A Review of Cross-border Mergers & Acquisitions in APEC

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Summary

In parallel with global trends, cross-border M&As have increased dramatically in the APEC economies especially since the mid-1990s. The rapid increase in cross-border M&As in the world in general and in the APEC economies in particular is driven by a combination of factors, including the liberalisation of trade and investment regimes, the deregulation of services sector, the privatisation of state-owned enterprises, and the relaxation of controls over cross-border M&As.

APEC economies accounted for 45 percent of the sales value and 31 percent of the value of purchases in world total cross-border M&As from 1991 to 2000. Cross-border M&As in APEC have been dominated by industrial economies. The United States has been both the largest seller and purchaser in APEC economies. APEC developing economies are still not large players in cross-border M&As. However, their role in cross-border M&As has been increasing especially since the late 1990s.

Cross-border M&As in the APEC economies have been concentrated in chemicals and chemical products, electrical and electronic equipment, motor vehicles and other transport equipment, electricity production and distribution, trade, telecommunications, finance, and business services.

During the 1990s the APEC economies as a whole were net sellers in cross-border M&A transactions, especially since 1998. This implies that the APEC economies have attracted a large amount of net capital inflow which has contributed to economic growth and economic recovery of the East and Southeast Asian economies affected by the financial crisis in the late 1990s. This imbalance between sales and purchases in cross-border M&As in APEC economies is likely to continue.

Mergers and acquisitions have different consequences with respect to legal obligations, acquisition procedures, and tax liabilities (Marren, 1993). In a cross-border merger, the

assets and operations of two firms belonging to two different economies are combined to establish a new legal entity. The target company ceases to exist as a separate entity. The transaction can be executed through an exchange of stock or assets. Cross-border mergers often require the approval of both the acquiring and target firm's shareholders and the acquiring firm assumes all of the target's assets and liabilities.

In a cross-border acquisition, the control of assets and operations is transferred from a local to a foreign company, the former becoming an affiliate of the latter. Cross-border acquisitions include full (foreign interest of 100 percent), majority (foreign interest of 50-99 percent), and minority (foreign interest of 10-49 percent) acquisitions. Acquisitions involving less than 10 percent are classified as portfolio investment.

Cross-border M&As are one mode of entry for foreign direct investors to host economies. The OLI (ownership advantage, location advantage and internalisation advantage) paradigm is a popular framework for the analysis of the determinants of foreign direct investment. The framework also provides a useful theoretical framework to explain the motivation for cross-border M&As. Apart from the general explanations of OLI paradigm, speed and access to proprietary assets are other reasons for firms to choose cross-border M&As to enter foreign markets. In addition, factors such as the search for market power, efficiency gains through synergies, size, diversification, and financial motivations affect the decision of firms to undertake cross-border M&As.

Although firms' motivations are the primary determinant of decisions to undertake cross-border M&As, changes in technology, regulatory framework and capital markets around the world in the last decade or so have greatly promoted and facilitated the growth of cross-border M&As.

The impact of cross-border M&As on corporate performance has been controversial. According to currently available studies, in a large number of cases, M&As have not produced a better performance for the firm as a whole. However, some studies have found a positive impact on the performance of companies which are taken over. This result is especially relevant to those host economies experiencing large-scale privatisation of state-owned enterprises or that are in financial crisis. In such a situation

cross-border M&As can play a positive role in improving the productivity of acquired firms and in promoting economic restructuring of host economies. Because most study of corporate performance is focused on domestic M&As and based on data from the United States and the United Kingdom, there is a lack of evidence from developing economies and economies in transition. With the exception of a few surveys, the experience in the 1990s has not been fully explored in the literature. Further studies, especially of finance and telecommunications, and in the context of developing economies, would be valuable.

Theoretically, both cross-border M&As and greenfield FDI are foreign investments from a host economy's point of view. But are cross-border M&As as a mode of FDI entry less beneficial for economic development than greenfield FDI? The concern is that cross-border M&As do not add to productive capacity at the time of entry, but simply transfer assets and ownership from domestic to foreign hands. This transfer is sometimes accompanied by the reduction in production, R&D activities and employment. It may also reduce competition in domestic market and lead to market dominance of foreign acquirers.

The concerns are not only economic, but also social, political and cultural. The fact that many cross-border M&As are infrastructure-related is directly linked to social and political opposition. It can be an important political issue if the ownership of the national telecommunications or electricity or water provider is to switch to foreigners. In industries like the media and entertainment, cross-border M&As may seem to threaten national culture or identity. A large shift of ownership of important enterprises from domestic to foreign hands may be seen as eroding national sovereignty.

However, in the long run, cross-border M&As and greenfield FDI will have similar contributions to host economy development in terms of capital formation, employment and technology transfer.

Developing host economies can derive substantial gains from cross-border M&As. Even though cross-border M&As may not directly create new assets in the short run, they involve cross-border capital transfers that can increase total investible funds

available to host economies. The benefits to capital-constrained host economies are even greater if cross-border M&As induce sequential and associated FDI by the acquiring companies and their suppliers. Cross-border M&As can offer access to technologies that local firms do not have. They may introduce innovative management practices in the host economy. They may render it easier for a developing host economy to become part of global sourcing and marketing networks, thereby improving international market penetration.

Cross-border M&As can be even more valuable for host economies when they preserve potentially profitable assets that are under threat. This is especially relevant in the context of privatisation-related cross-border M&As in transition economies and in financially distressed developing economies.

Cross-border M&As can bring many benefits to the host economy especially in special economic circumstances, like during a privatisation program and or a financial crisis. However, there is the possibility that cross-border M&As may have a negative impact on market structure and competition. The adoption of competition policy measures and their effective implementation are very important to the governments of host economies.

The industrial economies in APEC have rich experience in making and implementing competition policies including those relating to M&As. For the APEC developing economies, especially economies in transition, cross-border M&As are a relatively new phenomenon. Those economies have little experience in making and enforcing competition policies. This lack of experience creates scope for bilateral and multilateral cooperation among APEC member economies in making and implementing suitable policies. Cooperation not only will help reduce the risk of anti-competitive practices but also will facilitate cross-border M&As among APEC member economies.

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Introduction

Since the mid-1990s, global cross-border mergers and acquisitions (M&As) have increased rapidly. In 2000, the total value of global cross-border M&As reached a record level of US$1144 billion, increasing nearly 50 percent over that in 1999. The rapid increase in global cross-border M&As is attributed to several factors, including the liberalisation of trade and investment, deregulation of services, privatisation of state-owned enterprises, and relaxation of controls. Although not all cross-border M&As are financed through foreign direct investment (FDI), cross-border M&As account for a significant share of global FDI flows, particularly in the industrial economies. Therefore, the fast growth of cross-border M&As has a significant impact on the magnitude and direction of global FDI flows.[1]

APEC economies have been some of the most important participants in this global surge of cross-border M&As. In 2000, the total value of cross-border M&A sales in the APEC economies reached US$471 billion, accounting for 41 percent of the world total. In the APEC economies, the United States has been the single most important contributor. In terms of the value of cross-border M&A sales, in 2000 the United States accounted for 28 percent of the world total and 67 percent of the APEC total respectively. Although the industrial economies have been the dominant force in cross-border M&As, developing economies in APEC have experienced a rapid increase in cross-border M&A activities especially since the late 1990s.

[1] According to the *World Investment Report 2002* (UNCTAD, 2002), which became available after this report was written, world foreign direct investment (FDI) inflows in 2001 declined to US$735 billion. This is less than half the 2000 figure. Behind this decline is the slowdown in the world economy (1.3%, as compared with 4.0% in 2000) and a weakening of business confidence. Both factors were accentuated by the September 11 events in the United States, and both contributed to a sharp reduction of cross-border mergers and acquisitions (M&As) that take place predominantly between industrialised countries. The value of cross-border M&As in 2001 stood at barely US$600 billion for less than 6,000 deals, vs US$1.1 trillion for some 7,900 deals in 2000. In light of the slow recovery of business confidence and of growth, especially in the United States which is the lead buyer and seller, as we stress in the text, UNCTAD does not expect a rebound of FDI flows in year 2002.

Fast growth of cross-border M&As is accompanied by increasing concerns about their impact on the host economy, particularly in developing host economies. This is not surprising given the limited experience of developing economies of cross-border M&As. What is the composition of cross-border M&As? What is the motivation for cross-border M&As? What would be the impact of a cross-border M&A on corporate performance and on host economy economic development? And what are the policy instruments that host economy governments can use to reduce or prevent the negative impact that cross-border M&As may have on economic development? The aim of this paper is to examine these questions by reviewing the available literature, studies and information on cross-border M&As.

An overview of cross-border M&As in APEC

Cross-border M&As are defined here as any transactions in assets of two firms belonging to two different economies. Therefore, cross-border M&As can take place between two firms located in different economies, or within one economy between two firms belonging to two different economies.

