1.14)	(1.24)		
Difference in RRIP					-0.01**	-0.012**
					(-2.35)	(-2.54)
Horizontal	0.19	0.2	0.06	0.076	0.05	0.06
	(1.14)	(1.22)	(0.3)	(0.36)	(0.22)	(0.29)
Target size		-0.001		-0.003		-0.01
		(-0.00)		(-0.04)		(-0.19)
Deal value	0.045		0.045		0.05	
	(0.97)		(0.83)		(0.91)	
Cash deal	0.16	0.14	0.03	0.01	0.01	-0.02
	(0.87)	(0.79)	(0.13)	(0.04)	(0.03)	(-0.08)
Hostile deal	-1.14*	-1.03	0.34	0.47	0.22	0.39
	(-1.81)	(-1.62)	(0.38)	(0.53)	(0.25)	(0.44)
Tender offer	0.54***	0.49***	0.56***	0.52**	0.61***	0.56***
	(3.1)	(2.85)	(2.73)	(2.57)	(2.97)	(2.76)
Contested deal	-0.03	-0.02	0.06	0.07	0.05	0.06
	(-0.12)	(-0.08)	(0.16)	(0.2)	(0.14)	(0.17)
Target advisor	0.10	0.12**	0.04	0.07	0.04	0.07
	(1.25)	(1.55)	(0.47)	(0.69)	(0.44)	(0.71)
Acquirer advisor	0.07	0.1	0.09	0.12	0.06	0.09
	(1.00)	(1.40)	(1.06)	(1.43)	(0.71)	(1.16)
Target legal origin	0.8***	0.84***	0.69***	0.73***	0.77***	0.81***
	(4.08)	(4.20)	(2.86)	(3.05)	(3.23)	(3.43)
Acquirer legal origin			0.15	0.14	0.16	0.15
			(0.79)	(0.75)	(0.81)	(0.76)
$R^2$	0.2433	0.2395	0.3136	0.3102	0.3000	0.2960
$N$ observations	215	215	173	173	173	173
F-Statistic	2.32***	2.28***	1.79***	1.76**	1.74**	1.71**
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.



previous findings in Table 4.2, Table 4.3 and Table 4.4. The significantly negative association between the acquisition premium in cross-border M&As and firm's reputational risk hold even when we remove the outliers.

Additionally, the time span might be a concern for our empirical analysis. It is possible that the signaling effect from the firm reputation would disappear and the announcement effect would rise when the market anticipates an M&A announcement soon. For instance, Laamanen (2007) and Starks and Wei (2013) use premiums 1 week prior to the original announcement date. Therefore, we use the acquisition premiums 1 week before the announcement date as the alternative measurement of the difference between the bid price and the target's stock price to reevaluate the validity of our analysis about firm reputation. As shown in Table 4.10, the results for all three specifications remain consistent with our previous findings. The target's ESG reputational risk is negatively and significantly associated with the acquisition premium, and the difference in the firm's reputational risk is also significantly and negatively related to the acquisition premium.

Our last robustness test is about the feature of the hostile deals. As hostile deals only represent 1.4% of the total acquisitions in our sample, and they are usually accomplished by tender offers, we exclude those hostile deals and keep the tender offers for robustness check in our three specifications. The results are presented in Table 4.11, and the main reputational risk variables get slightly more significant after removing the hostile deals. Overall, excluding hostile deals do not affect our main findings.

**Table 4.10: OLS Regression of Target RRIP on Cross-Border Acquisition Premium (Alternative Premium)**

The table presents the results of six OLS regressions for the sample of cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target 1 week before the announcement. Independent variables include target RRIP, acquirer RRIP and the difference in RRIP between target and acquirer. The control variable at the cross-country level is target/acquirer legal origin, a dummy variable that equals one if the country has common law system. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; hostile deal, a dummy variable that equals one if the deal is hostile and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)
	Target RRIP only		Target & Acquirer RRIP		Difference in RRIP	
Target RRIP	-0.01** (2.06)	-0.01** (-2.13)	-0.02*** (-2.62)	-0.02*** (-2.85)		
Acquirer RRIP			0.001 (0.21)	0.01 (0.42)		
Difference in RRIP					-0.01* (1.64)	-0.01* (-1.92)
Horizontal	0.10 (0.54)	0.13 (0.73)	0.07 (0.32)	0.08 (0.36)	0.06 (0.26)	0.07 (0.32)
Target size		-0.03 (-0.56)		-0.03 (-0.49)		-0.05 (-0.68)
Deal value	0.07 (1.37)		0.09 (1.39)		0.09 (1.45)	
Cash deal	0.08 (0.40)	0.04 (0.23)	0.06 (0.23)	0.01 (0.03)	0.03 (0.11)	-0.02 (-0.10)
Hostile deal	-1.19* (-1.68)	-0.93 (-1.31)	0.58 (0.59)	0.93 (0.93)	0.40 (0.40)	0.81 (0.79)
Tender offer	0.49** (2.52)	0.39** (2.01)	0.47** (2.05)	0.39* (1.70)	0.54** (2.32)	0.45* (1.92)
Contested deal	-0.29 (-0.9)	-0.27 (-0.85)	-0.10 (-0.26)	-0.08 (-0.21)	-0.11 (-0.29)	-0.09 (-0.24)
Target advisor	0.16* (1.80)	0.21** (2.38)	0.13 (1.22)	0.18* (1.71)	0.13 (1.15)	0.19* (1.70)
Acquirer advisor	0.04 (0.47)	0.09 (1.20)	0.05 (0.59)	0.12 (1.30)	0.01 (0.15)	0.09 (0.96)
Target legal origin	0.69*** (3.11)	0.71*** (3.20)	0.53* (1.94)	0.58** (2.16)	0.65** (2.42)	0.71*** (2.64)
Acquirer legal origin			0.19 (0.87)	0.16 (0.76)	0.20 (0.91)	0.17 (0.78)
$R^2$	0.2020	0.1956	0.2875	0.2788	0.2626	0.2540
$N$ observations	219	219	176	176	176	176
F-Statistic	1.89***	1.80***	1.61**	1.55**	1.48*	1.41*
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.

