OECDpublishing

Please cite this paper as:

Kang, N. and S. Johansson (2000), "Cross-Border Mergers and Acquisitions: Their Role in Industrial Globalisation", *OECD Science, Technology and Industry Working Papers*, 2000/01, OECD Publishing.
http://dx.doi.org/10.1787/137157251088

OECD Science, Technology and Industry Working Papers 2000/01

Cross-Border Mergers and Acquisitions

THEIR ROLE IN INDUSTRIAL GLOBALISATION

Nam-Hoon Kang, Sara Johansson

OECD

Unclassified **DSTI/DOC(2000)1**

Organisation de Coopération et de Développement Economiques
Organisation for Economic Co-operation and Development

OLIS : 07-Jan-2000
Dist. : 10-Jan-2000

English text only

DIRECTORATE FOR SCIENCE, TECHNOLOGY AND INDUSTRY

DSTI/DOC(2000)1
Unclassified

STI WORKING PAPERS
2000/1
Cross-border Mergers and Acquisitions: Their Role in Industrial Globalisation

Nam-Hoon Kang and Sara Johansson

English text only

86036

Document complet disponible sur OLIS dans son format d'origine
Complete document available on OLIS in its original format

STI Working Paper Series

The Working Paper series of the OECD Directorate for Science, Technology and Industry of the OECD is designed to make available to a wider readership selected studies prepared by staff in the Directorate or by outside consultants working on OECD projects. The papers included in the series are of a technical and analytical nature and deal with issues of data, methodology and empirical analysis in the areas of work of the DSTI. The Working Papers are generally available only in their original language – English or French – with a summary in the other.

Comment on the papers is invited, and should be sent to the Directorate for Science, Technology and Industry, OECD, 2 rue André Pascal, 75775 Paris Cedex 16, France.

The opinions expressed in these papers are the sole responsibility of the author(s) and do not necessarily reflect those of the OECD or of the governments of its Member countries.

http://www.oecd.org/dsti/sti/prod/sti_wp.htm

CROSS-BORDER MERGERS AND ACQUISITIONS: THEIR ROLE IN INDUSTRIAL GLOBALISATION

Nam-Hoon Kang and Sara Johansson

This paper examines recent trends and drivers of cross-border mergers and acquisitions (M&As) which grew six-fold in 1991-98 and now account for more than 85% of foreign direct investment. They are prompted by a range of factors, including excess capacity and increased competition in traditional industries and new market opportunities in high-technology sectors. However, the main driver of M&As in place of greenfield investment is the need to acquire complementary intangible assets –technology, human resources, brand names, etc. In allowing for global industrial restructuring and efficiency gains, cross-border M&As can yield dividends in terms of company performance and profits. The extent to which they result in benefits for home and host countries is argued to be strongly influenced by policy frameworks.

FUSIONS ET ACQUISITIONS INTERNATIONALES : LEUR ROLE DANS LA MONDIALISATION DE L'INDUSTRIE

Nam-Hoon Kang et Sara Johansson

Le présent document analyse les tendances récentes en matière de fusions et acquisitions (F-A) internationales, ainsi que les éléments moteurs de ces regroupements, qui se sont multipliés par six entre 1991 et 1998 pour représenter actuellement plus de 85 % des investissements directs étrangers. Ils résultent d'une série de facteurs, notamment les surcapacités et l'intensification de la concurrence dans les activités traditionnelles ainsi que des nouveaux débouchés qui s'offrent dans les secteurs de haute technologie. Toutefois, le principal facteur qui conduit les entreprises à préférer les F-A aux nouveaux investissements est la nécessité d'acquérir des actifs incorporels complémentaires – technologie, ressources humaines, marques commerciales, etc. Les F-A internationales, qui sont à l'origine d'une restructuration industrielle à l'échelle mondiale et de gains d'efficience, peuvent avoir des effets positifs sur les résultats des entreprises. On fait valoir que les avantages qu'elles peuvent présenter pour les pays d'origine et les pays d'accueil dépendent, dans une large mesure, des cadres d'action de ces pays.