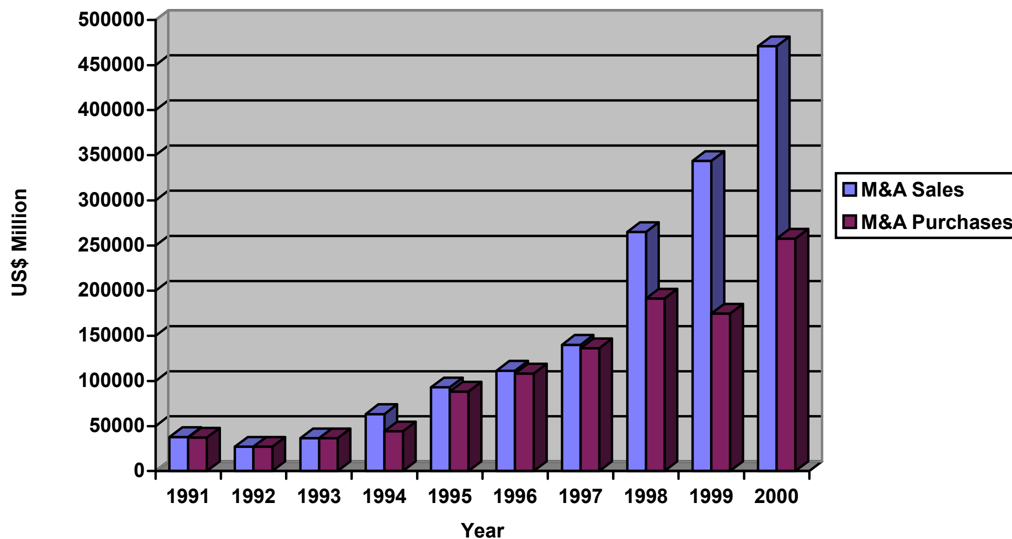
Rapid growth in cross-border M&As in APEC in the 1990s

Cross-border M&As have increased dramatically in the APEC economies in the 1990s. The value in APEC of cross-border M&As sales (in 1995 constant US dollar prices)[2] rose from US$41 billion in 1991 to US$435 billion in 2000, increasing by more than 10 times. The value of cross-border purchases rose from US$40 billion in 1991 to US$238 billion in 2000, nearly 5 times (Figure 1).

APEC economies account for a large percentage of world cross-border M&As. From 1991 to 2000, APEC economies accounted for 45 percent of the world total value of cross-border M&A sales and for 31 percent of the world total value of cross-border M&A purchases. Among the top 50 cross-border M&A deals completed during 1987-99, 33 deals were conducted by APEC economies, especially by the United States, as either sellers or purchasers. Among the 109 cross-border M&A deals with a value of

over US$1 billion completed in 1999, APEC economies participated in 64, and 21 of these were conducted between two APEC economies, including mainly the United States, Canada, Australia, Japan, China, Korea and Mexico (UNCTAD, 2000a).

Figure 1 Cross-border M&As in APEC



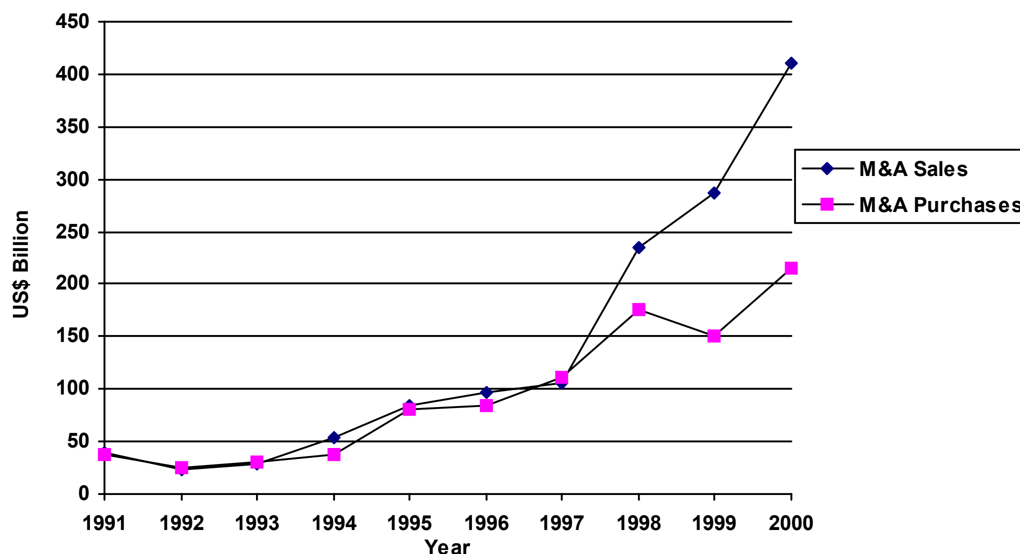
Source: UNCTAD, 2001.

Dominance of industrial economies in cross-border M&As

Cross-border M&As in APEC have been mainly concentrated in industrial economies, which account for 90 percent of sales value and 85 percent of purchase value of cross-border M&As in APEC in the period of 1991-2000. Cross-border M&As grew very fast in the developed APEC economies. Cross-border M&A sales increased from US$38.8 billion in 1991 to US$410 billion in 2000, while cross-border M&A purchases rose from US$38 billion to US$215 billion in the same period (Figure 2).

[2] The values of M&As discussed in this section are all based on 1995 constant US dollar prices.

Figure 2 Cross-border M&As of developed economies in APEC



Source: UNCTAD, 2001.

Among the industrial economies, the United States has been both the largest seller and purchaser in APEC economies. In 2000, the value of cross-border M&As sales in the United States was US$300 billion, accounting for 69 percent of the APEC total, while US firms spent US$147 billion on acquiring foreign firms, accounting for 62 percent of the APEC total (Tables 1 and 2).

Canada and Australia are also important players. In 2000, the sales value and purchase value of cross-border M&As of Canada reached US$71 billion and US$37 billion respectively. In the same period, the value of cross-border M&As sales of Australia were US$20 billion, while Australian firms purchased US$10 billion foreign firms through cross-border M&As.

Table 1 Cross-border M&A sales in APEC economies (US$ million)

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Industrial economies										
Australia	2838	2614	3330	3041	17360	12845	14252	14034	11249	20073
Canada	4006	2730	2414	4460	11567	10629	8198	15648	22459	71303
Japan	195	246	97	767	541	1686	2970	3830	15408	14377
New Zealand	892	1237	1492	324	1828	4745	1297	2206	1499	4068
USA	30910	16929	20851	45718	53237	66747	78716	199551	236247	300046
Sub-total	38842	23756	28185	54309	84533	96651	105434	235268	286861	409867
Developing economies										
Brunei	0	0	2	0	0	0	0	0	0	0
Chile	370	553	288	911	717	2004	2338	1519	7840	2710
China	137	236	586	731	403	1869	1788	760	2246	2079
Hong Kong, China	622	1789	5540	1637	1703	3204	7062	893	3921	4434
Indonesia	163	249	176	211	809	520	320	650	1092	758
Korea	737	0	2	1	192	553	805	3783	9435	5965
Malaysia	140	49	541	453	98	753	338	1044	1093	408
Mexico	11	1027	1945	1955	719	1400	7637	2858	806	3668
Papua New Guinea	31	0	2	37	51	38	248	39	99	0
Peru	16	186	65	3150	945	828	878	154	807	99
Philippines	69	432	142	846	1208	453	4005	1814	1428	339
Russia	0	35	322	64	100	93	2582	140	169	701
Singapore	260	295	378	363	1238	581	283	446	2774	1417
Chinese Taipei	0	3	17	16	42	49	579	23	1722	596
Thailand	87	532	44	91	161	229	610	3056	1886	2377
Vietnam	0	0	0	2	1	6	61	0	55	18
Sub-total	2642	5387	10050	10468	8387	12581	29534	17179	35374	25566
APEC total sales	41484	29143	38235	64777	92920	109232	134967	252447	322236	435433
World total sales	88388	84737	86693	129916	186593	222615	293688	506283	718346	1058109
Share of APEC in world	46.93	34.39	44.10	49.86	49.80	49.07	45.96	49.86	44.86	41.15

Source: UNCTAD, 2001.

Table 2 Cross-border M&As purchases in APEC economies (US$ million)

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Industrial economies										
Australia	1162	723	1933	1637	6145	9103	11315	7758	9507	10043
Canada	4496	2303	4309	5191	12491	8587	18150	33919	17415	36675
Japan	13006	4694	1154	1081	3943	5550	2646	1223	9862	19295
New Zealand	967	987	263	45	573	1157	756	949	1333	1770
USA	18174	16070	22340	29161	57343	59545	77908	130865	112819	147335
Sub-total	38256	24777	30000	37116	80495	83962	110777	174714	150935	215118
Developing economies										
Brunei	0	0	211	0	31	185	0	0	0	0
Chile	0	473	864	299	794	3753	1442	563	302	469
China	3	612	506	314	249	442	770	1215	95	435
Hong Kong, China	1470	1350	4293	2317	2299	2855	8094	2096	2176	5336
Indonesia	3	17	52	33	163	214	651	37	228	1059
Korea	205	77	77	511	1392	1627	2292	178	1029	1584
Malaysia	163	158	808	830	1122	9448	861	1008	1291	704
Mexico	3	949	322	2238	196	850	3039	641	2078	3914
Papua New Guinea	0	0	0	0	13	8	0	0	0	303
Peru	0	0	0	7	62	232	42	45	206	57
Philippines	15	0	26	43	153	186	52	1	309	69
Russia	0	19	6	250	0	237	2	287	49	208
Singapore	624	314	886	1200	892	1979	2782	790	4426	8184
Chinese Taipei	0	140	0	31	122	4	417	598	383	1053
Thailand	65	1	40	12	144	177	53	41	144	5
Vietnam	0	6	0	1	0	11	26	0	0	0
Sub-total	2552	4118	8092	8087	7632	22208	20524	7500	12717	23380
APEC total purchases	40807	28895	38092	45202	88127	106170	131301	182214	163652	238498
World total purchases	88388	84737	86693	129916	186593	222615	293688	506283	718346	1058109
Share of APEC in world	46.17	34.10	43.94	34.79	47.23	47.69	44.71	35.99	22.78	22.54

Source: UNCTAD, 2001.

