Cultural Determinants of M&A Returns: How Fairness Opinions by Boutique Firms Affect Value

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Abstract

In recent years, an increasing amount of attention has been drawn to boutique investment banks as they climb industry league tables. I examine the difference between boutique and full-service firms, and whether cultural distinctions can be seen through the transactions they advise on. I use announcement period returns to determine the effect of differences in an acquirer's investment bank on transaction returns. First, I find that transactions that have at least one boutique as a buy-side advisor have 2.8% higher returns than transactions entirely run by full-service banks. Second, I demonstrate the contradictory negative impact that a boutique has as a provider of buy-side fairness opinions. I interpret this to mean that both with and without providing a fairness opinion, boutiques are perceived to act differently than full-service firms, and often act as a check against potential conflicts of interest.

Keywords: Financial advisor, boutique, fairness opinion, merger, corporate culture, announcement return

I. Introduction

In recent years, the concept of "culture" has become just another buzzword in the business world, used frequently and without great thought. Companies promote generalized statements concerning their corporate culture, and how it uniquely prepares them for the work that they do. Yet what is culture, and can its impact on a business truly be determined? Recent literature has aimed to measure the effect of different elements of culture – shared trust, social hierarchies, etc. – on the overall performance of a firm.

When it comes to any firm, culture is akin to a shared body of information that communicates fundamental values and traits of a company, such as social hierarchy, incentive structures, and behavioral governance. A large amount of work behavior is linked to whether one party trusts the other, and this trust is informed by the cultural context of the situation (Blair & Stout 2001). At the same time, it is recognized that trust is also known to be the means by which mutually beneficial transactions are able to occur (Kreps 1990). Many factors go into the basis for trust, several of which include reputation, past performance, and company familiarity. Within investment banking, trust is a necessity for merger and acquisition (M&A) transactions to occur, as clients rely on the firm's amalgamation of industry knowledge, valuation skills, and deal-making experience to achieve their desired sell- or buy-side objective (i.e., a successful business/asset sale or acquisition). This firm-client relationship is difficult to contract due to the tacit nature of the aforementioned firm skills; as such, the ability to trust in a firm is a necessity. Clients have a lengthy list of firms from which to select when considering an M&A deal, and trust appears to play an important role for clients not only when initially selecting/retaining the investment firm but in the success of the M&A transaction itself. Thus, although the role of trust may be difficult to

precisely quantify empirically - I argue that the presence of trust in an advisory firm should appear in the performance of its clients' transactions.

After years of not being able to find evidence of a link between the choice of advisors and M&A performance, Bao and Edmans (2011) used announcement period returns to determine that there are in fact advisory-dependent factors, which they attribute to reputation, that impact the performance of a firm and the associated success of M&A transactions. Reputation is an element on which trust is built. As trust is recognized to be an important factor in corporate culture as well as in performance (Guiso et al. 2015), I believe that we can use a proxy for trust to estimate the potential effects of cultural differences between types of advisory firms. Specifically, I propose that M&A advisors at boutique advisory firms are subject to fewer conflicts of interest than those at full service. Due to their smaller size and stated focus on the maintenance of client relationships as being the key driver of business, boutiques have a greater need to maintain their trustworthiness.

While full-service banks provide a broad variety of services for consumers, and tend to be the largest players in the marker, boutique firms are more specialized and have lower levels of conflicts of interest (Song 2009). As most boutiques gain the majority of their revenues from M&A, while M&A is only a fraction of full-service revenue, boutiques have a much higher economic incentive to ensure that they are trustworthy and their good reputation is maintained. I believe that this implies that boutiques are perceived to be more trustworthy than full-service banks, at least when considering elements of M&A that are highly susceptible to conflicts of interest.

Therefore, this paper uses manually compilied information on transactions announced between 2006 and 2017 to study the effect that boutique advisory services provided to acquiring firms have on transactions. In order to calculate this effect, I examine the difference between the

announcement period returns of transactions with a buy-side boutique advisor, as opposed to those with only full-service advisors.

To further study the impact of boutiques on transaction returns, I use fairness opinions as a measure for the presence, or lack, of trust in the financial advisors ability to aid on a transaction without facing any conflicts of interests. A fairness opinion (FO) is a professional analysis as to whether the proposed price for a merger or acquisition is considered "fair." These opinions are often completed by the firm that serves as a financial advisor to the deal, and can be requested by both the acquiring ("buy-side") and target ("sell-side") companies. Alternatively, an independent firm such as a boutique M&A advisor or a consulting group may provide the opinion, as could an independent full-service bank. An FO is typically "obtained prior to the board's decision on a transaction and, consequently, prior to the deal being announced" (Kisgen et al. 2008); this timeline is the result of an FO's primary use: to protect the board from a lawsuit over the perception of the transaction being "unfair" to the shareholders. As a tool used to determine "fairness," these opinions require a great amount of trust to be perceived as unbiased.

Thus, I explore how we can see the impact of cultural differences between boutique and full-service firms through how the market responds to an FO provided for an acquiring company. Prior studies (Kisgen et al. 2008; Cain & Denis 2012; Chen 2010) show that the disclosure of a potentially conflicted FO by an acquiring company can lead to a negative impact on the transaction's announcement period returns. This announcement return estimates the potential value-add benefit of a transaction to the acquiring company, and is the most frequent measure for advisory firm performance. Therefore, this is the best current method by which we can see the effect of - and draw assumptions around - a particular firm.

Based on prior research and my own assumptions, I would expect there to be difference in response to FOs provided for acquirers by full-service and boutique firms, both when they are the primary advisor for the firm as well as when they are a third party ("independent"). Regarding independent FOs, I believe that the presence of a boutique firm would have a more positive impact than a full-service firm. For situations where the FO-provider is also the primary advisor ("not independent"), the issuance of FOs may have a negative effect on performance when disclosed, as this may increase the chance that an questionable deal (i.e., one that involves a possible internal conflict of interest) makes it to announcement, which I more fully discuss below (Kisgen et al. 2008). However, I still believe that a boutique would have an ameliorating effect on this negative impact, as the presence of greater trust in the boutiques ability to stay impartial could allow there to be negligible effect on announcement returns.

This paper contributes to the current literature in multiple ways. First, I aim to continue the research into boutique financial advisory firms, as begun by Song (2009). While discussion of the advantages and disadvantages of boutique firms exists in the news and M&A business discussion there is a large gap in academic research pertaining to these firms. Second, I posit an alternative way to understand the diversity in responses to acquirer FOs, as seen in Kisgen et al. (2008), Cain and Denis (2012), and Chen (2010). While these all discuss that the reputation of the advising firm has an impact on the transaction, as seen by the FO impact, they do not go so far as to allocate trust and reputational considerations based on the type of advisory firm.

II. Related Literature

II.A: Culture and Trust within M&A

To begin, it is first necessary to understand what I mean by "culture," and how I intend to apply the term to investment banks and boutique advisory firms. Prior research has relied on various definitions of culture. As is fitting for such a broad topic, there are a multitude of contested definitions that have been applied, mostly dependent on the discipline of study and on the organizational tier (e.g. the entire society, a particular social class within the society, an industry, a village, a company) of the group discussed. Here, I summarize the key sources that informed my definition and analysis of culture.

Within anthropology, one of the more useful concepts is to see culture as being similar to a set of control mechanisms – plans, recipes, rules, and instructions – that are necessary for the governing of behavior (Geertz, 1973). In this sense culture is something more manufactured; nurture rather than nature. Boyd and Richardson (2005) elaborate on this point, and offer additional details as to how it is inherited: culture is socially learned, passed down from person to person by way of social interactions that inform how we should make decisions, how to react, what is right, and what is wrong. This social learning is also known as the ways by which people form "common ground" through communication (Lyons & Kashima 2001), and is illustrated by humans developing shared public "meaning" (Geertz 1973).

Sociologists offer differing responses to the debate over a concrete definition of culture. It is Turco's (2010) belief that culture is a resource that people use to understand and act around their respective social positions. She makes no distinction between general culture and firm culture, instead using the term to describe the interactions people have with the various aspects of their worlds. Patterson (2014) takes this resource theory and elaborates on it, taking a more meticulous

approach and dividing the term into two different "schemata": the knowledge and the pragmatic processes, the former maintaining this same idea of meaningful shared knowledge, the latter being the interactional ways in which people use culture. Similar to Boyd and Richardson (2005), Patterson agrees that culture is something both self-regulating and internally reinforced. Ridgeway et al.'s (1998) study narrows down from the broad topic of culture to a specific value of culture - status beliefs - which evolves from the ways that cultural information is shared.