TABLE OF CONTENTS

SUMMARY

Cross-border mergers and acquisitions (M&As) have rapidly increased in recent years, accelerating the globalisation of industry and reshaping industrial structure at the international level. In the 1990s, there has been a marked tendency in foreign direct investment towards mergers and acquisitions rather then greenfield investment. The value of cross-border M&As grew more than six-fold in the period 1991-98, with an increasing tendency towards very large-scale unions. Although non-OECD countries have increased their share of cross-border mergers and acquisitions, they primarily involve OECD countries and firms. M&As are taking place in a range of industries – including mature manufacturing sectors, high-technology fields and service sectors – and reflect a need to restructure and strengthen global competitiveness in core businesses.

The driving forces underlying the trend to cross-border M&As are complex and vary by sector. Prolonged economic growth in countries such as the United States increases the capital available for industrial purchases abroad and attracts more inward investment, while the globalisation of financial markets is also a factor. In some mature industrial sectors, international competition and market pressures due to excess capacity and falling demand are driving restructuring. Technological change, particularly in information technology, facilitates the international expansion of firms, which are also seeking to capture new market opportunities in fast-changing technologies and to pool research and development costs. Enterprises increasingly seek to exploit intangible assets – technology, human resources, brand names – through geographical diversification and acquisition of complementary assets in other countries. Government policies such as investment liberalisation, privatisation and regulatory reform are also increasing the number of and access to industrial targets for acquisition.

Cross-border mergers and acquisitions can yield dividends in terms of company performance and profits as well as benefits for home and host countries when successful industrial restructuring leads to greater efficiency without undue market concentration. Benefits from such M&As are increasingly intangible and found in economy-wide spillover effects. They can help revitalise ailing firms and local economies and create jobs through the restructuring process, acquisition of technology and productivity growth. Yet countries have differed widely in their openness to M&As involving foreign firms. And in some cases, poorly functioning factor and product markets may impede the realisation of the favourable impacts of M&As in terms of economic growth and job creation. Government policies – in areas such as investment, competition, labour and technology – need to promote sufficient flexibility to enable firms to engage in necessary restructuring at the international level.

INTRODUCTION

Cross-border mergers and acquisitions (M&As), *i.e.* those taking place between firms of different national origin or home countries, have grown rapidly in the 1990s. A merger and acquisition, strictly defined, occurs when an operating enterprise acquires control over the whole or a part of the business of another enterprise. The share of cross-border M&As in overall M&As has increased dramatically in the 1990s. While there have long been many M&As targeting SMEs, the 1990s have seen an explosion in, and geographical widening of, the number and value of mega-mergers among well-known multinationals. Recent examples include the British Petroleum-Amoco and Exxon-Mobil mergers in the petroleum industry, the Daimler-Benz-Chrysler and Renault-Nissan unions in the automotive industry, the Astra AB and Zeneca Group Plc merger in pharmaceuticals, and the Vodafone Group Plc and Airtouch Communications merger in telecommunications.

Cross-border M&As must now be included among the fundamental mechanisms of industrial globalisation. The overwhelming share of flows of foreign direct investment, which are the prime vehicle for deep-rooted business engagement across international borders, now consists of mergers and acquisitions rather than greenfield investment. This has been accompanied by more diverse forms of collaboration between enterprises, such as informal alliances for research and development and other strategic purposes. Meanwhile, new channels for globalisation such as electronic commerce are supplementing more traditional modes of trade and foreign investment. And a wider range of sectors, particularly many service sectors, and countries, increasingly non-OECD countries, are represented in the current wave of industrial globalisation.

This paper aims to increase understanding of the changing patterns of industrial globalisation, the driving forces behind the recent surge of cross-border M&As, and their impact on industry and implications for government policies. The study follows up recent OECD/DSTI work on globalisation, which looks at the implications of globalisation for firm and sector performance and examines government policies implemented to fully realise the benefits of globalisation (OECD, 1999*a*; 1999*b*). It also complements the analyses of trends in foreign direct investment (OECD, 1999*b)* and of the competition aspects of mergers and acquisitions (OECD, 1988; OECD, 1994) carried out by OECD/DAFFE.

This paper first reviews recent trends in cross-border M&As in terms of value, number and geographical patterns during the period 1991-98; analyses the modes of entry for direct investments across countries, including cross-border M&As; and examines the main features of international M&As in major industries such as the automotive, telecommunications, steel, oil and gas, and pharmaceuticals. The paper proceeds to identify the main driving forces of cross-border M&As, including macro-, industry- and firm-level factors as well as new technologies and government actions. The final section discusses the potential impacts of cross-border M&As on firm and industry performance and highlights some implications for government policies.