Note: The classifications of economies are used by UNCTAD.
The values are based on 1995 constant US dollar price.

Japanese overseas M&A purchases increased significantly in 2000, reaching US$19 billion nearly double that in 1999. Although this signals a shift from the traditional Japanese preference for greenfield FDI, the latter remains the preferred mode of FDI entry (UNCTAD, 1999). Japanese trans-national corporations (TNCs) tend to use the M&A option more in industrial than in developing economies. As of March 1996, about a quarter of Japanese manufacturing affiliates in industrial economies were established through M&As, while the comparable figure in developing Asia was less than one-tenth (Japan, MITI, 1998). Cross-border M&A sales in Japan increased rapidly since 1995 and exceeded purchases in the period of 1997-1999.

Compared to other industrial economies in APEC, New Zealand has been a relatively small player in cross-border M&As. However, New Zealand has increased its participation in such transactions since the mid-1990s especially in cross-border M&A sales. In 2000, the value of cross-border M&A sales reached US$4 billion, 170 percent higher than that in 1999.

Increasing trend of cross-border M&As in developing economies

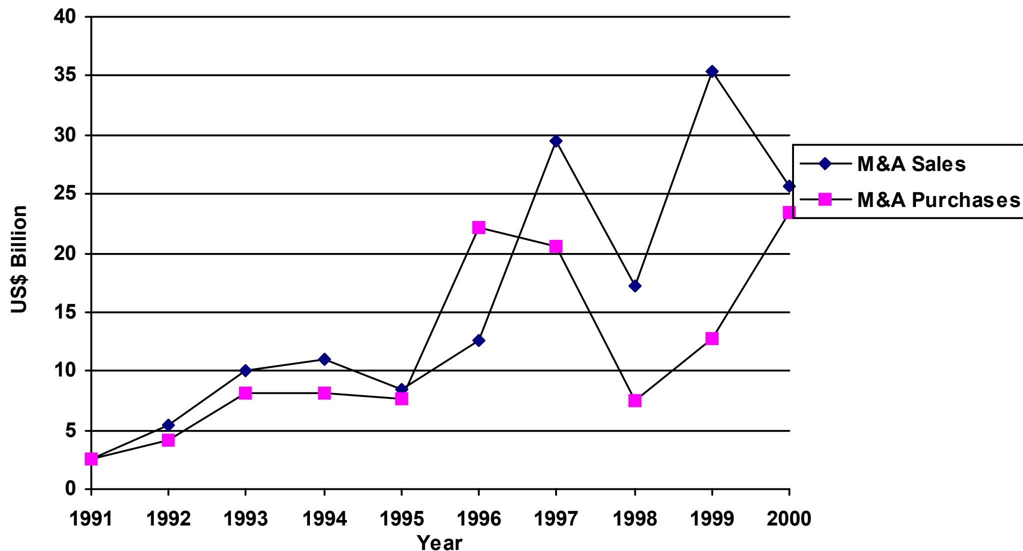
Although APEC developing economies are still not large players in cross-border M&As, the total value of cross-border M&As of APEC developing economies has increased rapidly in the 1990s, especially since the late 1990s (Figure 3). The value of total cross-border M&A sales increased from US$2.6 billion in 1991 to US$25.6 billion in 2000, and the value of cross-border M&A purchases rose from US$2.5 billion to US$23.4 billion in the same period (Table 1 and Table 2).

The increase in cross-border M&A purchases in APEC developing economies is mainly driven by a number of East and Southeast Asian developing economies, among whom Singapore and Hong Kong are the main bases of acquiring firms. The targets are primarily firms in developing economies in the Asian region.

Cross-border M&A sales have increased dramatically since the mid-1990s in the APEC developing economies, particularly in the five Asian economies most affected by the financial crisis, including Indonesia, Malaysia, Philippines, Korea and Thailand. In

addition, Mexico and Chile have also witnessed a large increase in cross-border M&A sales due to the implementation of large-scale privatisation programs.

Figure 3 Cross-border M&As of developing economies in APEC



Source: UNCTAD, 2001.

The wave of cross-border M&As was triggered by important policy changes following the financial crisis in the five Asian economies, particularly in Korea and Thailand. Policy changes were based on the expectation that cross-border M&As would speed up corporate and financial restructuring and facilitate faster economic recovery. Cross-border M&As sales in the five crisis economies increased sharply from US$2.4 billion in 1996 to US$14.9 billion in 1999, before falling slightly to US$9.9 billion in 2000. As a consequence of recent increases, cross-border M&As have accounted for an increasing share of FDI inflows to these economies. The share of cross-border M&As in FDI inflows to the five economies rose from 13 percent in 1996 to 91 percent in 1999 (Indonesia had a negative FDI inflow of US$3270 million in 1999). Cross-border M&As grew faster than traditional foreign investment in greenfield projects.

However, cross-border M&A activity is still in an early phase of development in the Asian financially distressed economies and remains relatively small. For example, in 1999 cross-border M&As accounted for 0.9 percent of GDP in East Asia, compared

with 1.8 percent of GDP in Latin America (Mody and Negishi, 2001). Liberalisation of foreign entry and of ownership restrictions, and the introduction of international accounting standards and shareholding systems, have reduced impediments to foreign investors' access to local financial markets and their ability to acquire assets within them.

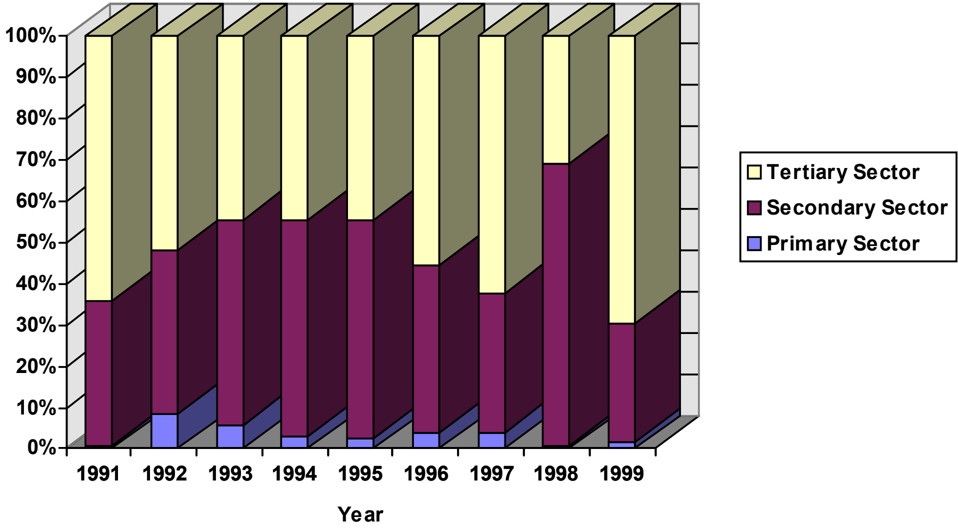
A significant role for cross-border M&As is to encourage longer-term corporate reforms, such as operational restructuring and reallocation of assets. Foreign participation through M&A can be more effective in improving efficiency, competitiveness, and corporate governance. However, more studies are needed to analyse the actual role and impact of cross-border M&As in the restructuring and continued economic development of financially distressed Asian economies.

The importance of the tertiary sector in cross-border M&As

Within the APEC economies the tertiary sector has been the most important economic sector in cross-border M&A transactions, followed by the secondary and the primary sectors. In terms of industries, cross-border M&As have been concentrated in chemicals and chemical products, electrical and electronic equipment, motor vehicles and other transport equipment, electricity production and distribution, trade, telecommunications, finance, and business services (Figure 4).

The present wave of cross-border M&As is driven by a combination of forces and motivations. In addition to the strategic considerations of firms, liberalisation and deregulation are the main factors behind the dramatic increase in cross-border M&As. Increasing cross-border M&As in the services sector in general, and in finance and telecommunications industries in particular, reflect the ongoing liberalisation and deregulation in APEC and the world. Finance industries accounted for one-fifth of the value of cross-border M&As sales in 1999 in APEC (Table 3). Telecommunications has been significantly liberalised. Because of its importance for other industries and the large market for its services, it has attracted substantial M&A activity. In 1999 the telecommunications industry accounted for one-third of the value of cross-border M&As sales in APEC. Prospects for cross-border M&As in telecommunications are

still high with the ongoing process of privatisation and liberalisation in many economies in APEC.