While economists and financial economists (hereafter 'economists') steered away from the topic until recent decades due to empirical difficulties, they are now taking up the equally difficult and important task of researching aspects of culture. In particular, many are researching the impact that cultural traits have on outputs such as firm organization, markets, financial performance, and public policy (Algan & Cahuc 2013). Academics in the field of economics note that culture differs from "standard" knowledge in that it is not empirically discovered nor analytically proved (Alesina & Giuliano 2015). As such, they recognize that humans are not wholly rational, make necessary simplifications for the sake of scientific estimation, and understand that what they find will not be able to explain the whole of reality. Therefore it is important to note that to evaluate the effects of culture, economists are taking something that is rooted in theory and loose technical definitions and trying to find precise results, leaving ample room for error.

For my thesis, I rely on an amalgam of the economists' and sociologists' approach. At its core, culture is a set of values, beliefs, and skills that determine our behavior, and is evolutionarily developed in response to human forces. In this paper, I will adopt a definition of culture that is similar to Boyd & Richardson (2005), Blair & Stout (2001), and the above literature: culture is shared information – our values, beliefs, and skills -- that are taught through social learning. The context of this learning is the "individuals perceptions of others' motivations, beliefs, likely

behaviors, and relationships to others" (Blair & Stout 2001). This approach is also consistent with Alesina and Giuliano (2015) and Morrison and Shapiro (2015).

To feasibly study culture through use of this definition, it is necessary to apply it to a narrower group of people. Within financial economics this is usually done through the study of corporate culture: how culture can be developed and analyzed within a specific company or a range of companies, and how we determine its importance. From my research, one of the more common measures used in the empirical estimation of culture is trust (Algan and Cahuc 2014; Blair & Stout 2001).

When it comes to the firm, Guiso et al. (2015) discuss integrity and trust as aspects of firm culture that affect performance. This is supported by Turco (2012), Lyons et al. (2007) and Blair and Stout (2001) in their explanations of culturally determined performance. As examined by Turco (2010), culture is a strong force within the firm and should not be disregarded. Despite economic theory, humans are not wholly rational nor efficient beings and as such make decisions based on a culturally-informed feeling of trust that is created by the ways in which we understand the current situation and our relationship to it.

Similarly, individual or cultural biases can influence firm decision-making such that otherwise rational decisions will be affected. A famous example of this is how job applicants are more likely to be hired if they have a contact within the firm, or if they meet certain characteristics, such as being a former athlete or having children, that are assumed to demonstrate work ethic and potential for longevity within the firm. Those hiring look at all potential applicants and, absent any work-related distinctions between them, decide to hire the person that they think has the best "fit," thus impacting the employee make-up of the firm (Turco 2010).

Another comparable factor affecting investment bank culture is the extraordinary network-based nature of the industry. Comprehensive studies such as Pak's *Gentlemen Bankers* focus on the complicated relationships and networks that historically define the world's top investment banks (Pak 2012). Her analysis shows how social learning and interactions within this industry are primary building blocks of firm culture.

Lyons et al. (2007) assess how specific culture in investment banks can lead them to innovate and continue to be successful, and that it is "best practice" to have strong client trust and interaction. Similarly, Blair & Stout's (2001) research into corporate behavioral theory provides a solid link between a trust-based culture and potential outcomes. To determine if "people do not trust randomly," they experimented on the social context in which people make their decisions, where researchers were able to artificially create situations of either trust or the absence of trust. They observed that these trust or no-trust situations led to either "competitive and self-regarding" or "cooperative and other-regarding" responses. Blair and Stout (2001) therefore found ample empirical evidence that there exists a set of characteristics beyond the idea of the economic, self-interested human which governs and sustains our performance and behavior: trust, and social context. I use their definition of social context to inform firm culture: the "individuals' perceptions of others' motivations, beliefs, likely behaviors, and relationships to themselves."

From here, a variety of additional studies have experimented with whether performance can be culturally determined. First, there are multiple ways of delineating the bounds of this culture. Bany-Ariffin et al. (2014), Gianetti and Yafeh (2012), and Gianetti et al. (2014) study cultural differences in firms along national lines. Others, such as Guan et al. (2012) and Guiso et al. (2015) look to define overarching themes of all corporate culture. The financial sector as a whole is examined in Morrison and Shapiro (2015), with investment banking in particular being discussed

in Morrison and Wilhelm (2015) and Chemmanur et al. (2012). Narrowed down even further, Bao & Edmans (2011) and Golubov et al. (2012) compare the M&A divisions of all investment banks, while Song (2009) makes comparisons between M&A boutiques and full-service firms.

Turning to investment banks, and M&A in firms in particular, it is key to understand how firm culture has an impact. As with most industries, investment banks are well known for having uniquely identified internal cultures. A primary source of differentiation among the diverse investment banks has so far been largely based on their cultural differences (Eccles & Crane 1988; Lyons 2007). As all such firms essentially provide quite similar services, each firm strives to establish its uniqueness. This leads to the individualization of corporate culture via the delineation of certain company principles, which are normally a mixture of publicly known and in-house conventions that are primarily communicated down the pecking order (Kreps 1990). Cultural principles within investment banks include organizational structures and processes such as behavioral norms, socialization, and knowledge sharing (Lyons 2007). While specific aspects are certainly developed by entry-level workers, it is the hierarchically senior personnel that have the most at stake in terms of reputation. For example, senior bankers spend a vast amount of time and effort building relationships of trust with their clients and industry members. As a result, they are the ones establishing the largest portion of corporate culture by virtue of how they exercise authority. Investment banks, as organizations that are well known for their strict hierarchies, are especially susceptible to this circumstance.

Reputation, or faith, is by definition the "beliefs or opinions that are generally held about someone or something,"[1] and is key to first gaining a client and then maintaining that relationship. It affects a customer's decision whether to enter into a transaction, especially one that would not

[1] Oxford Dictionaries [or https://en.oxforddictionaries.com/definition/reputation [last accessed 12/23/2017]].

otherwise occur due to the high level of associated costs (Kreps 1990). Within a bank, advisors have a significant incentive to build a reputation for trustworthiness (Chen et al. 2015). This trust is one of the key socially contingent phenomena that results from the reputation of a firm, as it encourages both cooperation within firms as well as between agent and client (Blair & Stout 2001; Algan & Cahuc 2013). While trust and reputation are not necessarily equal, the appearance of the former can lead to large impacts on the latter. It is Kreps' (1990) belief that trust and faith are what permit mutually beneficial transactions to occur.

Unlike other forms of financial business, such as securities trading, it is impossible to put all of the considerations that go into a transaction into a contract; in essence, the client is at the mercy of its M&A firm – which has the financial expertise and ability to synthesize essential information that are critical to successful acquisitions. There are so many variables at play that the client must simply be able to believe its bank has its best interests in mind. In effect, the client is trusting the bank to have complete market sector familiarity, conduct appropriate due diligence on the target business (including identifying known and foreseeable transactional risks), be aware of the short-term and long-term financial prospects for the target's services/products to accurately assess its value, and give good advice on pricing. Thus, a reputation for being trustworthy is instrumental to the long-term success of client relationships, especially if a firm wants to retain the client beyond the point of individual banker turnover. Prior research mapped onto the industry shows that without trust in the firm, conflict will replace agent-client cooperation, along the fault lines where trust breaks down (Boyd & Richardson 2005).

Despite this need for trust, Chen et al. (2015) focus on how concerns of a bank over its reputation are no longer sufficient to prevent banks from exposing themselves to conflicts of interest that appear as the scale, scope, and complexity of the institution increases. Within M&A,

conflicts of interest are an unfortunate (but not uncommon) circumstance that can undermine the structures of trust and reputation that the firm aims to build. Nonetheless, these conflicts are an inherent result of the broad range of services that many advisory firms provide to a spectrum of clients. Investment banks – particularly full-service firms – often operate by building relationships with parties on both sides of the transaction. For example, it is possible that a banker could provide financing to the acquirer while serving as sell-side advisor to the target, as seen in the case of the Royal Bank of Canada, Warburg Pincus, and Rural/Metro. Alternatively, Guan et al. (2012) analyzes the effects of recent SEC reforms on the conflicts of interest faced by investment bank analysts. Specifically, it points to the placement of research departments under the same roof as investment banks, as seen in full-service banks, as a key conflict.

Firm culture can lead to a variety of negative effects on performance. Liu (2016) studies how corrupt corporate culture in banking can lead to an increased amount of corporate misconduct. By measuring the "average corruption attitudes" of corporate decision-makers, he determines that there is a significant positive relationship between a corrupt culture and misconduct, such as "earnings management, accounting fraud, option back-dating, and opportunistic insider trading". Similarly, Morrison and Shapiro (2015) comment that socially undesirable firm behavior can negatively impact economic efficiency, and thus performance, of a company. They contend that these "bad cultures" emerge when leadership of the firm transitions from historical management, which prioritizes certain cultural artifacts which are no longer compatible with the values of new management. As such, the cultural incompatibility within a bank led to conflicts within the firm, which fosters inefficiencies and bad performance.