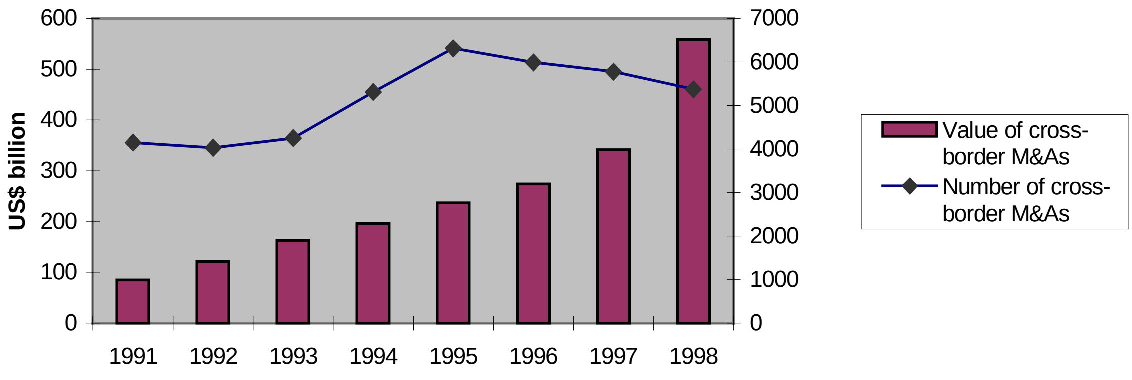
RECENT TRENDS IN CROSS-BORDER M&As

Overall trends

The value of cross-border M&As worldwide increased more than six-fold during the period 1991-98, from US$85 billion in 1991 to US$558 billion in 1998 (**Figure 1**). In 1998, cross-border M&As were worth 60% more than in 1997 and more than twice as much as in 1996. The total number of cross-border M&As also increased rapidly during the same period, from 4 149 in 1991 to 5 373 in 1998, reaching a record high 6 310 in 1995.

Cross-border M&As are also growing in size, with the average size, increasing almost five-fold during the period 1991-98, from US$21 million in 1991 to US$104 million in 1998. The tendency toward large-scale cross-border M&As has strengthened in recent years: since 1995, the value of cross-border M&As more than doubled, while the total number of cross-border M&As decreased (**Figure 1**). Thus, large-scale cross-border M&As now account for the bulk of the increase in the value of cross-border M&As. For example, in 1998, the value of the top six cross-border M&As reached US$169 billion, *i.e.* more than 30% of global M&A transaction values (**Table 1**). The deal between British Petroleum and Amoco was valued at US$61 billion, and that between Daimler-Benz and Chrysler at US$39 billion. The value of other recent cross-border mega-mergers is equally striking, exceeding US$10 billion.

Figure 1. Cross-border M&As, 1991-98



Source: KPMG Corporate Finance, 1999.

Cross-border M&As are taking place in all sectors, manufacturing as well as services. These cross-border M&As are changing the shape of industry on a global basis in sectors including the automotive, chemical and pharmaceuticals, telecommunications and financial industries. However, unlike the cross-border M&As of the 1980s, which often took place between different fields of business or industry, most recent cross-border M&As are taking place in the same or related industries (UNCTAD, 1998). This is particularly true for the very large-scale M&As. By way of illustration, the largest cross-border mergers in

1998 were among firms in the same sector: petroleum, automobile, pharmaceuticals, finance, electricity, etc. This may reflect the efforts of multinational enterprises (MNEs) to strengthen global competitiveness in their core businesses through cross-border M&As or a desire to reduce competition in increasingly globalised markets.

Even though cross-border M&As are concentrated in a few countries such as the United States, the United Kingdom and Germany, countries which were traditionally quite negative towards cross-border M&As are also becoming more acquiescent towards take-overs by foreign investors. For example, in the case of the Renault-Nissan alliance, the Japanese business community confirmed its willingness to accept greater foreign participation in Japanese firms as part of corporate reforms to tackle problems of surplus industrial capacity and debt overhangs (**Box 1**). In the case of Korea, all remaining restrictions on acquisitions by foreign investors were repealed in 1998 as part of the structural reforms in the wake of the economic crisis. M&A investments into Korea are rapidly increasing due to falling asset prices as well as to changes in business practices and the creation of an environment more favourable to foreign acquisitions.