Source: UNCTAD, 2000a.

Table 3 Cross-border M&A sales by sector and by industry in APEC economies (US$ million)

	1991	1992	1993	1994	1995	1996	1997	1998	1999
Primary	307	1728	1647	1420	1574	3063	3726	1321	3712
Agriculture, forestry, and fishing	169	41	81	595	40	353	1468	412	479
Mining, quarrying and petroleum	138	1688	1566	826	1535	2711	2258	908	3233
Secondary	11587	8264	14240	26933	31702	31391	33865	150110	74506
Food, beverages and tobacco	953	825	1730	5638	6893	642	4913	2496	1788
Textiles, clothing and leather	221	28	321	251	1486	169	94	439	119
Wood and wood products	55	36	603	1765	1471	876	2162	1645	2104
Publishing, printing, and reproduction of recorded media	119	342	786	1327	361	8318	1382	10000	6672
Coke, petroleum and unclear fuel	1247	451	721	546	3003	943	2396	51801	3077
Chemicals and chemical products	2382	2434	6258	11810	10075	6634	11281	9174	12426
Rubber and plastic products	395	71	126	166	353	2777	1003	314	750
Non-metallic mineral products	551	1496	263	196	1232	318	1127	2115	3846
Metal and metal products	517	709	295	843	696	1289	2225	2245	2782
Machinery and equipment	326	188	636	1307	1349	2268	1812	5715	15296
Electrical and electronic equipment	3805	504	2056	1044	2844	3974	3390	17633	15408
Precision instruments	819	803	339	1423	1040	934	498	4758	2668
Motor vehicles and other transport equipment	189	115	11	609	888	2170	1530	41671	7523
Other manufacturing	8	235	92	9	73	82	51	155	49
Tertiary	21458	10829	12647	22885	26780	43211	62000	66986	178579
Electric, gas and water	0	7	56	198	11	1570	4840	3564	14875
Construction	107	187	207	584	357	634	341	187	1639
Trade	1465	1453	2713	6526	2094	13828	8860	11540	9082
Hotels and restaurants	428	557	384	545	1858	875	1982	2196	2301
Transport, storage and communications	212	979	2497	4331	1181	7435	3336	12418	78162
Finance	8759	4180	3420	3286	5855	14812	21092	17783	52766
Business services	1283	1256	2105	4241	3995	3009	9258	18455	14857
Public administration and defence	0	0	0	0	0	0	25	8	1259
Education	3	0	439	18	0	1	111	0	9
Health and social services	58	109	55	2373	829	265	2287	70	52
Community, social and personal service activities	9119	2077	773	755	7920	786	9873	765	3578
Other services	23	26	0	31	2680	0	0	0	0
Total	33351	20821	28532	51239	60056	77989	99592	218467	256838

Source: UNCTAD, 2000a.

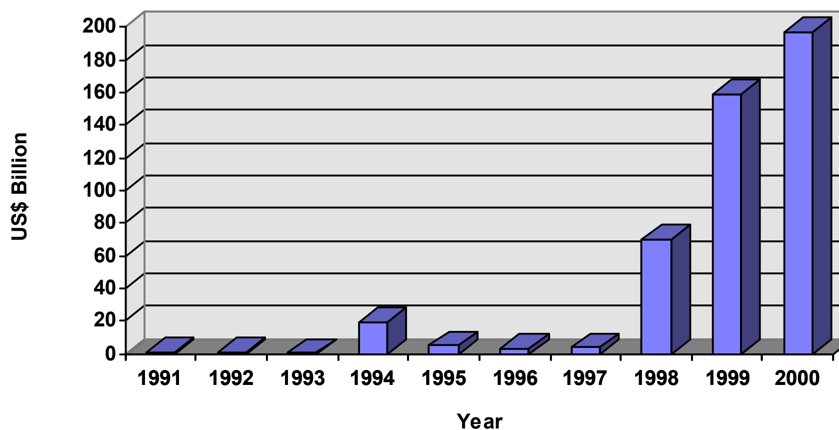
Note: Data include Japan, United States, and the East and Southeast Asian developing economies.
The values are based on 1995 constant US dollar price.

The increasing imbalance between purchases and sales of cross-border M&As

The APEC economies as a whole are net sellers in cross-border M&A transactions. This trend continued throughout the 1990s and the value of net sales increased rapidly since 1998 (Figure 5). The increasing imbalance between purchases and sales of cross-border M&As in APEC economies is largely explained by the fact that European firms often target APEC economies' firms, in particular the UK firms often target US firms.

There are several reasons for this imbalance. First, increasing investment and trade liberalisation and deregulation in the APEC region has greatly facilitated cross-border M&A activities. Second, fast economic growth in the APEC economies, particularly in the United States, Australia, China and other East and Southeast Asian economies has attracted a large number of firms outside the APEC region, especially European firms, into the APEC economies' markets. Third, the financial crisis of the late 1990s in several East and Southeast Asian economies also contributed to the surge of cross-border M&As sales in the APEC economies. The net sale position in cross-border M&As has brought a large amount of capital into the APEC economies and it has been very important for their sustained economic growth. This trend is likely to continue in the foreseeable future.

Figure 5 Net sales of cross-border M&As in APEC



Source: UNCTAD, 2001.

Definitions and classifications of cross-border M&As

Mergers and acquisitions have different consequences with respect to legal obligations, acquisition procedures, and tax liabilities (Marren, 1993).

In a cross-border merger, the assets and operations of two firms belonging to two different economies are combined to establish a new legal entity. The target company ceases to exist as a separate entity. The transaction can be executed through an exchange of stock or assets. The procedures for executing a merger transaction tend to be fairly straightforward. Cross-border mergers often require the approval of both the acquiring and target firm's shareholders and the acquiring firm assumes all of the target's assets and liabilities. There are two forms of cross-border merger:

- merger by absorption, in which one company absorbs one or more other companies and the absorbed companies are dissolved and
- merger by establishment, in which two or more companies are merged into a newly created company and the parties to the merger are dissolved.

In a cross-border acquisition, the control of assets and operations is transferred from a local to a foreign company, the former becoming an affiliate of the latter. Cross-border acquisitions include full (foreign interest of 100 percent), majority (foreign interest of 50-99 percent), and minority (foreign interest of 10-49 percent) acquisitions. Acquisitions involving less than 10 percent are classified as portfolio investment.

Cross-border acquisitions can take two forms: asset acquisitions and share acquisitions.

- In an asset acquisition, an acquiring company purchases part or all the assets of the target. The target remains legally in existence after the transaction, although it may be liquidated after a major asset sale to return money to the shareholders. The transaction is normally executed by the management of both the target and the acquiring firm.
- A share acquisition occurs when the acquiring company buys shares in the target company from individual shareholders. If the company shares are privately held, the acquirer can deal with the private owners individually. If the target is a wholly owned subsidiary of another company, the transaction is conducted by the

management of the acquiring firm and the target's parent. If the share of the target is publicly held, the acquiring firm may have to deal with a large group of disorganised shareholders. In this case, a tender offer is usually announced for the shares outstanding. An advantage of share acquisitions is that they tend to be easy to execute, and can be accomplished quickly.

Acquisitions dominate cross-border M&A transactions. In the period of 1987 to 1999, more than 97 percent of cross-border M&As by number were acquisitions. Full acquisitions accounted for more than half of all cross-border M&As in 1999. However, in developing economies, about one-third of acquisitions by foreign firms were minority (foreign interest of 10-49 percent) acquisitions, compared to less than one-fifth in industrial economies (UNCTAD, 2000a). This may reflect the differences of government regulations toward cross-border M&As between developing and industrial economies.

In terms of the relationship of the acquiring and the target companies, cross-border M&As can be classified as horizontal, vertical or conglomerate.

- *Horizontal* cross-border M&As take place between competing firms in the same industry. This category has grown rapidly recently because of the global restructuring of many industries in response to technological change and liberalisation. Industries in which such cross-border M&As has been observed are pharmaceuticals, automobiles, petroleum and, increasingly, several services industries.[3]

- *Vertical* cross-border M&As take place between firms in client-supplier or buyer-seller relationship. Typically they seek to reduce uncertainty and transaction costs in forward and backward linkages in the production chain, and to benefit from economies of scope. It is also possible that a buyer could be seeking to control access by its competitors to some important input. Cross-border M&As between

[3] The focus on 'the same industry' in this definition of horizontal M&As is a standard approach from a perspective on determinants of investment strategy and according to available statistics. When considering competition policy issues and implications of such mergers, it is important to focus on markets rather than industries.

parts and components makers and their clients (such as final electronics or automobile manufacturers) are good examples.

- *Conglomerate* cross-border M&As take place between companies in unrelated activities. They seek to diversify risk and attain economies of scope.