II.B: Comparison of Buy-Side Advisory Firms and Measurement Tools

In recent decades, certain investment banks have been able to corner large portions of the market for M&A services. While this is somewhat tied to the large scale and scope of modern-day investment banks and full-service banks, boutique M&A firms that gain a share of the market appear to do so because of their capacity for strong client relationships through trust and sterling reputation. In order to study this situation further, I compare boutique to full service banks with the assumption that the cultural differences between these two types of firms would be visible through statistical analysis

Boutiques make up two of the top ten M&A firms in terms of revenue on current league tables, and are currently on trajectory to continue their growth in the M&A market.[2] Additionally, top-tier boutiques may out-earn other investment banks, as they take in a smaller deal flow but can charge the highest rates in the industry due to their expertise.[3] Despite this, there is limited academic research on the choice between a boutique and full-service advisory firm. There are marked differences between the two: boutiques are smaller with a narrower focus, specializing in M&A and client relationships, while full-service investment banks are dramatically larger and can offer deal financing and earn the majority of their earnings outside of M&A across a variety of sectors. As a result, full-service banks face an interesting situation: they have a broader network that allows them to take in more clients, but they do so while facing significant conflicts of interest as a result of the contradictions that arise from housing many services with different values under one roof.

An example of a key conflict of interest in full-service banks is the sway that other divisions can have over M&A advisory. It is common for parties outside of the advisory division to

[2] Financial Times 1H 2017 league table
[3] Financial Times, "Boutique advisors crash M&A league table thanks to high fees", July 5, 2017

pressure M&A advisors to suggest that their clients make acquisitions, even if it not in the client's best interest, simply to increase the numbers of deals closed by year-end.[4] Additionally, the advisor might ignore warning signs of a bad transaction since almost all fees received by the bank are contingent on the deal closing. Furthermore, if someone that favors an arms-length approach leads the bank, there will be inherent conflict with the relationship-based nature of M&A advisory. They might not care as much about the reputational impact of a bad deal, as to them it is less crucial to maintain relationships, and the impact would be mitigated by the performance-based strength of trading or brokerage divisions.[5]

Chen, Morrison and Wilhelm (2015) suggest that one way to solve these conflicts within full-service banks would be to spin off advisory services into boutique firms. By keeping advisory separate from easily-contracted and arms-length divisions such as trading, bankers are better able to provide unbiased advice more appropriate for their clients. This belief is supported by statements made by bankers who left a full-service firm in order to found a boutique. In the 2006 announcement for the formation of Centerview Partners, founding partners Stephen Crawford, Robert Pruzan, and Blair Effron all cite concerns over client relationships as a driver to spin off and form a boutique. From their perspective, the boutique would allow them the opportunity to be "partners" with their clients and focus on the clients' long-term strategy, whether or not there was a transaction on the horizon.[6]

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[4] Philip Keevil (investment banker with 35+ years experience at both full-service and boutique banks) in discussion with the author, April 2018. States that one reason for this "is that there is a drive to get a bank's name attached to as many deals as possible by end of year in order to influence League Table rankings."
[5] Philip Keevil in discussion with author, April 2018.
[6] Centerview Partners formation announcement [or https://www.prnewswire.com/news-releases/three-senior-wall-street-professionals-announce-formation-of-centerview-partners-55979567.html [last accessed 4/18/2018]]

It is believed that boutiques have seen a marked increase in relevance because of two reasons: Due to past SEC reforms (e.g. Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, P.L. 111- 203 (2010) [also known as the "Volcker Rule"]) and/or the financial crisis of the late 2000s, working with large full-service banks became less attractive due to their heavy regulation to mitigate volatility and financial exposure risks; and second, senior bankers increasingly were dissatisfied with the organizational strictures of large firms. Both factors have contributed to senior bankers leaving to join or start a boutique firm, where they can have fewer conflicts with the vast full-service web (e.g. the securities trading or DCM divisions) while maintaining a large amount of their strong client relationships. The emergence of increasing numbers of boutiques may also be a result of other SEC reforms that have clarified that boutique firms may be exempt from certain SEC rules on M&A transactions (e.g. SEC M&A Brokers No-Action Letter, January 31, 2014).

To test my hypotheses about differentiating performance factors between boutique and full-service firms, I draw upon prior research and the metrics developed in recent studies of firm culture and performance. From my research, one of the more common measures used in the empirical estimation of culture is trust (Algan and Cahuc 2014; Blair & Stout 2001). As I briefly explained earlier, prior research has drawn a tentative link between culture (sometimes through "trust") and performance. For example, Algan and Cahuc (2014) used surveys, experiments, and multiple other measures to determine a causal relationship between trust and growth, similar to how Guiso et al. (2015) used employee survey response to the Great Place to Work Institute (GPTWI) to determine that firm performance is stronger when employees perceive managers to be trustworthy. While useful for understanding large trends and for getting clear answers around people's beliefs about trust, the survey method is dependent on availability of surveys, response

rate, and interpretation, and as such are not the best method to consider for both a shorter study as well as one on a particularly secretive industry.

Examining another angle of the corporate culture, Kolastiski (2001) and Liu (2016) both study potential conflicts of interest that can emerge in companies. Liu constructed a firm-level measure of corporate culture that was based the GPTWI's survey on the average corruption attitudes of company employees. Kolastiski, on the other hand, took data on analyst affiliations with acquirers to find evidence that affiliations (conflicts) were likely to affect analyst recommendations.

Additional studies define firm culture along demographic (Leonard & Levine 2006; Turco 2010) or geographic lines (Giannetti 2012), and use the respective make-up or location of the firm to draw conclusions about the place of culture within companies. Turco (2010), like many others, used interview sample analysis to compile data on firm culture. From there, she compared findings from across her sample to establish her theories of tokenism within leveraged buy-out (LBO) firms, as a contribution to the study of cultural inequality within the workplace.

Based on these examples, as well as additional research, I use the appearance of trust as a measure for cultural differences between boutiques and full-service firms. According to Perella Weinberg Partners' Business Principles: " 'I Trust You' is the highest compliment we can receive from an advisory client, an investor, or a colleague" (Clayton and Malik 2011). As this commitment to trust is a key differentiator between boutique and full-service firms, I aim to see the effect that this trust has on transaction performance. Furthermore, I use fairness opinions provided by these types of firms as an independent variable to explain acquisition performance of their respective transactions. I presume that once I control for other variables, the effect of an FO on a transaction's performance can be ascribed to the strength of the trust the market has in that firm's

ability to fairly present an opinion. For example, a risky transaction that obtained an independent FO will perform better than the same transaction with an FO prepared by a conflicted advisor.

Based on the literature, the standard measure for estimating the effects of an advisory firm on M&A performance is announcement returns, estimated using either 5-day or 3-day cumulative abnormal returns (CARs) (Bao & Edmans 2011; Bany-Ariffin et al. 2014; Song 2009; Kisgen et al 2008; Chemmanur et al. 2012). Guiso et al. (2015) used return on sales and Tobin's Q as stand-ins for performance, while Brune et al. (2012) used post-acquisition stock data for the acquiring company to study performance, relying on the change in return on assets (ROA) and change in return on equity (ROE).

It is assumed that announcement returns reflect the value added by the acquisition to the acquirer. Calculating the cumulative abnormal returns around the announcement date allows us to determine the reaction of the stock market to the acquisition, and thus interpret that response. Prior studies believe that in the absence of other information about the acquisition, the market will use its knowledge and perception of the advising companies to estimate the value of the acquisition (Chemmanaur et al. 2012). This could be dependent on the level of experience of the investment banker, as seen in Chemmanaur et al. (2012), or it could instead signify the impact of firm reputation, most often measured by market share (Bao & Edmans 2011) or by prior performance of the firm (Golubov et al. 2012). It is likely that multiple of these firm-related variables are captured in cumulative abnormal returns (CARs).

II.C: Background on the Use of Fairness Opinions

A fairness opinion is a professional analysis done by a firm as to whether a merger, acquisition, privatization, buyback, or spin-off of a company is considered "fair." FOs are not

required by law, but are recommended according to legal precedent as a measure to protect the board of a target or an acquirer from a shareholder lawsuit under the accusation that the transaction price was "unfair" to that party. Here, "fairness" is defined from a financial standpoint: does the advisor's valuation fall within a range of values that are appropriate given the target and the transaction's financial considerations (Davidoff et al. 2011). FOs emerged from the Delaware Supreme Court ruling in *Smith v. Van Gorkom* (1985), whereby the board of the Trans Union Corporation was found to have made an uninformed business decision in the completion of an acquisition that breached the board's duty of care. Through the interpretation of both the opinion and the court's response to the Delaware statute used in Trans Union's defense, it was implied that the valuation was vague and needed an additional FO, and that this would potentially satisfy the court as a defense. (Davidoff et al. 2011). While not necessarily the best practice, it is the most common solution for preventing potential litigation over valuation concerns.