**Table 4.11: OLS Regression of Target RRIP on Cross-Border Acquisition Premium (Excluding Hostile)**

The table presents the results of six OLS regressions for the sample of cross-border deals. The dependent variable is the natural logarithm of premium, or the bid price as a percentage of the closing price of the target four weeks before the announcement. Independent variables include target RRIP, acquirer RRIP and the difference in RRIP between target and acquirer. The control variable at the cross-country level is target/acquirer legal origin, a dummy variable that equals one if the country has common law system. Control variables at the firm level are: horizontal, a dummy variable that equals one if they belong to the same industry at two-digit SIC-code level, and target size, the logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million. Control variables at the deal level are: target/acquirer advisor, the number of target's and acquirer's advisors involved in the transaction; deal value, the logarithm of the transaction volume; cash deal, a dummy variable that equals one if it is a cash deal and zero otherwise; tender offer, a dummy variable that equals one if the deal involves a tender offer and zero otherwise; contested, a dummy variable that equals one if the number of bidders is larger than one and zero otherwise. In all regressions, we also include year and industry (at one-digit SIC-code level) dummies (not shown).

	(1)	(2)	(3)	(4)	(5)	(6)
	Target RRIP only		Target & Acquirer RRIP		Difference in RRIP	
Target RRIP	-0.01*	-0.01*	-0.02***	-0.02***		
	(-1.89)	(-1.91)	(-2.84)	(-3.01)		
Acquirer RRIP			0.01	0.01		
			(1.23)	(1.38)		
Difference in RRIP					-0.01**	-0.012***
					(-2.40)	(-2.63)
Horizontal	0.15	0.17	-0.06	-0.05	-0.07	-0.06
	(0.90)	(1.01)	(-0.28)	(-0.25)	(-0.31)	(-0.28)
Target size		-0.03		-0.01		-0.02
		(-0.50)		(-0.20)		(-0.36)
Deal value	0.05		0.06		0.07	
	(1.00)		(1.17)		(1.20)	
Cash deal	0.02	-0.01	-0.07	-0.1	-0.08	-0.12
	(0.10)	(-0.03)	(-0.31)	(-0.49)	(-0.38)	(-0.57)
Tender offer	0.54***	0.48***	0.61***	0.57***	0.65***	0.60***
	(3.10)	(2.76)	(2.99)	(2.77)	(3.17)	(2.92)
Contested deal	-0.02	-0.01	0.03	0.04	0.03	0.04
	(-0.05)	(-0.04)	(0.10)	(0.12)	(0.08)	(0.11)
Target advisor	0.14*	0.17**	0.05	0.09	0.05	0.09
	(1.67)	(2.10)	(0.56)	(0.91)	(0.54)	(0.92)
Acquirer advisor	0.06	0.09	0.06	0.10	0.04	0.09
	(0.78)	(1.35)	(0.76)	(1.28)	(0.48)	(1.07)
Target legal origin	0.81***	0.83***	0.78***	0.83***	0.85***	0.91***
	(3.99)	(4.12)	(3.20)	(3.46)	(3.56)	(3.83)
Acquirer legal origin			0.02	0.0005	0.03	0.01
			(0.11)	(0.00)	(0.16)	(0.04)
$R^2$	0.2210	0.2179	0.3205	0.3141	0.3097	0.3034
$N$ observations	219	219	176	176	176	176
F-Statistic	2.19***	2.15***	1.96***	1.90***	1.93**	1.87***
Industry fixed effect	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effect	Yes	Yes	Yes	Yes	Yes	Yes

\*\*\*, \*\*, \* indicate significance at 1%, 5% and 10% levels, respectively.