Most cross-border M&As are horizontal, in the period of 1987 to 1999, over 60 percent of the value of cross-border M&As were horizontal, around 30 percent were conglomerate and less than 10 percent were vertical (UNCTAD, 2000a).

Cross-border M&As can also be classified as ‘friendly’ and ‘hostile’. In a friendly M&A, the board of a target firm agrees to the transaction. However, a hostile M&A is undertaken against the wishes of the target firm and the board of the target firma rejects the offer. The overwhelming number of cross-border M&As are friendly. Hostile cross-border M&As accounted for less than 5 percent of the total value and less than 0.2 percent of the total number of cross-border M&As during the 1990s. Most hostile cross-border M&As occur in the industrial economies. Over the period 1987 to 1999, of the 104 hostile cross-border M&As, 100 targeted industrial economy firms and only 4 targeted developing economy firms (UNCTAD, 2000a).

Cross-border M&As can be financed in several ways, including FDI (purchase of foreign equity share at least 10 percent of the total equity), portfolio equity investments (less than 10 percent of the total equity), domestically raised capital, and capital raised from international capital markets. Most cross-border M&As are financed through FDI in industrial economies.

Changes in the levels of cross-border M&As are not always reflected in changes in FDI flows. The foreign equity component, which is classified as an FDI flow, comprises only a part of a cross-border M&A transaction, namely the foreign equity component of these transactions with a share of the total equity of at least 10 percent. It is, therefore, possible to witness a large increase in cross-border M&As that is not fully reflected in FDI flows. However, there is a close relationship between movements in cross-border M&As and FDI flows at least in the industrial economies.

Motivations for cross-border M&As

Cross-border M&As are one mode of FDI entry into foreign locations. The OLI (ownership advantage, location advantage and internalisation advantage) paradigm (Dunning, 1993) is the most influential explanation for international production. It does not explicitly distinguish between different modes of entry and was formulated primarily in reference to greenfield FDI. However, it does provide a useful theoretical framework to analyse and explain the motives and causes of FDI through the mode of cross-border M&As. The OLI paradigm is applied to cross-border M&As in Table 4.

Table 4 The OLI paradigm and cross-border M&As

Type	Horizontal	Vertical	Conglomerate
Mergers	O: Both firms have O advantages complementing each other in scale, synergy, finance or market power. L: Standard location factors are not relevant where two TNCs merge their global production systems. I: Both firms seek to gain economies of scale by internalising joint advantages. Joint internalisation differs from "internalisation" in usual OLI terms, but determinants (transaction costs in some sense) are similar. Mergers provide a much faster way of exploiting each other's advantages.	O: Both firms have O advantages that complement each other in different processes of the production chain. L: As with greenfield FDI, but also see horizontal mergers. I: Merging firms both seek to gain security, information, finance or market power, and to reduce transaction costs.	O: Both firms have O advantages in unrelated activities that may have economies of scope, but not technological complementarity. A merger is thus not based on O advantages in the usual sense; it may just involve access to finance. L: Mainly market size, growth or prospects of capital appreciation, not location advantages in the OLI sense. I: Merging firms seek a larger capital base or economies of scope, but are not internalising their O assets to save on transaction costs.
Acquisitions	O: Acquiring firms tend to have greater O advantages than acquired firms, or seek specific new O advantages (technology, contacts, etc.). L: As with greenfield FDI, except that many L advantages are "embodied" in the acquired firm. I: As with greenfield FDI, acquiring firms strengthen their competitive positions by internalisation.	O: Acquiring firms have a stronger financial or managerial base that allows them to acquire vertically linked firms abroad. L: As with horizontal acquisitions. I: As with greenfield FDI, acquiring firms strengthen their competitive positions by internalisation.	O: Acquiring firms have greater financial and/or managerial resources, but no O advantages in the usual sense. L: Mainly market size and growth and prospects of capital appreciation, not location advantages. I: Acquiring firms seek diversification or economies of scope, but are not internalising in an OLI sense.

Source: UNCTAD (2000a)

Apart from the general explanations of the paradigm, there are some specific factors affecting the motivations for firms to choose cross-border M&As as a vehicle for

investment in foreign locations. Among others, speed and access to proprietary assets are particularly important.[4]

Cross-border M&As are the fastest means for firms to expand their production and market internationally. When time is vital, takeover of or merger with an existing firm in a new market with an established distribution system is far more preferable to developing a new local distribution and marketing network. For a latecomer to a market or a new field of technology, cross-border M&As can provide a way to catch up rapidly. With the acceleration of globalisation, enhanced competition and shorter product life cycles, there are increasing pressures for firms to respond quickly to opportunities in the fast changing global economic environment. This is especially highlighted by the fast development and increasing competition in the information and communication technology industry.

To access proprietary assets is another important motivation for firms to undertake cross-border M&As. Merging with or acquiring an existing company is the least-cost, and sometimes the only, way to acquire strategic assets, such as R&D or technical know-how, patents, brand names, local permits and licences, and supplier or distribution networks, because they are not available elsewhere in the market and they take time to develop. Such assets may be crucial to increase a firm's income-generating resources and capabilities (Dunning, 2000).

Although speed and access to proprietary assets are the main advantages of cross-border M&As, other factors also affect the decision to undertake cross-border M&As, such as the search for new markets and for market power, efficiency gains through synergies, size or diversification, and financial motivations.

The search for new markets is a constant concern for firms. Through cross-border M&As, firms can quickly access international new market opportunities. By taking over an existing local company, the acquiring firm can immediately have access to the

[4] See e.g. Ravenscraft and Scherer (1987), Scherer and Ross (1990), Hopkins (1999), Mueller (1980), and Brealey and Myers (1988) for a discussion on different motives for M&As.

local network of suppliers and customers. Cross-border M&As can also be motivated by the pursuit of market power.

Efficiency gains can be found through synergies in cross-border M&As. Synergies can be static or dynamic. Static synergies include the pooling of management resources, revenue enhancement by using each other's marketing and distribution networks, purchasing synergies, economies of scale in production leading to cost reductions, and the avoidance of duplication of production, R&D or other activities. Dynamic synergies involve the matching of complementary resources and skills to enhance a firm's innovatory capabilities with long-term positive effects on sales, market shares and profits. The search for static synergies may be particularly important in industries characterised by increased competitive pressure, falling prices and excess capacity, such as in the automotive industries. Meanwhile, dynamic synergies may be crucial in industries experiencing fast technological change and that are innovation-driven, such as in information technology and pharmaceuticals.

Size is important in operations requiring economies of scale, large expenditures for R&D and the expansion of distribution networks. Large size can create financial, managerial and operational synergies that reduce the operational vulnerability of firms. Another advantage of size is that larger firms with multiple operations across geographical locations can have an advantage in the collection and adoption of new information and innovation.

The desire for risk reduction through product or geographical market diversification is another driving factor. Firms may make cross-border M&As on the basis that industry returns across economies may be less correlated than within an economy (Vasconcellos and Kish, 1998). As intensified global competition and rapid technology development have led firms to focus on their core activities, the need for product diversification has become less important (Morck and Yeung, 1999), although geographical diversification plays a role.

There can be financial motives behind cross-border M&As. Stock prices do not always reflect the true value of a firm. Bad management of a firm, imperfections in the capital

market and major exchange rate rearrangements may provide short-term capital gains through acquiring an undervalued firm. This motivation is particularly important in the case of portfolio-type cross-border M&As and in those host economies which have poorly developed capital markets or are in financial crisis.

Firms' motivations are the primary determinant of decisions to undertake cross-border M&As. However, changes in international economic and regulatory environment have greatly promoted and facilitated cross-border M&As. Such changes include technology, the regulatory framework and capital markets.

Some firms seek to maintain a lead in innovation. In such an environment, one of the quicker ways for firms to share innovation costs is through cross-border M&As. Participating firms can gain access to new technological assets and enhance their innovatory capabilities. Such proprietary asset-seeking cross-border M&As from industrial and increasingly from developing economies are becoming a more important form of FDI. It will become even more common as intangible, knowledge-based assets and access to a pool of skilled people and work teams become more important to competitiveness in an open economy.

Changes in the policy and regulatory environment during the past decade have provided more space for international production systems to expand. The important changes in policy and regulatory environment are the liberalisation of FDI and trade regimes, privatisation and the deregulation of various markets.

The liberalisation of FDI regimes throughout the world has continued typically on a unilateral basis. Most economies are now trying to attract FDI, not only by removing restrictions, but also through active promotion and by providing high standards of treatment, legal protection and guarantees. Examples of such changes relevant to cross-border M&As include the removal of compulsory joint venture requirements, restrictions on majority ownership and authorisation requirements. The international regulatory framework has also been strengthened, especially through the conclusion of bilateral investment protection and double taxation treaties. Multilateral agreements

support these trends, for instance, the WTO's Trade-Related Investment Measures (TRIMs) Agreement and the General Agreement on Trade in Services (GATS).