Table 1. Top six cross-border M&As in 1998

Acquiring company	**Acquired company**	**Deal value (US$ billion)**
British Petroleum (United Kingdom) *Petroleum*	Amoco (U.S.) *Petroleum*	61.0
Daimler-Benz (Germany) *Automobile*	Chrysler (U.S.) *Automobile*	39.0
Zeneca Group Plc (United Kingdom) *Pharmaceuticals*	Astra (Sweden) *Pharmaceuticals*	34.0
Fortis (Netherlands) *Bank*	General de Banque (Belgium) *Bank*	14.0
Texas Utilities Co (United States) *Electricity*	Energy Group Plc (U.K.) *Electricity*	10.4
Seagram (Canada) *Music*	PolyGram (Netherlands) *Music*	10.4

Source: KPMG Corporate Finance, 1999.

Box 1. Mergers and acquisitions in Japan

In Japan, where corporate managers have maintained a cautious attitude towards accepting foreign capital (inward cross-border M&As), several recent cases suggest a possible shift in Japanese corporate behaviour. Nissan-Renault’s global partnership agreement in March 1999, in which Renault spent US$5.4 billion to buy a 36.8% equity stake in Nissan and a 22.5% stake in Nissan Diesel, is one example. The highlight of the alliance is Renault’s huge capital injection into Nissan and the fact that this leading Japanese manufacturer has allowed Renault’s Chief Operating Officer to formulate revival plans. In the face of a sluggish local economy and lower domestic demand, as well as increased competition worldwide, Nissan was forced to seek foreign capital.

There are other examples in the financial sector where Japanese companies have sought and accepted foreign capital through cross-border M&As: the merger of GE Capital and the Toho Mutual Life Insurance Company in April 1998, leading to the establishment of “GE Edison Life” in Japan; and the establishment of “Nikko Salomon Smith Barney”, a 1999 joint venture with a 51% stake owned by Nikko Securities and a 49% stake by TravelersGroup (Salomon Smith Barney).

Since 1980, a series of amendments to the Foreign Exchange Law have liberalised cross-border capital transactions and have contributed to these M&A activities in Japan. Still, Japanese corporate culture, based on a lifetime employment system and a lack of labour mobility, leads Japanese managers to consider M&As involving foreign firms as a measure of last resort. The resultant restructuring measures could mean a drastic cut in jobs and negative pressure from employees is quite high. As a result of the prolonged recession, many Japanese companies have had to streamline their businesses and are forced to consider M&As with domestic or foreign firms as an option enabling them to survive global competition.

It is too soon to say if this trend marks a fundamental change, with Japanese corporate behaviour becoming more open to liaisons with foreign firms. In the automotive industry, while companies like Nissan and Mazda have put themselves in the hands of foreign partners (*i.e.* Renault and Ford), other companies such as Toyota have prepared for competition by strengthening their strategic ties with Japanese partners such as Daihatsu Motor (a small vehicle company) and Hino Motors (a truck maker). The recent major bank merger (Dai-Ichi Kangyo Bank, Fuji Bank and the Industrial Bank of Japan) to consolidate operations is another example of a domestic Japanese alliance.

Inward cross-border M&As

Cross-border M&As can be either inward or outward. *Inward* cross-border M&As incur an inward capital movement through the sale of domestic firms to foreign investors (M&A sales), while *outward* cross-border M&As incur an outward capital movement through the purchase of all or parts of foreign firms (M&A purchases). However, inward and outward cross-border M&As are closely related, since M&A transactions involve both sales and purchases. Trends in cross-border M&A differ among developed and developing countries. For statistical purposes, this paper adopts the UNCTAD definition of developed countries, which includes 24 OECD countries (excluding Korea, Mexico, Poland, Hungary and the Czech Republic), plus South Africa and Israel.

