# Accounting firms deliver fairer value for M&A than investment banks, study finds

February 23 2022

Credit: Pixabay/CC0 Public Domain

New research by Bayes Business School (formerly Cass) shows that accounting firms leverage their auditing expertise to produce fairer target valuations on mergers and acquisitions (M&A) than investment banks.

"Accounting Firms in the European M&A Advisory Market" by Dr. Pawel Bilinski, Reader in Finance and Dr. Andrew Yim, Senior Lecturer in Accounting at Bayes Business School (formerly Cass), shows the benefits of auditing proficiency and experience possessed by accounting firms in assessing fair value of targets in a deal.

Highlights of the research include:

- Acquirer announcement returns are higher when a deal is brokered with an accountancy firm.
- Offer premiums are lower if the bidder is advised by audit specialists with prior target industry experience.
- Bidders advised by investment banks experience negative price reactions when attempting to purchase hard-to-value targets.
- Accounting firms' more up-to-date knowledge of auditing practices generates higher returns for acquiring shareholders.

With overpayment on targets among the most common reasons for M&A failure, the study of transactions from 15 European Union countries between 1990 and 2014 builds upon "Knowledge-based view of the resource-based' theory, which states that competitive advantage can be developed through firm-level knowledge as a strategic source.

Using the Securities Data Company (SDC) Platinum M&A database and Compustat Global database, the research sampled 7,771 deals by investments banks and 691 by accounting firms and their respective prices. Measuring accounting quality by accruals quality—which correlates with the accuracy of free cash flow valuation—the researchers then developed an index to measure the target valuation difficulty based on whether or not the target firm was private, how large the target was and whether or not the target was US-based.

Dr. Bilinski said the research had many key contributions, adding to the knowledge-based view of resource-based theory.

"Our study documents the role of accounting firms in the M&A advisory field, which makes a strong case for using their services over traditional investment banks in the pursuit of target acquisitions."

"Accounting firms possess an excellent skillset for determining a company's true value through auditing expertise, and this is invaluable given the number of deals that collapse or fail due to overpayment."

"With preference for Environmental, Social and Governance-friendly (ESG) deals on the rise, there are new dimensions for assessing the value of a target firm. Audit expertise could help overcome this additional challenge."

"Of course, investment banks are still widely used in M&A transactions and have their own merits, but we hope our study sheds light on the advantages of the accounting profession and the positive role it can play in target acquisition."

Dr. Yim said it is in accounting firms' own interest to continue high-quality audit and reporting services in order to be competitive in delivering M&A advisory services.

"Our findings help policymakers and regulators to appreciate the benefit of letting accounting firms develop different lines of service," he said. "The study adds to the list of pros and cons that should be rationally assessed in the debate about separating the audit from advisory functions within accounting firms."

"Our study also advances the knowledge-based perspective of organizations explaining how knowledge spillover from audit work can enhance the quality of M&A advisory work, helping accounting firms establish their strong foothold in investment banks' specialty territory."

"Otherwise, it is hard to understand why accounting firms are listed among the top ten M&A financial advisors in the European Thomson Reuters and Mergermarket league tables."

The research is published in the *British Journal of Management*.

**More information:** Pawel Bilinski et al, Accounting Firms in the European M&A Advisory Market, *British Journal of Management* (2021). DOI: 10.1111/1467-8551.12571

Provided by City University London

Citation: Accounting firms deliver fairer value for M&A than investment banks, study finds (2022, February 23) retrieved 13 May 2024 from https://phys.org/news/2022-02-accounting-firms-fairer-ma-investment.html