In most APEC economies, the laws dealing with FDI apply to both greenfield FDI and cross-border M&As. Therefore, the liberalisation of FDI regimes has also facilitated the growth of both modes but some economies apply specific policy instruments to cross-border M&As. First, in some economies special authorisation is required, for example, in China, Malaysia, Canada, and New Zealand. Second, some economies screen cross-border M&As for particular purposes, for example national security considerations in the United States and Australia. Third, governments may reserve the right to approve some proposed investment projects and reject or modify others to preserve particular public interests (APEC, 1999).

Practice for dealing with cross-border M&As has also changed over time. In the APEC member economies, for example, Korea had not allowed foreign purchases of majority interests in local firms before 1998, but in the face of the East Asian financial crisis, it opened nearly all industries to cross-border M&As (APEC, 1999). In response to the financial crisis, Thailand liberalised its regulatory regime for cross-border M&As and even promoted them (Brimble and Sherman, 1999).

In parallel with investment liberalisation, there has been widespread privatisation and deregulation, most notably in such service industries as telecommunications, transportation, power generation and financial services. These changes have provided another stimulus to cross-border M&As. Privatisation programs in many developing economies and economies in transition have increased the availability of domestic companies for sale. Previously state-owned utility companies, for example, facing new competitive pressures at home, have responded by becoming dynamic international investors. Previously homebound activities, such as water supply, power generation, rail transport, telecommunications, and airport construction, are now undertaken by transnational operators.

Cross-border M&As have been facilitated by changes in world capital markets. The liberalisation of capital movements, the application of new information technology,

more active market intermediaries, and new financial instruments have had a profound impact on cross-border M&A activity worldwide. Whereas the liberalisation of capital markets since the mid-1980s had already greatly facilitated the growth of cross-border M&As, most industrial economies now have completely liberalised their capital accounts, with virtually unrestricted facilities for cross-border loans and credits, foreign currency deposits and portfolio investment. More recently, financial transactions have also been substantially liberalised in many developing economies especially in the APEC region.

Impact of M&As on corporate performance

The impact on corporate performance after M&As is a very important issue not only to the companies and shareholders directly involved but also to the host economies in which the transactions take place. Although there are many successful M&As deals, most M&As, as reported in the *Financial Times* (12 April 2000) and revealed by a large number of studies, fail to deliver the expected financial gains. Therefore, there is much controversy surrounding the question of post M&A corporate performance.

Studies on the impact of M&As on corporate performance fall into two main groups in the finance literature and the management literature. In the finance literature, corporate performance is measured by comparing the returns earned on a portfolio of acquiring firms compared to some risk adjusted benchmark portfolio return (Cooper and Gregory, 2000). The finance literature suggests that M&As at best do not add value to the acquiring firms, and that more probably they are seriously detrimental to shareholder wealth in the longer term (Carper, 1990; Datta, Pinches and Narayanan, 1992; Holl and Kyriazis, 1997; Loderer and Martin, 1992; Agarwal, Jaffe and Mandelker, 1992; Rau and Vermaelen, 1998; Lubatkin, Srinivasan and Merchant, 1997).

By contrast, the management literature has assessed the performance of acquiring firms using a more diverse range of tools, including questionnaires and case study investigations of acquiring firm management. There are three main bodies of management literature which discuss the determinants of M&A on corporate performance (Schoenberg, 2000). The first is the "strategic fit" literature, which

focuses on the link between performance and the strategic attributes of the combining firms, in particular, the extent to which a target company's business should be related to that of acquirer (Kusewitt, 1985; Lubatkin, 1987; Singh and Montgomery, 1987; Seth, 1990; Flanagan, 1996; Brush, 1996; Capron, Dussauge and Mitchell, 1998; Farjoun, 1998; Capron, 1999). The second is the "process" literature, which focuses on the important role that the choice of M&A process can play. The studies highlight that inappropriate decision-making, negotiation and integration processes can impede adequate consideration of strategic and organisational fit issues and so lead to inferior M&A outcomes (Jemison and Sitkin, 1986; Hunt, 1990; Haspeslagh and Jemison, 1991; Pablo, Sitkin and Jemison, 1996; Singh and Zollo, 1998). The third is the "organisational fit" literature, which attempts to understand how the organisational human resources aspects of an M&A influence the subsequent performance of union. This stream of literature has its origins in the human resource, organisational behaviour and strategic management disciplines. They provide both theoretical and empirical perspectives on the factors influencing organisational and cultural compatibility (Sales and Mirvis, 1984; Napier, 1989; Schweiger and Walsh, 1990; Cartwright and Cooper, 1993; Very, Lubatkin and Calori, 1996; Morosini, Shane and Singh, 1998). Poor management of the strategic fit, the process or the organisational fit account for many M&A failures (Cooper and Gregory, 2000).

The two groups of studies focus on different aspects in evaluating corporate performance after M&As. But studies from both the finance and management literature have found that most M&A deals have a negative impact on corporate performance in terms of the acquiring firms' share prices and profitability (Jensen and Ruback, 1983; Ravenscraft and Scherer, 1987; Magenheim and Mueller, 1988; Mueller, 1996; Sirower, 1997; Bild, 1998; Markids and Oyon, 1998; Schenk, 2000). Indeed, broader surveys reveal that 43 percent of cross-border M&As fail to produce a financial return in excess of the acquirer's cost of capital (Bleeke, Isono, Ernst and Weinburg, 1993), while 45 percent fail to meet their initial strategic objectives (Rostand, 1994). Several management surveys of predominant cross-border M&As in the mid-1990s concluded that the value of shares held by owners declined in more than half of the cases examined, while increases in the value of shares followed only a small proportion of all M&As (AT Kearney, 1999; KPMG, 1999). Also a large number of studies found strong

evidence of negative performance in long-term profitability after M&As (Scherer, 1988; Agarwal, Jaffe and Mandelker, 1992; Anderson and Mandelker, 1993; Datta and Puia, 1995; Loughran and Vijh, 1997; Dickerson, Gibson and Tsakalotos, 1997; Gregory, 1997; Bild, 1998; Rau and Vermaelen, 1998). The most exhaustive study of post merger performance, covering almost 6000 cases, again found poor financial results from M&As (Ravenscraft and Scherer, 1987).

These findings support the view that a large number of M&As do not produce better results in terms of share prices and profitability of acquiring firms. However, several points should be kept in mind in explaining the findings. First, most studies focused on domestic M&As and were based on data from the United States and the United Kingdom, and there is little evidence from developing economies and economies in transition. Second, except for a few surveys, most studies were based on the data from the 1970s and 1980s, and the experience in the 1990s has not been fully explored in the literature. Third, the use of appropriate criteria is very important in assessing the "success" or "failure" of M&As. As Hopkins (1999) pointed out: "If failure is used in an extreme sense, such as the sale or liquidation of business, then the rate of failure is relatively low. If failure is the lack of attainment of management's financial objectives, then the rate of failure is high" (p. 220). And finally, it is reasonable to consider the counterfactuals when assessing the impact of M&As on corporate performance. What would have happened if a firm had not undertaken a particular merger or acquisition?

The poor corporate performance of the acquiring firms after M&As may be due to a variety of factors. A recent survey of Forbes 500 CEOs (Schmidt, 1999) identified the factors contributing to M&A failure by using a 7-point scale where higher scores indicate a greater contribution to failure. It was found that incompatible culture (5.60), inability to manage targets (5.39), inability to implement change (5.11), clash of management styles (5.11), and incompatible marketing systems (4.01), were among the top 10 reasons cited. Poor strategic rationale for the M&A, hubris of acquirer managers leading to an excessive acquisition premium, flawed implementation of post M&A integration, faulty financial evaluation of M&A benefits or just bad luck might also be contribute to an M&A failure (Sudarsanam, 2000). However, one important factor is the quality of corporate governance. Poor corporate governance in the acquirer firms

may have led to inadequate monitoring of the various stages of the M&A process, including pre M&A evaluation of target, deal structuring and negotiation, and post M&A integration..

The studies mentioned above are mainly focused on the performance of an acquiring firm or a firm as a whole after a merger or acquisition. There are also some studies which focus on the impact of M&As on the target companies or target plants after takeover. Although these studies have produced mixed results, on average, they found that the target firm shareholders experience significant positive returns from M&As (Datta, Pinches and Narayanan, 1992; Jensen and Ruback, 1983; Lubatkin, Srinivasan and Merchant, 1997; Schweiger and Goulet, 2000). Therefore, the shareholders in an acquired firm benefit from a merger or acquisition. To the extent that shares in a domestic firm in a developing APEC economy are held by local citizens (or by government), the acquisition of that firm will result in a wealth transfer to them. For example, in Thailand local firms restructured through cross-border M&As after the financial crisis, especially in the public sector, have shown stronger growth in share prices and better prospects (Brimble and Sherman, 1999).