Developed countries are playing a major role in inward cross-border M&As, accounting for 73% (US$1 447 billion) of the total (US$1 977 billion) during the period 1991-98 (**Tables 2 and 3**). Within this group, Western Europe and North America accounted for the bulk of inward cross-border M&As, 38% and 30%, respectively, during the same period. The United States (27%), the United Kingdom (14%), Germany (5%), France (5%) and Canada (4%) played a particularly dominant role in attracting inward M&As (**Table 4**). These five countries represented 55% ($1 066 billion) of global inward M&As between 1991 and 1998. The European Union accounted for 36% of all inward cross-border M&As during the same period 1991-98 and evidenced a marked increase in merger activity in recent years. Other developed countries such as Japan and Australia accounted for 6% of inward cross-border M&As in this period. Compared with the size of the economy, inward cross-border M&As in Japan are quite rare despite recent active M&A activities, accounting for only slightly over 1% of global inward M&As in the1990s. Companies from OECD countries accounted for almost all – 87% – of inward cross-border M&As in 1991-98.

Developing countries accounted for 27% (US$530 billion) of inward cross-border M&As during the period 1991-98 (**Tables 2 and 3**). The value of inward cross-border M&As in developing countries continued to increase rapidly – from US$14 billion in 1991 to US$108 billion in 1997 – until the onset of the Asian financial crisis. The share of developing countries in inward cross-border M&As almost doubled in the 1990s, from 16% in 1991 to 32% in 1997. However, in 1998, developing countries experienced a 27% decrease in inward cross-border M&As, for the first time in the 1990s. The sharp decrease was largely due to a 44% drop in Asian cross-border M&A sales, although some Asian countries such as Korea experienced a rapid increase in M&A sales. The value of inward cross-border M&As in 1998 in Latin America and Central and Eastern Europe remained at almost the same level as in 1997. As a result, with the sharp increase in inward cross-border M&As in developed countries in 1998, the share of developing countries in global inward M&As actually decreased to 14%, the lowest level of the decade.

Table 2. Inward cross-border M&As, by region (US$ billion)

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98
Developed countries	71.4	83.7	97.8	129.1	167.0	186.2	232.9	478.6	1 446.8
Western Europe	39.8	59.2	52.4	60.9	76.4	81.9	138.3	231.8	740.7
(EU)	(38.7)	(56.9)	(51.7)	(58.4)	(74.8)	(76.7)	(133.6)	(223.4)	(714.3)
North America	26.1	19.2	40.3	62.9	72.5	81.1	76.3	218.1	596.4
Other countries	5.6	5.3	5.1	5.3	18.1	23.2	18.3	28.7	109.7
Developing countries	13.8	38.2	64.5	67.2	70.3	88.3	108.1	79.3	529.8
Latin America	3.9	10.4	13.7	14.8	11.4	22.3	43.8	41.3	161.5
Asia/Pacific	6.4	21.2	33.5	44.0	38.6	55.5	48.4	27.1	274.8
Central & Eastern Europe	3.0	6.0	15.8	4.9	16.0	4.1	9.9	9.2	69.0
TOTAL	85.3	121.9	162.3	196.4	237.3	274.5	341.0	558.0	1 976.6

Source: KPMG Corporate Finance, 1999.

Table 3. Inward cross-border M&As, by region (%)

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98
Developed countries	83.8	68.7	60.3	65.8	70.4	67.8	68.3	85.8	73.2
Western Europe	46.6	48.6	32.3	31.0	32.2	29.8	40.6	41.5	37.5
(EU)	(45.4)	(46.7)	(31.9)	(29.7)	(31.6)	(28.0)	(39.2)	(40.0)	(36.1)
North America	30.6	15.7	24.8	32.0	30.6	29.5	22.4	39.1	30.2
Other countries	6.6	4.3	3.2	2.7	7.6	8.5	5.4	5.2	5.6
Developing countries	16.2	31.3	39.7	34.2	29.6	32.2	31.7	14.2	26.8
Latin America	4.6	8.5	8.4	7.6	4.8	8.1	12.8	7.4	8.2
Asia/Pacific	7.5	17.4	20.7	22.4	16.3	20.2	14.2	4.8	13.9
Central & Eastern Europe	3.6	4.9	9.8	2.5	6.8	1.5	2.9	1.6	3.5
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: KPMG Corporate Finance, 1999.