Although the Trans Union litigation was brought by the target's shareholders, similar types of litigation have arisen through cases brought by acquirer shareholders. Buy-side litigation – which is more directly relevant to my proposed thesis since I focus on the buy-side effects of FOs – is most often a response to large deal losses as a result of the acquirer over-valuing the target company (Moeller et al. 2005). One example is the HP acquisition of Autonomy, whereby HP and Autonomy executives were sued by HP shareholders on account of allegedly ignoring numerous due diligence red flags, such as "accounting improprieties, . . . concerns about Autonomy's finances, . . . [and] the enormous amount of goodwill and intangible assets HP was forced to book as part of the Autonomy acquisition." Despite these flaws, HP continued with the transaction and offered a 64% premium over Autonomy's market price the day before announcement. In the end,

HP would write down $8.8bn in goodwill a year after the acquisition, resulting in stock plummeting and shareholders bringing the acquirer to court (*Riccardi et al. v. Lynch*, ¶3).

Due to these types of concerns, about a third of acquirers and the majority of target companies obtain FOs. More specifically, of Kisgen et al.'s (2009) sample dataset from 1994 to 2003, 80 percent of the targets and 37 percent of acquirers obtained FOs. Meanwhile, Cain and Denis' (2012) 1998 to 2005 sample showed disclosure of opinions by 96 percent of the targets and 28 percent of acquirers. The disparity in responses could imply that the number of targets that request an FO has increased over time, while acquirers have done the opposite and less frequently requested an opinion. However, this could also be a result of the differences in standards for determining the sample, and is likely also affected by changes in Securities and Exchange Commission (SEC) law. For example, the SEC began to require that all FOs be disclosed in a transaction's proxy statement in the mid-2000s, implying that there might not have been total disclosure before this point. Regarding the large gap between targets' and acquirers' disclosure of FOs, Cain and Denis (2012) acknowledge that this discrepancy is likely a result of the prominence of litigation against the board by shareholders of target companies, while acquirers less often need the approval of their shareholders to complete a transaction.

On the acquirer's side, the FO is really a device to help the transaction go forward – an assurance that the price of the deal for the shareholders was fair. Additionally, when an FO has been provided for a target company, then the acquirer may believe there is less cost-benefit value to completing an FO. However, there are certain risky situations where an acquirer is more likely to undergo an FO, as explained in Kisgen et al. (2008). The larger the size of the transaction, the more likely an acquirer is to disclose an FO, implying that the board does have stricter approval requirements when they have to put more on the line. Alternatively, when an acquirer, due

potentially to corporate governance policies, has reason to be cautious of shareholder concerns over conflicts of interest, then its board is more likely to pay for an FO (Kisgen et al. 2008). For example, if a target is being bought in a friendly, non-arm's length acquisition, then there is the potential that the acquirer is not paying market value for the company, which could bring scrutiny onto the acquiring company's board. Furthermore, as I noted in the HP-Autonomy case, the board should take notice if the acquirer offers too high of a premium for a target, as this could be an example of reckless behavior.

Prior studies have come to a few interesting conclusions regarding FOs. The first is that the use of a non-independent FO by an acquiring firm has a significant negative impact on the return outcome of the deal, as measured by announcement returns (Kisgen et al. 2008). On the other hand, according to Kisgen et al.'s (2008) "Transaction Improvement" hypothesis, the reputation of the advisor providing the FO has a positive effect on announcement returns. Thirdly, there is no current evidence that "unaffiliated third-party investment banks provide valuations that are more accurate than affiliated advisors" (Cain and Denis 2012). Here, the measurement for accuracy was done by comparing the FO-predicted change in acquirer shareholder wealth to actual shareholder wealth changes. Yet, there is still research showing that an independent FO can have a higher announcement return than a non-independent one (Chen 2010). This would imply that there is a factor beyond simple accuracy that causes transactions with independent FOs to perform better than those with non-independent FOs.

Additionally, the negative impact as seen by Kisgen et al. (2008) is more significant for the "one advisor, one FO" structure, with the acquirer's primary advisor also providing the FO, than for a multi-advisor structure (defined by Kisgen et al. as two advisors, with at least one completing a FO). This implies that the market reaction to the appearance (and assumed necessity) of an FO is

made worse by the perception of the one-advisor conflict of interest bias. Therefore, I believe that the one-advisor agency bias, as well as some other trust measure, is at the core of why the market reacts more negatively to some FOs as opposed to others.

At the same time, FOs have faced their own scrutiny as their efficacy has come under question: despite being used to mitigate concerns about conflicts of interest, FOs are also exposed to a large amount of conflict of interest. The primary concern is that if the same primary advisory firm is doing the FO, that firm may get an additional fee contingent upon the transaction closing, instead of just a flat fee for the opinion (Marshall 2007). This situation implies that there might be a difference in the value of FOs depending on the type and relationship of the firm that completes them.

A common critique of FOs is the idea of "rubber-stamping": that the valuation range may be too wide, and thus ineffective at truly determining whether the transaction should proceed. Additionally, acquirer-side FOs may be more likely to exhibit a positive bias towards a FO, while the target FO is more likely to have negative bias in relation to the offered price of the transaction (Cain & Denis 2012).

As noted above, the threat of litigation can also be a factor influencing the completion of FOs. Litigation over M&A transactions reached an all-time high in 2014, with 94.9% of these deals leading to lawsuits (Cain and Davidoff Soloman, 2016) (although most appear to have involved claims by the target's shareholders). From here, it could be assumed that we had reached a steady state where all transactions would eventually lead to litigation, a state that was heavily critiqued for its frivolity in Fisch et al. (2015). As a result, the Delaware Courts have made striking efforts to discourage suits by making it more difficult for disclosure-only settlements to pass through courts. Specifically, the courts are limiting the types of settlements that commonly give a

fee award to the plaintiffs' counsel, but have no substantial benefits for shareholders. This has led to a decline in the amount of transactions that experience litigation (87.7% in 2015). It is yet to be determined what litigation rates will stabilize at, and how the courts' recent efforts to curtail litigation will affect the prevalence of FOs.

III. Hypothesis Development

It is generally accepted that boutiques face fewer conflicts of interest than full-service banks. Boutiques even publicly state that being free of conflicts of interest allowed them to provide trustworthy, unbiased advice, giving them a competitive advantage over their competitors[7]. I believe that these conflicts of interest have a negative impact on the levels of trust that the market holds for full-service versus boutique banks. As such, I analyze the effect that a boutique firm has on acquirers' announcement returns. As an additional tool in measuring the trust present in both boutiques and full-service firms, I also study the impact of boutique-provided FOs.

The overarching hypothesis is that the addition of a boutique firm as a buy-side advisor will increase the announcement period return of the transaction ("Improvement" hypothesis). Here, the boutique is assumed to be chosen as a buy-side advisor in order to improve the otherwise precarious nature of the transaction. In this situation, the acquirer predicts that there could be a shareholder dispute, and is using the boutique to ensure that there are no apparent advisor conflicts. To explore this concept further, I consider the use of buy-side FOs in a transaction with boutique advisors. These hypotheses are not mutually exclusive from the main hypothesis; rather, they supplement it through the study of FOs.

[7] See Perella Weinberg Partners 2011 HBS Case by Rose and Malik. See also Moelis home page and business statement, which has the slogan: "A global independent investment bank providing unconflicted, strategic advice to a diverse client base".

The second hypothesis is that if a boutique firm, as compared to a full-service firm, is both the advising firm and the source of the FO for an acquiring company then there will be a different effect on announcement returns ("Reliability" hypothesis). The interpretation of this is that a non-independent FO causes a negative announcement return, but the boutique would have a positive impact on the FO as compared to a full-service bank. As seen in Kisgen et al. (2008), the disclosure of an FO can negatively impact announcement returns. This is additionally impactful when considering that acquiring companies are less likely than targets to have an FO since the boards are not as at risk. If an acquirer requests an FO, it could be signifying that there is something about the deal that would seem wrong. Therefore, I am not certain that even a boutique providing a FO would cause there to be a positive impact on announcement returns. The results of this analysis would imply whether boutique firms are overall perceived to be more trustworthy, or less exposed to conflict, than full-service firms. However, I anticipate that it may be difficult to measure a significant difference, because a confounding factor/variable is whether the FO is provided by the same firm or an independent advisor.