Other studies found that M&As have a positive impact on the productivity of the acquired firms (Lichtenberg and Siegel, 1987; Lichtenberg, 1992). For example, Canadian plants that were taken over in the 1970s achieved higher productivity increases than those that did not experience a change in ownership (Baldwin, 1995). A Swedish study (Moden, 1998) of ownership changes undertaken during 1980-1994 found that, prior to takeover, the average labour productivity of the target firms was lagging behind the industry average. However, after an acquisition, firms taken over by foreign investors showed a substantial increase in labour productivity relative to the industry average. In addition, compared with both the industry average and with the acquired firms in domestic takeovers, foreign acquisitions developed more favourably in terms of total factor productivity, employment and market shares. Similar observations have also been made in Argentina. Compared with companies that were not taken over, acquired companies experienced stronger growth rates of sales, productivity, employment and exports. Moreover, acquired firms reported stronger organisational and technological improvements. These results apply to both domestic

and cross-border M&As compared with non-acquired companies (Chudnovsky and Lopez, 2000). More evidence of the positive impact of cross-border M&As on acquired firms have emerged from the transition economies in the Central and Eastern Europe. For example, in Poland the performance of the enterprises privatised through cross-border M&As, both in terms of qualitative changes and of financial measures, have been better than that of the firms privatised locally (Uminski, 2001). In the Czech Republic firms privatised through cross-border M&As achieved productivity growth higher not only than the local firms but also than the greenfield FDI firms (Zemplinerova and Jarolim, 2001).

Although a large number of M&As would not produce better results with regard to the performance of a firm as a whole, there is a positive impact of M&As on the performance of target companies. This finding is especially relevant to those host economies that are experiencing large-scale privatisation of state-owned enterprises and that are in financial crisis. Cross-border M&As can play a positive role in improving productivity of acquired firms and in promoting economic restructuring of host economies.

Impact on the host economy

Theoretically, both cross-border M&As and greenfield FDI are foreign investments from a host economy's point of view. However, there are some concerns that cross-border M&As as a mode of FDI entry are less beneficial for economic development than greenfield FDI. The essential concern is that cross-border M&As do not add to productive capacity at the time of entry, but simply transfer assets and ownership from domestic to foreign hands. This transfer is sometimes accompanied by the reduction in production and R&D activities and employment. It may also reduce competition in domestic market and add to the market power of the foreign acquirers.

The concerns are not only economic, but also social, political and cultural. The fact that many cross-border M&As are infrastructure-related is directly linked to social and political opposition. It can be an important political issue if the ownership of the national telecommunications or electricity or water provider is to switch to foreigners. In industries like the media and entertainment, cross-border M&As may seem to threaten national culture or identity. A large shift of ownership of important enterprises from domestic to foreign hands may be seen as eroding national sovereignty.

Therefore, it is valuable to evaluate the impact of cross-border M&As on host economy economic development. The analysis can be carried out by comparing the impact of cross-border M&As with greenfield FDI in order to evaluate the relative merits of these two types of foreign investments. Both short-term and long-term effects can be taken into account in assessing the impact of these two kinds of foreign investments on host economy economic development.

Foreign financial resources

Greenfield FDI and cross-border M&As bring foreign financial resources to a host economy, given that both modes of entry are not financed by locally raised capital. Foreign financial resource inflows through greenfield FDI manifest themselves in new production facilities, while inflows through cross-border M&As place investible resources in the hands of local owners in the form of cash or disposable shares.

However, in terms of the financial impact on host economy, there are some differences between the two modes of entry because cross-border M&As may highlight the problem of pricing of firms' assets and the risk of asset stripping.

When equity markets are underdeveloped or economic systems are in transition, it may be difficult to price assets correctly. If an enterprise is sold at a price below its long-term value, there is a loss to the host economy. Experiences from economies in transition show that in the absence of equity markets there can be major problems in pricing the assets of state-owned enterprises. In some cases, the possibility of undervaluation increases if the negotiating position of the host economy is weak, or if the host economy does not make potential investors compete through bidding (Samonis, 2000). In other cases, the situation is the opposite. For example, China's central authority is particularly concerned about undervaluation of state-owned assets sold or contributed to foreign investors. Thus, before the transaction, the Chinese target company must be appraised by State-owned Assets Administration Bureau for its asset value. A recurring problem with the asset evaluation is that the Chinese appraisers, who typically base their valuation on replacement value less depreciation, often grossly overvalue the assets to be acquired. As a result, many potential cross-border M&A deals are stopped (Chen Chunlai, 2001).

Under economic or financial crises, firms are usually significantly under-valued against their long-term values because the owners of firms are critically short of funds and there are few buyers. In this situation, foreign investors can acquire local firms at cheap or so-called "fire-sale" prices. Following the East Asian financial crisis, there were complaints that post-crisis asset acquisitions by foreign investors took place at "fire-sale" prices. This is not an easy proposition to evaluate. While some asset prices dropped precipitously after the crisis, it is not clear whether these prices were below the assets' long-terms values. Krugman (1998) suggests that the recent asset sales in the East Asia could be interpreted in two very different ways. Pre-crisis asset values may have been inflated by implicit guarantees that ultimately failed, so that the crisis restored asset values to their appropriate levels. In that case, the assets were sold at values which reflected the long term stream of returns. The alternative explanation for M&A activity in the crisis economies is that excessive exchange rate depreciation,

perhaps the result of contagion in international markets, forced domestic firms to sell assets to pay off short-term debts. Foreign firms that had enough liquidity purchased these domestic firms or projects and generated a stream of profits that more than justified their liquidation values. Under these assumptions, there was a transfer of wealth from the domestic economy to foreigners, who bought assets at prices below their values based on long-term returns.

Even in such cases, and even if the foreign investors were to sell their acquisitions for a profit when markets recovered, cross-border M&As can create a net gain to a host economy if the acquired firms would otherwise have gone bankrupt. Even so, there is little evidence to suggest that most M&As in Asia were undertaken for short-term financial reasons (Brimble and Sherman, 1999; Zhan and Ozawa, 2000). In addition, the limited evidence available goes against the hypothesis that significant amount of assets of Asian economies following the financial crisis were sold at fire-sale prices (Brimble and Sherman, 1999; Mody and Negishi, 2001).

There is a concern about asset stripping associated with cross-border M&As. The acquired firms can be broken up by corporate raiders and their component parts sold off at a profit. Proceeds of assets sales might be repatriated to home economies. Asset stripping is often regarded with disfavour as it may cut productive capacity. On other hand, the process of asset stripping can be an important part of the process of adjustment of a business. In the case of privatisation, concerns about negative effects of asset stripping can be guarded against by governments retaining a "golden share" to enable them to influence or even veto corporate decisions they consider undesirable (UNCTAD, 2000a).

Capital formation

Greenfield FDI is an investment in new productive facilities and, therefore, it adds to the productive capital stock to the host economy once a project is completed. Cross-border M&As transfer assets from a host economy owner to a foreign TNC and provide funds to local asset owners. Proceeds obtained through cross-border M&As can then be used for other productive purposes, or reallocated through the financial system.

In the long run, the acquirer may carry out modernisation and capacity expansion or induce other related investments. New incremental or supplementary capital formation may then eventually occur in the form of both sequential and associated investment which sometimes is larger than the original purchase, especially in the cases of privatisation. For example, in Peru, privatisation brought in an FDI stock of US$8.5 billion by the end of 1999, and the new owners committed themselves to additional investments of around US$7 billion for modernisation and expansion of acquired facilities (UNCTAD, 2000b). In Korea, cross-border M&As led to larger sequential investments than greenfield FDI: during the period of 1997-1999, the ratio of sequential to new investments was 125 percent for cross-border M&As and 85 percent for greenfield investments (Yun, 2000). Similar evidence has also been observed in Thailand and other Asian economies (Brimble and Sherman, 1999; Mody and Negishi, 2001). Furthermore, if the acquired firm would otherwise have gone bankrupt, thus decreasing the capital stock involved, cross-border M&As may have played a role in maintaining or revitalising a host economy's capital stock. Therefore, in the long run, both greenfield FDI and cross-border M&As can contribute to the capital formation of the host economy.

Employment

Greenfield FDI will create job opportunities, increase the demand for certain types of workers and may lead to a reallocation of the labour force. In contrast, the employment effects of cross-border M&As are more varied. While no new production capacity is created in a merger or an acquisition, and while job reduction may take place if an acquisition involves a troubled high-cost firm that needs to be restructured, the purchaser may also create a more productive business with a higher potential for growth. Cross-border M&As can generate employment if a TNC turns an acquired firm into a successful unit as part of its corporate network, and if sequential investments take place and if the linkages of acquired firms are retained or strengthened. Corporate decisions after an acquisition might also lead to the immediate expansion of capacity. Furthermore, the freed up funds can be reinvested creating employment opportunities in other businesses. Studies have also found that in crisis or transition economies, the

employment conservation effect of cross-border M&As may be quite strong (Zhan and Ozawa, 2000; Hunya and Kalotay, 2000).

In terms of the effects on employment skills, there may be a risk of skill loss if an acquiring firm transfers abroad the best jobs or the most qualified employees of an acquired firm. However, this is not likely in most cases; on the contrary, acquired firms are more likely to benefit from an inflow of new skills as technologies and management systems are integrated into the parent TNCs.

Technology transfer

Transnational corporations are the leading innovators and are also the leading suppliers of technologies to developing economies and economies in transition through FDI (UNCTAD, 2000a). They can also stimulate the development of innovative capacities of host economies. Therefore, both cross-border M&As and greenfield FDI can lead to similar technology transfers and upgrading in affiliates established in host economies. However, the content of the transfer depends on the situation of the acquired firms in a given context of local factor endowments, market conditions and the orientation of affiliates.