Table 4. Top five countries for inward cross-border M&As

		1991	1992	1993	1994	1995	1996	1997	1998	1991-98
United States	US$ billion	23.8	13.9	34.7	56.4	61.4	70.6	64.3	202.7	527.8
	Percentage	27.9	11.4	21.4	28.7	25.9	25.7	18.9	36.3	26.7
United Kingdom	US$ billion	12.1	18.7	12.0	14.5	36.4	39.2	55.4	85.6	274.0
	Percentage	14.1	15.4	7.4	7.4	15.3	14.3	16.2	15.3	13.9
Germany	US$ billion	5.0	7.7	5.9	9.9	6.2	6.7	19.3	38.0	98.6
	Percentage	5.9	6.3	3.7	5.0	2.6	2.4	5.6	6.8	5.0
France	US$ billion	5.0	8.8	5.0	12.5	12.8	11.4	14.5	24.2	94.1
	Percentage	5.8	7.2	3.1	6.4	5.4	4.2	4.3	4.3	4.8
Canada	US$ billion	2.3	5.2	5.6	6.5	11.1	10.4	12.0	15.4	68.6
	Percentage	2.7	4.3	3.4	3.3	4.7	3.8	3.5	2.8	3.5

Source: KPMG Corporate Finance, 1999.

Outward cross-border M&As

As for inward cross-border M&As, developed countries are playing a dominant role in outward cross-border M&As. Developed countries accounted for 89% (US$1 768 billion) of world outward cross-border M&As (US$1 977 billion) during the period 1991-98 (**Tables 5 and 6**). Western Europe and North America accounted for most outward cross-border M&As, 52% and 30%, respectively, during this period. Again, the United States (23%), the United Kingdom (15%), Germany (8%), France (7%) and Canada (6%) played a dominant role in outward cross-border M&As (**Table 7**). These five countries represented almost 60% (US$1 190 billion) of outward cross-border M&As from 1991 to 1998, just as they accounted for the major share of inward cross-border M&As. This implies that cross-border mergers and acquisitions, like foreign direct investment in general and trade, tend to take place among a small group of predominantly rich countries. Other developed countries such as Japan and Australia accounted for 8% of outward cross-border M&As during 1991-98. The European Union accounted for almost half of outward cross-border M&As from 1991 to 1998, and the OECD countries represented 90% of outward cross-border M&As.

Unsurprisingly, developing countries are relatively less important in outward cross-border M&As compared with inward cross-border M&As, accounting for only 11% (US$209 billion) of world outward cross-border M&As during the period 1991-98 (**Tables 5 and 6**). The share of developing countries in outward cross-border M&As has tended to increase throughout the 1990s, from 6% in 1991 to 12% in 1997. However, as in inward cross-border M&As, the value of outward cross-border M&As in developing countries in 1998 decreased to less than half of the level for 1997: from US$41 billion in 1997 to US$18 billion in 1998. In particular, outward cross-border M&As in those Asian countries which experienced the financial crisis were worth less than one-third of their 1997 value. As a result, the share of developing countries in global outward M&As fell to 3% in 1998.

Table 5. Outward cross-border M&As, by region (US$ billion)

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98
Developed countries	79.9	99.2	134.9	163.0	212.2	239.3	299.3	540.0	1 767.7
Western Europe	53.8	55.2	77.0	92.6	108.1	129.8	168.0	344.0	1 028.6
(EU)	(50.5)	(50.0)	(74.8)	(75.3)	(98.7)	(114.3)	(127.5)	(330.6)	(921.7)
North America	15.7	26.4	44.7	52.0	80.5	87.7	106.4	175.2	588.4
Other countries	10.4	17.6	13.2	18.3	23.6	21.8	24.7	20.9	150.5
Developing countries	5.4	22.7	27.4	33.4	25.1	35.1	41.7	18.0	208.9
Latin America	0.7	5.1	3.4	8.5	2.8	5.2	7.2	7.0	40.0
Asia/Pacific	4.3	16.9	23.4	23.8	21.6	26.9	33.5	9.6	160.0
Central & Eastern Europe	0.1	0.2	0.3	0.9	0.6	1.6	1.6	1.0	6.3
TOTAL	85.3	121.9	162.3	196.4	237.3	274.5	341.0	558.0	1 976.6

Source: KPMG Corporate Finance, 1999.