## **Chapter 5: Conclusions**

Using a sample of cross-border deals in 36 different countries, announced between 2007 and 2017, we find that the firm with a better ESG-related reputation is associated with a higher acquisition premium in cross-border deals, and this relation is robust across different investment environment. Also, acquirers are likely to pay more for targets with the better reputation than themselves, indicating a concern for the potential reputation transfer from target to acquirer after the acquisition. In the U.S. target subsample, we find consistent negative results between the difference in reputational risk between the target and acquirer and the cross-border acquisition premium. Additionally, this negative association remains robust when controlling for different investment environment characteristics. Those results support for our argument concerning the signaling role of a firm's reputation as a mechanism that reduces the information asymmetry between the target and acquirer in cross-border M&As. Also, our study indicates that firm's socially irresponsible performances, similar to its socially responsible behaviors, could affect the firm value in cross-border M&As.

The present findings can also contribute to answering the broader question of how information asymmetry affects cross-border premiums. Due to the different culture, corporate governance, law system and regulations, there is a higher uncertainty and information asymmetry between the foreign target and acquirer, making it more difficult for firms to conduct target assessment and valuation. Therefore, acquirers are motivated to utilize available signals to gain useful information about the target, and our study suggests that a firm's ESG-related reputation level could help reduce the information asymmetry by sending out a signal of the firm's overall quality.

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## Appendix: Variable Definitions and Sources

### 1. Firm-level variables

Variables	Notations	Descriptions	Data source(s)
<b>Target/Acquirer RRIP</b>	<i>TARGETRRIP ACQUIRERRIP</i>	An index that is equal to the highest level of the RRI over the last two years – a proxy for overall ESG and business risk exposure.	RepRisk Platform
<b>Target/Acquirer RRI</b>	<i>TARGETRRI ACQUIRERRRI</i>	An index that denotes the current level of media and stakeholder coverage of a company related to ESG issues.	RepRisk Platform
<b>Difference in RRIP/RRI between target and acquirer</b>	<i>DIFFERENCEINRRI DIFFERENCEINRRIP</i>	Target's RRIP/RRI index minus acquirer's RRIP/RRI index.	RepRisk Platform
<b>Horizontal</b>	<i>HORIZONTAL</i>	A dummy variable that is equal to one if they belong to the same industry at two-digit SIC-code level, and zero otherwise.	Thomson Financial SDC
<b>Target size</b>	<i>LNTARGETEQUITY</i>	The logarithm of the market capitalization of the target four weeks before the announcement of the deal in US\$ million.	Thomson Financial SDC

2. Deal-level variables

<b>Variables</b>	<b>Notations</b>	<b>Descriptions</b>	<b>Data source(s)</b>
<b>Premium</b>	<i>LNPREMIUM4WEEK</i>	The natural logarithm of bid price as a percentage of the closing price of the target four weeks before the announcement.	Thomson Financial SDC
<b>Deal Value</b>	<i>LNDV</i>	The natural logarithm of the deal value.	Thomson Financial SDC
<b>Cash deal</b>	<i>CASHDEAL</i>	A dummy variable that is equal to 1 if the acquisition is entirely paid in cash, and 0 otherwise.	Thomson Financial SDC
<b>Hostile deal</b>	<i>HOSTILE</i>	A dummy variable that is equal to 1 if the bid is classified as unsolicited, 0 otherwise.	Thomson Financial SDC
<b>Tender offer</b>	<i>TENDER</i>	A dummy variable that is equal to 1 if the acquisition is done through a tender offer, 0 otherwise.	Thomson Financial SDC
<b>Contested</b>	<i>CONTESTED</i>	A dummy variable that is equal to 1 if the number of bidders is larger than one, 0 otherwise.	Thomson Financial SDC
<b>Cross border</b>	<i>CROSSBORDER</i>	A dummy variable that is equal to 1 if the target country differs from the acquirer country, 0 otherwise.	Thomson Financial SDC
<b>Target/Acquirer advisor</b>	<i>TARGETADVISOR ACQUIRERADVISOR</i>	The number of advisors that target/acquirer hired during the transaction.	Thomson Financial SDC

### 3. Country-level variables

<b>Variables</b>	<b>Notations</b>	<b>Descriptions</b>	<b>Data source(s)</b>
<b>Target Legal Origin</b>	<i>TARGETLO</i>	A dummy variable that is equal to 1 if the target country has common law system, and zero otherwise.	CIA Factbook
<b>Acquirer Legal Origin</b>	<i>ACQUIRERLO</i>	A dummy variable that is equal to 1 if the acquirer country has common law system, and zero otherwise.	CIA Factbook
<b>ADRI(LLSV)</b>	<i>ADRI</i>	An index ranges from 0 to 6 that aggregates the shareholder rights. A higher value indicates better shareholder protection.	La Porta et al. (1998)
<b>ADRI(Spamann)</b>	<i>ANTI</i>	An index aggregating corrected anti-director rights from 0 to 6.	Spamann (2005)
<b>Enforcement</b>	<i>ENFORCEMENT</i>	An index ranges from 0 to 10 that assesses efficiency and integrity of the legal environment as it affects business, particularly foreign firms, with a higher value better judicial efficiency.	La Porta et al. (1998)
<b>Accounting</b>	<i>ACCOUNTING</i>	An index created by examining and rating companies' 1990 annual reports on their inclusion or omission of 90 items. A minimum of 3 companies in each country were studied.	La Porta et al. (1998)