The speed of technology transfer through cross-border M&As depends on the efficiency of the implementation of the cross-border M&A transactions and the absorptive capacity of the local enterprises. The better managed the cross-border M&A process and the greater the technological strengths and capabilities of acquired firms, the greater the likelihood that cross-border M&As would contribute to a rapid build-up of technological competence and activity.

Cross-border M&As can be followed by transfer of new or better production technology, organisational and managerial practices especially when acquired firms are restructured to increase the efficiency of their operations. Foreign affiliates established through cross-border M&As may be able to absorb technologies faster because of capabilities already existing in the acquired firms. Moreover, cross-border M&As may diffuse technology faster because their linkages are likely to be stronger.

Market structure and competition

Market competition is desirable because it stimulates and improves efficiency, resulting in lower prices for consumers. The initial entry of TNCs to a new market may increase the number of firms, in particular, in oligopolistic industries where the nature of the ownership advantages leads to a greater role for TNCs. It can also force less efficient firms out of the industry and raise the concentration level. This is not necessarily anti-competitive. If markets are open, the result can be a more efficient and competitive industrial structure. Much depends on the openness of a market to trade, the intensity of local competition, the actual conduct of leading firms and the nature of technology. The chances of abuse of market power are much greater in protected markets than in open markets. There is evidence that the entry of TNCs puts competitive pressure on domestic firms, thus leading to an increase in product quality, variety and innovation in host economies.

What difference does the mode of foreign investment entry make to market structure? Generally, greenfield FDI can enhance local competition as it adds to the number of firms in existence. Cross-border M&As may simply maintain the level of competition that existed pre-merger or where the acquiring firm is already present in the host economy in the same market as its acquisition, cross-border M&As will increase concentration. On the other hand, even for M&As in the same market, higher concentration by itself does not indicate anti-competitive behaviour. In addition, where a market is open to import competition, a high level concentration among domestic suppliers need not necessarily make a difference to the extent of competition. Cross-border M&As can also challenge established domestic oligopolies by merging with other domestic firms to create effective rivals.

On the other hand, if the acquiring firm were part of a small number of firms at the global level, the takeover might reduce global competition as well as competition in the host economy. Furthermore, the parties need not be located in the same market for this effect to be observed. For instance, a merger may increase the potential for keeping rivals from sources of supply. As these examples illustrate, the competition effects have to be assessed in each case.

One of the prominent characteristics of infrastructure industries has been natural monopoly, leading to a large array of government regulations and rules. Industrial economies, such as Australia, Canada and the United States, are experimenting with different policies, like introducing competition in particular segments where several producers can operate (e.g. power generation), or regulating and assessing the operation of monopolies in different ways.

In APEC economies, especially in developing economies, a large percentage of cross-border M&As are in infrastructure sectors, especially in telecommunications and transportation. These can often raise different competition and other policy issues from cross-border M&As in manufacturing sectors. In a telecommunications, railroad, electricity or water cross-border M&A, questions are not directed to potential closures of facilities, but whether the host economy will be able to detect and prosecute any anticompetitive conduct undertaken by the merged or acquired entities. Correspondingly, foreign investors must assess the risk of expropriation of their sunk capital, which in turn has an impact on their commercial decisions as to whether to make capital improvements in the facilities they acquired.

Evidence from both developed and developing APEC economies suggests that the majority of M&As do not have negative effects on competition. In the United States, in fiscal year 1999 only 1.6 percent of 4679 M&As transactions notified to anti-trust authorities resulted in enforcement actions, with only about 1 percent being challenged in the end. In Japan, all 3813 M&As notified in 1998 were cleared, although two transactions were revised in response to concerns raised during pre-notification consultation (United States, Department of Justice, 2000). In Korea, only 3 out of 132 cross-border M&As notified in 1998 raised concerns (Yun, 2000). In Mexico, all 55 notified cases of cross-border acquisitions of Mexican firms in 1997 went through unhindered as no competition risk was registered (Mexico, Federal Commission on Competition, 1997).

Overview of impact

Developing host economies can derive substantial gains from cross-border M&As. Cross-border M&As involve cross-border capital transfers that can increase total investible funds available to host economies. The benefits to capital-constrained host economies are even greater if cross-border M&As induce sequential and associated FDI by the acquiring companies and their suppliers. Cross-border M&As, like greenfield projects, can offer access to technologies that local firms do not possess. They may introduce innovative management practices in the host economy and render it easier to become part of global sourcing and marketing networks of the acquiring TNCs, thereby improving opportunities to penetrate international markets.

Cross-border M&As can be even more valuable for host economies when they prevent potentially profitable assets from being liquidated. This is especially relevant in the context of privatisation-related cross-border M&As in transition economies and sales of firms in financially distressed developing economies. The transition to a market system may leave loss-making state-owned companies with no alternative but to declare bankruptcy, unless a private investor, foreign or domestic, with sufficient resources is willing to revitalise the ailing company. Frequently, the resources have to come from abroad, given the serious financial and technological constraints facing firms in early stages of economic transition. The same thing applies to a number of developing economies in which communications, transport, energy and financial systems are privatised, or in which financially distressed firms are forced to seek buyers for their assets.

There is a possibility that cross-border M&As may have a negative impact on the process of competition. However, the specific consequences of cross-border M&As can also be influenced by government policy measures of host economies. The challenge is to ensure that systems are in place to deal with those cross-border M&As that raise competition policy concerns.

For example, pre-merger notification and the ability to enforce demands for the information necessary for an investigation, are important measures. By June 2000, some 90 economies have adopted competition laws or were in the process of doing so. Merger review systems have been widely used for this purpose in a number of

industrial economies for many years. During the past 15 years, such systems have also been adopted or strengthened in developing economies and economies in transition. In APEC, the five industrial economies all have adopted competition laws; in the sixteen developing economies, ten have adopted competition laws and in two they are under preparation. Thus, rather than applying blanket restrictions on foreign takeovers as imposed in past years under FDI laws, M&A reviews now proceed under competition laws on a case-by-case basis. By and large, M&A reviews based on competition policy do not tend to discriminate between cross-border and domestic M&As. Thus, a switch from an investment to a competition policy focus represents a step towards liberalisation.

In the increasingly integrated global economic environment, it is valuable for competition authorities to strengthen cooperation at the bilateral, regional and multilateral levels in order to respond effectively to cross-border M&As and to the risk of anti-competitive practices of firms. In the context of APEC, the industrial economies, especially the United States, have a long history of cross-border M&As and, therefore, have rich experience in making and implementing competition laws and policies. However, for the developing economies, especially economies in transition, cross-border M&As are a relatively new phenomenon, as a result, they have little experience not only in making competition laws and policies but also in enforcing such policies to deal with anti-competitive practices of firms relating to cross-border M&As.

Next steps

In parallel with global trends, cross-border M&As have become a more important source of foreign investment in APEC economies. Not only do they dominate FDI flows in industrial economies, they have also become a more and more important mode of FDI entry into developing economies and economies in transition.

However, the fast growth of cross-border M&As is accompanied by increasing concerns of their impact on the host economy, especially the developing economies. Because of the controversy surrounding cross-border M&As, a lot of studies have been conducted seeking to analyse and evaluate the impact of cross-border M&As on corporate performance and on the host economy. However, most of the studies were focused on the data from industrial economies, mainly from the United States and the United Kingdom. There is little evidence from developing economies and economies in transition. In addition, except for a few surveys, the experience in the 1990s has not been fully explored in the literature. Therefore, more careful and comprehensive studies on the impact of cross-border M&As on corporate performance and on the host economy, especially developing economies and economies in transition, are valuable. Further studies on cross-border M&As could focus on the following aspects.

- *Case studies on the impact of cross-border M&As on corporate performance*: These studies could analyse and evaluate the impact of cross-border M&As on employment, share prices, profitability, technology, innovation, entrepreneurial culture, and other synergies of the acquirer, the acquired, and the merged entity both in developed and in developing economies in APEC. Particular emphasis could be given to the cases of cross-border M&As conducted in the economies affected by financial crisis and economies in transition. The studies could cover the following major sectors: petrochemicals, automotive, electrical and electronics; financial services including banking and insurance; and infrastructure activities such as electric power, railroads and telecommunications.

- *Case studies on the impact of cross-border M&As on the host economy*: These studies would analyse and evaluate the impact of cross-border M&As on the macroeconomic environment in the host economies, including the effects on capital inflows, employment and human resource development, technology transfer and development, market structure and competition. The studies would cover cases of cross-border M&As conducted both between industrial economies, and between a developed economy and a developing economy.

- *Studies of cross-border M&A policies and regulations in APEC economies*. These studies would review the current policies and regulations relating to cross-border M&As in APEC economies and comment on (1) whether cross-border M&As require a different regulatory response compared to domestic M&As; (2) the implications of cross-border M&As for competition laws and policies; (3) the scope for cooperation in APEC economies in providing technical assistance valued by developing member economies in the design and operation of their legal infrastructure for M&As.

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