My third hypothesis is that buy-side fairness opinions issued by an independent boutique firm will have a more positive effect on announcement returns than one issued by an independent full-service bank ("Outsider" hypothesis). Based on Kisgen et al. (2008) and Chen's (2010) findings, an un-conflicted, independent opinion is likely to improve the announcement returns of a transaction. As I have discussed, I believe that boutiques are more able to avoid conflict than full-service banks due to the nature of their businesses. Thus, when comparing the transaction returns of an independent full-service FO versus an independent boutique FO, the boutique FO should produce higher positive returns.

IV.A: Description of Data

I began by collecting my sample of transactions from the Thomson Financial Securities Data Company (SDC) mergers and acquisition database. The initial sample included both successful and unsuccessful transactions from January 2006 to December 2017 categorized as a merger or acquisition. I excluded all deals where the acquiring stake was less than 50%, as well as all deals below $10 million. There needed to be at least one easily identifiable advisor for the acquiring firm and the advisor must be clearly categorized as a full-service, boutique, or other (consulting firm; in-house deals) firm. Additionally, both acquirers and targets must be both public and covered in the Center for Research in Security Prices (CRSP) database to calculate cumulative abnormal returns.

I furthered narrowed the sample by implementing a requirement based on the transaction advisors. At this stage, I created a ranked list of advisors based on both number of deals done and the average transaction size of those deals, and divided this list into either full-service or boutique classification. I then sorted through the sample using this list, keeping only transactions where one of the advisors was ranked as a top-10 full-service or boutique firm (see Table 2 for Bank List). This was done with the assumption that top-ranked firms would have the greatest amount of bearing to the question of full-service and boutique cultural & reputational differences.

Financial and return data for the transaction parties was collected from Compustat and CRSP. Data regarding fairness opinions was collected both from SDC as well as a manual search, as it has been found to sometimes be an unreliable source. Specifically, for each transaction without FO information given by SDC, I used the SEC's EDGAR filing system to search for DEFM14A (the merger proxy statement) where FOs are required to be disclosed.

To measure the creation of value, I rely on acquiring firm returns as reported by CRSP. For each transaction, I calculate either the 3-day (-1, +1) cumulative abnormal return (CAR) using the CRSP value-weighted index return as the market return, for which the estimation period will be 181 to 22 days prior. The abnormal return will be the difference between the acquiring firm's return and the expected market return, which is calculated across the announcement window and then summed.

After applying all selection criteria, the final merger sample included 846 M&A transactions. Table 1 and Table 2 display the frequency of sample transactions according to year and acquirer advisor (note: one transaction may have multiple advisors). Table 3 further summarizes the merger sample. Of all of the transactions included, 206 involved a boutique firm (*Boutique*); in 57 of these cases, the boutique was the sole advisor to the acquiring firm (*Boutique_Sole*), while in the other 149 the boutique was one of multiple advisors to the transaction (*Boutique_Multi*). Additionally, each transaction had at least one and up to nine buy-side financial advisors. If the acquirer had a fairness opinion, there were between one and three FOs disclosed. [8]

225 of the 846 transactions involved a buy-side fairness opinion, or 26.6%, which is consistent with Cain & Denis's (2012) sample and less than Kisgen et al.'s (2009). Of these 225, only 71 had a boutique advisor complete an FO, 13 of which were as the sole advisor and the other 58 as one of many advisors. The low number of sole boutique-provided FOs could be explained by concerns over reputation impact. As I discussed with Philip Keevil, he believes that there is a strong risk associated with providing a fairness opinion in that, if the deal is eventually contested

[8] When a deal has multiple advisors, the deal is credited to each advisor separately, as seen in Bao & Edmans (2011)

and deemed unfair there can be strong reputational impact on behalf of the advising firms. While larger full-service banks are able to weather dips in clients and/or deals, it can be extremely difficult on boutiques, which are more financially constrained by their lack of commercial lending or large-scale sales & trading divisions. To this end, Keevil posited that few boutiques may be willing to be both the sole advisor to a transaction and a provider of a fairness opinion, as the blame for a faulty deal could fall on their shoulders.

Table 4 shows summary statistics based on the variety of advisor and FO structures that I employ in my regressions. Transactions with boutiques and transactions with fairness opinions tend to have a larger deal size than those done by full-service firms or without an FO. Looking at the *Boutique_Sole* and *Boutique_Multi* variables, the sample shows that a full-service bank is more likely to solely run a larger transaction than a boutique firm. However, boutiques take part in syndicates in much larger deals than those that are exclusively full-service. In scenarios where boutiques perform FOs, the deal size is on average smaller than when a full-service bank provides the FO.

Other characteristics of note are relative size, related industry, average premium, and hostile transactions. As expected, acquirers tend to be much larger than the targets they acquire. This tendency is exaggerated when a single buy-side advisor as opposed to a syndicate of advisors leads the transaction. Combined with the fact that syndicates work on larger deals, this shows that more complicated transactions with larger parties at stake are more likely to have multiple advisors. Additionally, the vast majority of transactions in the sample are between companies of related industries. The only instances where there is a noticeably different percentage are in the *BoutiqueFO, BoutiqueFO_1* and *BoutiqueFO_Multi* variables. In these cases, the transactions with a boutique FO were more likely to be from different industries than transactions with only full-

service FOs. Lastly, consistent with prior literature, acquirers request FOs in transactions with much higher premiums than those without FOs. The presence of a majority stock consideration also seems to indicate the use of an FO.

The hostile variable is especially interesting. In prior studies (Kisgen et al. 2008) the use of FOs were correlated with friendly transactions. The reasoning for this was that hostile transactions should be more open to market pricing, while friendly transactions could have a price that is influenced by company relationships and therefore conflicted. Similarly, in Song's (2009) sample, full-service banks were more likely to advise on hostile transactions than boutique firms. However, in my sample there is the opposite correlation – transactions with FOs are more likely to be hostile than friendly, as are transactions with buy-side boutique advisors.

IV.B: Empirical Tests

The primary variable to conduct the regression analysis are the CAR returns of each transaction. This dependent variable, *RET*, represents the performance of the transaction as measured by its announcement returns (the CARs). To determine the validity of each hypothesis, I alter one explanatory variable per hypothesis while holding the rest of the explanatory variables constant. The three least squares (OLS) regressions I use are:

$$RET_{i,t} = \alpha_t + \beta_1 * Boutique_{i,t} + Control\ variables + \varepsilon_{i,t} \quad (1)$$

$$RET_{i,t} = \alpha_t + \beta_1 * BoutiqueFO_{i,t} + Control\ variables + \varepsilon_{i,t} \quad (2)$$

$$RET_{i,t} = \alpha_t + \beta_1 * BoutiqueFO\_Sole_{i,t} + Control\ variables + \varepsilon_{i,t} \quad (3)$$

The second OLS regression (2) will assess the reliability hypothesis through the use of the *BoutiqueFO* variable. This explanatory variable is a binary variable that equals one if the acquirer's primary advisor provided an FO and was a boutique, with the variable equaling zero if this firm is full-service. If my hypothesis is correct, this coefficient should be positive. The third

equation (3) tests the outsider hypothesis. The primary explanatory variable, *BoutiqueFO_Sole*, is a binary variable that equals one if the acquirer had an independent boutique complete an FO and zero if an independent full-service firm completed the FO. According to the outsider hypothesis, I also expect the coefficient of this variable to be positive.

The decision making process for which control variables I would use was affected by a self-selection problem: the use of a boutique firm and the use of an FO are endogenously determined by merging firms, and have historically been correlated with characteristics of the firms and the transaction. To control for this self-selection endogeneity, I run both ordinary least squares (OLS) regressions and a two-stage procedure, as seen in Maddala (1983) and used by Kisgen et al. (2008), Song (2009), and others. This two-stage model consists firstly of a treatment equation, followed by a regression equation on the announcement returns of the transaction. The primary difference between this model and OLS is that the two-stage takes into account a hazard rate that augments the binary dummy variables that I use in the equations. In the first stage of the two-stage procedure, I run probit regressions determining which variables have an impact on the use of an FO or a boutique on the acquirer side. As in Kisgen (2008) I assume a treatment where there is an unobservable underlying variable, *USE**, which determines whether a firm obtains an FO/boutique, where the rule is that *USE** is greater than zero if an FO/boutique is used by the acquirer. If Z_i denotes a "column vector that predicts whether a firm obtains an FO, the first stage treatment rule is given by":

$$USE_i^* = \varphi Z_i + u_i \qquad \text{(i)}$$

In order to calculate the hazard rate, h_i, I first estimate the probits of the first equation, $\Pr(USE_i = 1 \mid Z_i) = \Phi(\varphi Z_i)$, using these estimates to compute $h_i = \phi(\varphi Z_i) / \Phi(\varphi Z_i)$, if $USE_i = 1$, or $h_i = -\phi(\varphi Z_i) / \{1-\Phi(\varphi Z_i)\}$, if $USE_i = 0$, given that ϕ is the density distributive function and Φ is

the cumulative distributive function of the standard normal distribution. Next, I run a second stage regression on the variables that have been shown to have a significant impact on announcement returns:

$$RET_i = \alpha + \beta X_i + \gamma USE_i + \lambda h_i + \varepsilon_i \quad \text{(ii)}$$

Therefore, through the use of this two-stage treatment procedure I am able to account for endogeneity via the variables that have been shown to impact announcement period returns, while also including a hazard rate which contains the key differences in the FO & boutique dummys between this procedure and the OLS equations.

An additional consideration is the potential for measurement error in CAR: as discussed in Edmans and Bao (2011), if the transaction is leaked before its announcement date, then there will be an underestimation of the effect of the transaction on the acquirer's 3-day CARs. This would lead to a compounded effect over time.

Empirical Tests on the Use of Boutiques

Table 5 presents the results from the OLS regressions with the 3-day announcement period returns as the dependent variable and the use of a boutique as the main explanatory variable[9]. Columns 1-3 focus on the power of the individual boutique explanatory variable, while controlling for year and bank fixed effects. In Column 1, I found that transactions with at least one boutique firm as a buy-side advisor has 2.2% higher returns than those with only full-service advisors. To explore this further, I divided the sample into transactions with only one advisor and transactions with two or more advisors. In Column 2, I test the sole-boutique explanatory variable. This had

[9] Following Bao and Edmans's (2011) research, I've included a fixed effect variable for the investment bank as a control. This, along with a year fixed effect, was added in order to capture potential omitted variables.

very low explanatory power on the CARs[10], showing that the relevance of the *Boutique* variable was not a result of the boutiques being higher quality than full-service firms on an individual basis. However, in Column 3 I test the significance of a boutique in a multiple-advisor scenario and find that the presence of a boutique is highly significant when it is one of many advisors.

In Columns 4-6 I test the strength of the boutique explanatory variables when controlling for multiple variables. I find that a transaction with at least one boutique buy-side advisor has an announcement return 2.78% higher than transactions with no boutique advisors. Again, I find that the source of this effect comes from cases with buy-side advisory syndicates, where syndicates with a boutique have returns 2.53% higher than those without. I find that in both Columns 4 and 6, the variables for acquirer size, stock, and target sales growth are significant, while target ROE is significant only for Column 4 and the variables for hostile and high premium are not significant. I found a surprisingly high R-squared for Columns 4-8. Despite not being statistically significant in these regressions, a large amount of explanatory power comes from the *HighPremium* variable, which is why I believe it to be a valuable indicator and a variable that should undergo further study.

Lastly, I use the *CommercialBank* variable to test whether or not the use of a boutique as a supplement to a syndicate was affected by whether the full-service banks used to be commercial banks. If so, this could explain if boutiques are being used for their long expertise in advisory services, since commercial banks, in a manner, are still "new" to the game. However, I was not able to find any distinguishable difference when controlling for the presence of a commercial bank.

I also employ a two-stage treatment procedure in order to control for endogeneity in the selection of a boutique advisor. This procedure is outlined in Table 6, where I first run probit

[10] Additional regressions with *Boutique_Sole* were run with using fixed effects and additional controls. As these variables failed to make *Boutique_Sole* significant, these tests were not reported.

regressions for each boutique variable and then use the results from these estimates to calculate a hazard rate, which augments the regressions in step 2.

IV.C: Empirical Tests on the Use of FOs

In Table 7 I present the results from the OLS regressions with the 3-day announcement period returns as the dependent variable and the use of an FO by an acquirer as the main explanatory variable. Columns 1-4 are run with only one explanatory variable each, plus the fixed effects for year and bank. In Column 1, I test the raw impact of a fairness opinion on CARs and do not find a significant effect. Therefore, in Column 2 I use the variable *BoutiqueFO*, which delves into the acquirer FO and indicates whether a boutique or a full-service bank provided it. While this variable creates significance, it also had a very large impact on the R-squared of the model, which rose from 0.035 to 0.32.

Similar to how I tested the boutique variables in Table 5, I further split *BoutiqueFO* into variables based on whether the transaction was led by one or multiple buy-side advisors. Reiterating the *Boutique* findings, once I control for transaction variables, the source of the significance in *BoutiqueFO* is in multiple-advisor syndicates as opposed to a sole boutique advisor that also provides an FO. Looking at both Columns 5 and 7, the coefficient of the *BoutiqueFO* and *BoutiqueFO_Multi* variables is striking: -7.78% and -6.58%, respectively. This would mean that rather than improving returns, the presence of a boutique-provided FO actually has a strong negative impact on transaction returns.

There are different variables that make up the regression controls in Table 7 than in Table 5. Deal size is used instead of acquirer size, and the variable for hostile transactions is taken out and replaced with the variables for toehold, related transaction parties, Target M/B and Acquirer M/B. Stock, High Premium, Target ROE, Target Sales Growth are included in both sets of

regressions. Again, the presence of a high premium had a large impact on the R-Squared without appearing as a significant coefficient. This could be related to findings in Kisgen et al. (2008) and in the HP-Autonomy case: the offering of too high a premium by an acquirer for a target could be an example of reckless behavior, for which boutiques and FOs are used in different manners to mitigate. Similar to Table 5, in Columns 8 and 9 of Table 7 I test the presence of a commercial bank as a buy-side financial advisor in order to see if there is any significance. However, I was not able to determine any significance in the *CommercialBank* variable.

To control for self-selection bias, I again employ the two-stage treatment procedure, as outlined above. It is also important to note the abnormally high R-squared of the models in Table 7. Since I do not believe I have actually managed to completely capture such a large percentage of the variability in transaction returns, I remain somewhat skeptical of the results in Table 7. While I believe the signs of the coefficients to be correct, I worry that there is still some source of multicollinearity that is inflating the numbers.

IV.D: Interpretation of Results

I find that there are mixed results when an acquirer uses a boutique firm as a financial advisor. While boutiques generally show negligible difference when compared to full-service firms in sole-advisor cases, they show positive impact on transactions with multiple financial advisors, thereby disproving the Outsider hypothesis through lack of evidence while partially supporting the Improvement hypothesis in cases with multiple buy-side advisors. The lack of difference between boutique and full-service advisors in the sole-advisor scenario could be due to the perception of relative equality between banks in sole-advisor deals. As I mentioned earlier, more complicated deals are more likely to have multiple advisors. As such, if a deal is simple and only needs one advisor, boutiques and full-service firms may be interpreted as interchangeable.

I believe that this negligible impact may also be a result of how the sample includes only the 10 "best" boutique and full-service firms. This criteria could support the idea that elite boutiques are perceived to be just as qualified to be the sole advisor to a buy-side party as the top full-service banks. This view is reflected in the rise of boutique in industry league tables, and would make sense due to the top-tier nature of the founders and clients of each of these boutiques.

On the other hand, boutiques seem to be a valuable member of a multiple-advisor group. One interpretation of this is that the acquirer, not trusting the full-service firms, brought on the boutique as a "check" to the other advisors. In this sense, boutiques are coming from a place of trust, or un-conflicted culture. As it is established that boutiques are exposed to less conflicts of interest, they could bring a governing hand to a more complicated transaction, thereby adding value. This seems to make the most sense, as advisors tend to fight against the addition of other advisors in a transaction, and would need to be pressured by the acquiring firm to include the boutique.[11] Therefore the inclusion of the boutique in a syndicate indicates to the market that the acquirer is concerned with preventing potential conflicts of interest. By the acquirer bringing on a boutique advisor that is independent of sources of financing, the market has greater confidence in the potential of the transaction to be successful, which is reflected in the announcement returns.

The last major finding is the negative impact for a boutique FO on transaction returns. Again, when split out between single and multiple-advisor transactions, there is no difference between an FO provided by a full-service bank or a boutique in a sole-advisor transaction. Instead, the strength of the impact of *BoutiqueFO* is rooted in *BoutiqueFO_Multi*. In opposition to the Reliability hypothesis, the presence of a boutique FO has a definite negative impact on transaction returns: -6.58% for transactions where the FO provider is a boutique and part of an advisory

[11] Confirmed in discussion with Mr. Keevil

syndicate. Kisgen et al (2008) finds that in in most cases where the FO was provided by an affiliated financial advisor, there was a negative impact of FOs on announcement returns. Since all of the FO-providers were also listed as financial advisors, there is a definite affiliation conflict that could have led to this negative result.

However, I believe that there is a more likely explanation that does not necessarily contradict with the reason of affiliation conflict. While the use of boutique advisors in syndicates for complicated transactions is seen as a positive signal to the market, as the provider of an FO a boutique could be sending the opposite signal. Plainly, the presence of an acquirer FO could be warning the market that there is something wrong with the transaction. The use of a boutique to provide the FO compounds the problem – it implies the acquirer believes it needs more than just the normal legal protection that an FO offers. Therefore, this negative impact on returns is not due to a lack of faith in the boutique itself; rather, it is the questioning of the transaction and the lack of faith in the "rubber stamp" nature of FOs.

The key question here is "in a multi-advisor syndicate, why would an acquirer need an FO provided by the boutique?" This draws on the earlier argument that a boutique firm in a syndicate is brought on at the urging of the acquirer. Additionally, while it is common for a target company to disclose an FO because of the expectation that sell-side shareholders dispute most transactions, the same case cannot be made for acquirers. Therefore, by having an FO completed, the acquirer is communicating that there is something about the transaction that could draw legal attention, and is using the FO and the boutique to cover itself.

V. Conclusion

This paper examines the importance of advisory firm culture on transaction returns. By comparing boutique to full-service firms, two advisory types that have evident cultural differences, I hoped to determine that firm-based differences do indeed have an impact on transaction returns. It finds that there is a significant impact made by boutique firms on announcement period returns of a transaction when employed by an acquiring company.

It is important to note that this significance is found on the acquiring side of the transaction, when much of the concern over conflicts of interests in banks occurs on the target side. Additional studies would need to be done in order to see what sorts of effect boutiques and boutique FOs have on target firms. This research is also relevant due to the prominence of boutiques in the current bank market. As boutiques and other financial institutions continue to evolve and chip away at the full-service behemoths, it is important to understand what exactly makes them different and if that difference truly has economic impact.

A potential flaw in my reasoning lies in my interpretation of the results from Table 7. As I noted in the analysis of deal characteristics, boutiques are much less likely than full-service firms to provide an FO. As discussed earlier, boutiques are more concerned about the reputational impact of providing an FO for a questionable transaction than full-service banks. However, if boutiques refuse to provide FOs for conflicted transactions, then why would the market not have faith in transactions where boutiques do choose to provide FOs? This is a question that I would aim to explore with both more time and FO data.

As always, there is room for additional study in both boutiques and fairness opinions. While I used trust as a lump measure to differentiate between boutique and full-service firms, there could be additional variables at play. It would be worthwhile to have a supplemental study

comparing the two advisory types, but instead using survey analysis gathered from bankers themselves. This could give further insight to if there are explanations that I did not take in to consideration. Regarding fairness opinions, much will depend on the rulings of the Delaware courts over upcoming years. I would be interested to see if acquirer fairness opinions will continue to be seen as a proper legal tool, while also acting as an indicator of fault to the markets.

Appendix A: List of Variable Used in Tests

1. **Boutique:** Dummy variable that takes the value of 1 if the acquiring firm had one or more boutique financial advisors
2. **Boutique_Sole:** Dummy variable that takes the value of 1 if the acquiring firm had a boutique as the sole financial advisor
3. **Boutique_Multi:** Dummy variable that takes the value of 1 if the acquiring firm has a boutique as one of multiple financial advisors
4. **FO:** Dummy variable that takes the value of 1 if the acquiring firm disclosed a fairness opinion
5. **BoutiqueFO:** Dummy variable that takes the value of 1 if that fairness opinion was completed by a one or more boutique financial advisors
6. **BoutiqueFO_1:** Dummy variable that takes the value of 1 if the acquiring firm had a fairness opinion done by a sole boutique advisor
7. **BoutiqueFO_Multi:** Dummy variable that takes the value of 1 if the acquiring firm had a fairness opinion done by a boutique that was one of many financial advisors
8. **Transaction Size:** The reported value of the transaction
9. **Relative Size:** The ratio of acquirer size to target size
10. **Acquirer Size:** The market value of equity of the acquirer prior to deal announcement
11. **Hostile:** Dummy variable that equals 1 if the acquisition was hostile as opposed to friendly
12. **Toehold:** Fraction of target shares owned by the acquirer prior to deal announcement
13. **Stock:** Defined as an offer with >50% consideration
14. **Related:** Dummy variable that equals 1 if the target and the acquirer are in related industries, as determined by SIC codes
15. **Competition:** Dummy variable that equals 1 if there is more than one bidder for the target company
16. **Premium:** The percentage difference between the offer price and the target share price four weeks in advance of the announcement date
17. **High Premium:** Dummy variable that equals 1 if the transaction premium is greater than the sample median
18. **Acquirer (Target) M/B:** The ratio of market value of equity relative to the book value of equity of the acquirer (target) for the prior fiscal year
19. **Target ROE:** The ratio of the earnings to average equity for the prior fiscal year
20. **Target Sales Growth:** The proportional change in sales over the prior fiscal year
21. **Target D/E:** The ratio of the debt to equity for the prior fiscal year
22. **Commercial Bank:** Dummy variable that equals 1 if one or more financial advisors were an investment bank that used to operate solely as a commercial bank

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Table 1
Observations by Year

Year	No. of Acquisitions	Percent
2006	51	6.03
2007	61	7.21
2008	33	3.9
2009	65	7.68
2010	62	7.33
2011	48	5.67
2012	62	7.33
2013	82	9.69
2014	109	12.88
2015	121	14.3
2016	90	10.64
2017	62	7.33
Total	846	

Table 2
Ranking of Transaction Advisors

Rank	Full-Service Advisor	No. of Acquisitions	Market Share	Boutique Advisor	No. of Acquisitions	Market Share
1	JP Morgan	103	12.17%	Evercore Partners	31	3.66%
2	Morgan Stanley	93	10.99%	Lazard	25	2.96%
3	Citi	90	10.64%	Centerview Partners LLC	17	2.01%
4	Goldman Sachs & Co	90	10.64%	Moelis & Co	14	1.65%
5	Bank of America Merrill Lynch	86	10.17%	Houlihan Lokey	9	1.06%
6	Barclays	75	8.87%	Greenhill & Co, LLC	8	0.95%
7	Credit Suisse Group	58	6.86%	Rothschild & Co	7	0.83%
8	UBS Investment Bank	47	5.56%	Guggenheim Securities LLC	6	0.71%
9	RBC Capital Markets	40	4.73%	Perella Weinberg Partners LP	5	0.59%
10	Deutsche Bank	39	4.61%	Blackstone Group LP	3	0.35%
		721	85.24%		125	14.77%

Table 3

Investment Banks and Fairness Opinions in M&A

This table presents the use of two types of financial advisors, boutiques and full service banks, as well as the use and structure of FOs in M&A transactions from 2006-2017. Information on advisor classification and FOs is obtained from SDC's M&A database, manually augmented using SEC's EDGAR filing search.

Boutique is a dummy variable that takes the value of 1 if the acquiring firm had one or more boutique financial advisors. Boutique_Sole is a dummy variable that takes the value of 1 if the acquiring firm had a boutique as the sole financial advisor, while Boutique_Multi is a dummy variable that takes the value of 1 if the acquiring firm has a boutique as one of multiple financial advisors.

FO is a dummy variable that takes the value of 1 if the acquiring firm disclosed a fairness opinion. BoutiqueFO is a dummy variable that takes the value of 1 if that fairness opinion was completed by a one or more boutique financial advisors. BoutiqueFO_1 is a dummy variable that takes the value of 1 if the acquiring firm had a fairness opinion done by a sole boutique advisor, while BoutiqueFO_Multi is a dummy variable that takes the value of 1 if the acquiring firm had a fairness opinion done by a boutique that was one of many financial advisors.

	Full Sample (N = 846)
Type of Advisors	
Full Service	640
Boutique	206
Use of FO	
No	621
Yes	225
Boutique Breakdown	
Boutique_Sole	57
Boutique_Multi	149
Boutique FO Breakdown	
BoutiqueFO	71
BoutiqueFO_1	13
BoutiqueFO_Multi	58

Table 4
Deal Characteristics

This table presents summary statistics of the 846 M&A deals and merging firms, sorted by the advisor classification and the structure of FOs. Data is for M&A deals between January 2006 and December 2017, in which the acquiring company has financial advisor(s). Dollar amount ($) are in millions. *Acquirer Size* is the market value of equity of the acquirer prior to deal announcement. *Relative Size* is the ratio of acquirer size to target size. *Acquirer (target) M/B* is the ratio of market value of equity relative to the book value of equity of the acquirer (target) for the prior fiscal year. *% Hostile* measures the amount of deals that were labeled hostile by the SDC database. A *stock offer* is defined as deals where the consideration is at least 50%. *Related* is a dummy variable that equals 1 if the target and the acquirer are in related industries, as determined by SIC codes. *Premium* is the percentage difference between the offer price and target share price four weeks prior to the announcement date. The number of non-missing observations for a particular variable is listed below the statistic.

Advisor Structure	Average Deal Size	Average Acquirer Size	Average Relative Size	Average Acquirer M/B	Average Target M/B	% Hostile	% Stock Offer	% Related	Average Premium
Boutique = 0	3469.96	30885.62	30.35	87.29	2.98	0.46%	27.93%	85.78%	20.43%
	640	506	285	535	402	640	555	640	455
Boutique = 1	6146.41	33052.60	42.69	2.57	3.68	7.77%	32.20%	87.86%	39.15%
	206	143	91	171	136	206	205	206	151
FO = 0	3149.09	33956.54	42.34	89.75	2.97	1.77%	17.20%	84.06%	14.00%
	621	486	281	519	390	621	535	621	426
FO = 1	6806.00	23630.47	6.70	3.01	3.67	3.56%	57.33%	92.44%	51.36%
	225	163	95	187	148	225	225	225	180
Boutique_Sole = 0	1959.82	35004.78	46.54	3.95	2.50	0.29%	25.17%	85.34%	20.34%
	348	281	158	292	215	348	290	348	241
Boutique_Sole = 1	1454.94	28726.15	157.22	4.60	5.39	1.75%	22.81%	85.96%	4.32%
	57	42	21	48	35	57	57	57	37
Boutique_Multi = 0	5269.71	25741.23	10.22	187.43	3.54	0.68%	30.94%	86.30%	20.53%
	292	225	127	243	187	292	265	292	214
Boutique_Multi = 1	7941.12	34851.72	8.33	1.79	3.08	10.07%	35.81%	88.59%	50.45%
	149	101	70	123	101	149	148	149	114
BoutiqueFO = 0	7024.30	26129.70	7.68	3.97	3.36	0.67%	58.39%	97.32%	60.83%
	149	119	71	123	101	149	149	149	130
BoutiqueFO = 1	6661.00	18501.44	4.28	0.90	4.29	9.86%	57.75%	84.51%	25.76%
	71	40	20	60	42	71	71	71	45
BoutiqueFO_1 = 0	3178.76	20757.75	12.58	6.07	2.36	1.75%	50.88%	94.74%	41.37%
	57	42	28	46	40	57	57	57	46
BoutiqueFO_1 = 1	1044.08	2984.06	2.91	4.54	2.38	7.69%	61.54%	69.23%	9.65%
	13	5	1	8	8	13	13	13	8
BoutiqueFO_Multi = 0	9043.59	27652.88	4.23	2.84	4.05	0.00%	60.82%	96.91%	69.45%
	97	81	47	81	66	97	97	97	89
BoutiqueFO_Multi = 1	7919.97	20718.21	4.35	0.35	4.74	10.34%	56.90%	87.93%	29.26%
	58	35	19	52	34	58	58	58	37
Total	4121.67	31363.09	33.34	66.77	3.16	2.25%	29.08%	86.29%	25.10%
	846	649	376	707	538	846	760	846	606

Table 5

The Impact of Boutique Advisory on 3-day Announcement Period Returns of Acquirers

Panel A presents OLS regressions on the 3-day (-1,+1) cumulative abnormal returns of acquirers (in %) around the deal announcement date on the type and structure of buy-side advisors (boutique vs. full-service). All variables are defined in Tables 3 and 4. I estimate the effect of each key explanatory variable in models 1-3, the explanatory variables including all constants in models 4-6, and the addition of the commercial bank variable in models 7-8.

Panel A: OLS	Initial Boutique OLS			Boutique Impact			Commercial Bank	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Advisor Type and Structure								
Boutique	0.0222**			0.0278**			0.0277**	
	(0.0104)			(0.0135)			(0.0132)	
Boutique_Sole		-0.0275			-0.0298			
		(0.0209)			(0.0351)			
Boutique_Multi			0.0312**			0.0253*		0.0254*
			(0.0131)			(0.0149)		(0.0147)
Transaction characteristics								
Ln(Acquirer Size)				-0.00888***	-0.00496	-0.0137***	-0.00890***	-0.0142***
				(0.00261)	(0.00412)	(0.00345)	(0.00265)	(0.00364)
Hostile				0.00403	-0.0381	0.0255	0.00425	0.0310*
				(0.0116)	(0.0271)	(0.0157)	(0.0119)	(0.0165)
Stock				-0.0556***	-0.0325	-0.0561***	-0.0557***	-0.0571***
				(0.0105)	(0.0202)	(0.0138)	(0.0108)	(0.0141)
High Premium				-0.00799	-0.000723	-0.0127	-0.00807	-0.0141
				(0.00826)	(0.0145)	(0.0130)	(0.00847)	(0.0133)
Target ROE				-0.00168*	-0.00320***	-0.000255	-0.00169*	-6.73e-05
				(0.000887)	(0.00105)	(0.00732)	(0.000886)	(0.00750)
Target Sales Growth				0.0329***	0.0125*	0.0845***	0.0329***	0.0833***
				(0.00820)	(0.00750)	(0.0127)	(0.00820)	(0.0128)
Commercial Bank							0.00108	0.0143
							(0.0120)	(0.0159)
Constant	0.00113	0.0324	-0.0239	0.0836**	0.0836	0.117**	0.0836**	0.118**
	(0.0264)	(0.0220)	(0.0472)	(0.0327)	(0.0535)	(0.0466)	(0.0328)	(0.0458)
Observations	846	405	441	316	141	175	316	175
R-squared	0.036	0.034	0.093	0.298	0.308	0.518	0.298	0.521
Time FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

Robust standard errors in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Table 6

The Impact of Boutique Fairness Opinions on 3-day Announcement Period Returns of Acquirers

Panel A presents OLS regressions on the 3-day (-1,+1) cumulative abnormal returns of acquirers (in %) around the deal announcement date on the use and provider of an FO (Boutique or full-service) . All variables are defined in Tables 3 and 4. I estimate the effect of each key explanatory variable in models 1-4, the explanatory variables including all constants in models 5-7, and the addition of the commercial bank variable in models 8-9.

Panel A: OLS	Initial FO OLS				FO Source			Commercial Bank	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
FO Characteristics									
FO	0.00635								
	(0.00874)								
BoutiqueFO		0.0283*			-0.0779***			-0.0792***	
		(0.0156)			(0.0220)			(0.0222)	
BoutiqueFO_1			0.00376			0.342			
			(0.0627)			(0.598)			
BoutiqueFO_Multi				0.0210			-0.0658**		-0.0518
				(0.0166)			(0.0315)		(0.0322)
Transaction Characteristics									
Ln(Deal Size)					-0.00163	0.0633	0.00178	-0.00130	0.00252
					(0.00822)	(0.174)	(0.00675)	(0.00821)	(0.00747)
Toehold					0.00386***		0.00452***	0.00399***	0.00452***
					(0.000873)		(0.00121)	(0.000885)	(0.00121)
Stock					-0.0572*	0.255	-0.0859**	-0.0547*	-0.0672*
					(0.0294)	(0.374)	(0.0318)	(0.0275)	(0.0373)
Related					-0.0987***	0.383	-0.216***	-0.0904***	-0.187***
					(0.0346)	(0.392)	(0.0574)	(0.0337)	(0.0554)
High Premium					-0.0137	-0.242	-0.0344	-0.0125	-0.0180
					(0.0261)	(0.196)	(0.0281)	(0.0264)	(0.0356)
Target M/B					-0.00514**	-0.00208	-0.00138	-0.00488**	-0.000818
					(0.00222)	(0.0465)	(0.00433)	(0.00237)	(0.00377)
Acquirer M/B					0.000872**	-0.0290	-0.00134	0.000885**	-0.00236
					(0.000380)	(0.0468)	(0.00162)	(0.000374)	(0.00157)
Target ROE					-0.0187	-1.221	-0.0244	-0.0175	-0.0154
					(0.0168)	(1.473)	(0.0274)	(0.0165)	(0.0386)
Target Sales Growth					0.0305***	-0.119	0.0194	0.0298***	-0.000476
					(0.00944)	(0.123)	(0.0626)	(0.00947)	(0.0639)
Commercial Bank								-0.0186	0.0799
								(0.0313)	(0.0521)
Constant	0.00114	-0.0330	-0.0731	0.0207	0.174*	-0.334	0.274***	0.163*	0.200**
	(0.0272)	(0.0246)	(0.0606)	(0.0421)	(0.0918)	(1.402)	(0.0718)	(0.0895)	(0.0852)
Observations	846	220	70	155	89	25	68	89	68
R-squared	0.035	0.321	0.297	0.444	0.748	0.962	0.894	0.750	0.915
Time FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

Robust standard errors in parentheses

*** p<0.01, ** p<0.05, * p<0.1