Table 6. Outward cross-border M&As, by region (%)

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98
Developed countries	93.7	81.4	83.1	83.0	89.4	87.2	87.8	96.8	89.4
Western Europe	63.1	45.3	47.5	47.2	45.6	47.3	49.3	61.6	52.0
(EU)	(59.3)	(41.0)	(46.1)	(38.4)	(41.6)	(41.6)	(37.4)	(59.3)	(46.6)
North America	18.4	21.6	27.5	26.5	33.9	31.9	31.2	31.4	29.8
Other countries	12.2	14.4	8.1	9.3	9.9	7.9	7.2	3.7	7.6
Developing countries	6.3	18.6	16.9	17.0	10.6	12.8	12.2	3.2	10.6
Latin America	0.9	4.2	2.1	4.3	1.2	1.9	2.1	1.3	2.0
Asia/Pacific	5.1	13.9	14.4	12.1	9.1	9.8	9.8	1.7	8.1
Central & Eastern Europe	0.1	0.2	0.2	0.5	0.2	0.6	0.5	0.2	0.3
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: KPMG Corporate Finance, 1999.

Table 7. Top five countries for outward cross-border M&As

		1991	1992	1993	1994	1995	1996	1997	1998	1991-98
United States	US$ billion	13.2	22.8	37.8	43.5	65.7	65.5	81.7	132.9	463.0
	Percentage	15.5	18.7	23.3	22.1	27.7	23.9	23.9	23.8	23.4
United Kingdom	US$ billion	8.1	9.2	29.1	33.4	27.0	34.8	32.6	128.9	303.1
	Percentage	9.5	7.5	18.0	17.0	11.4	12.7	9.6	23.1	15.3
Germany	US$ billion	7.5	6.5	6.7	13.2	22.6	27.4	15.7	60.5	160.1
	Percentage	8.8	5.3	4.1	6.7	9.5	10.0	4.6	10.8	8.1
France	US$ billion	15.9	14.2	10.7	11.5	13.3	11.5	21.6	41.2	140.0
	Percentage	18.6	11.7	6.6	5.9	5.6	4.2	6.3	7.4	7.1
Canada	US$ billion	2.5	3.6	6.8	8.6	14.8	22.2	24.7	42.3	125.4
	Percentage	2.9	2.9	4.2	4.4	6.2	8.1	7.2	7.6	6.3

Source: KPMG Corporate Finance, 1999.

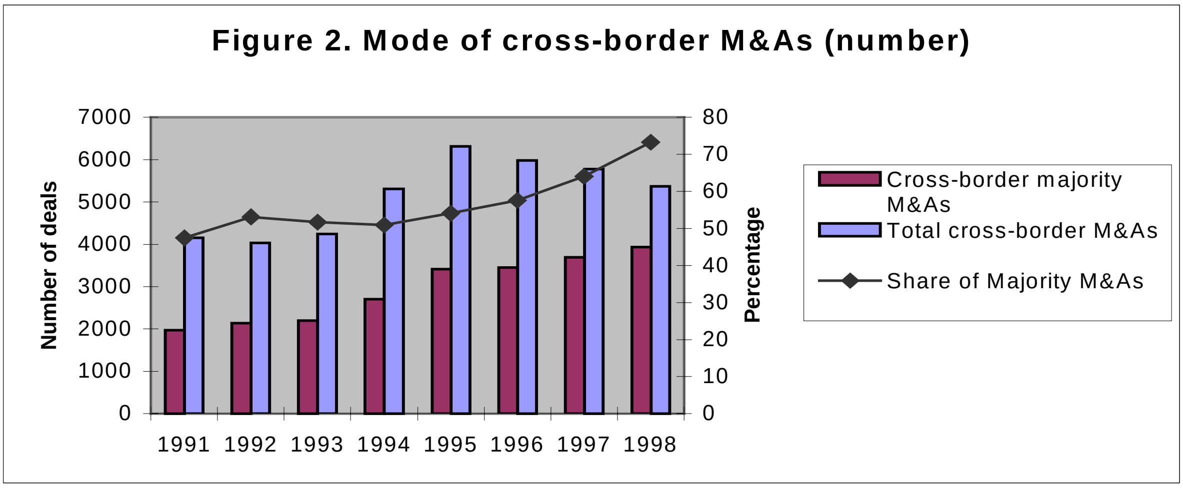
M&As AS AN ENTRY MODE FOR DIRECT INVESTMENT

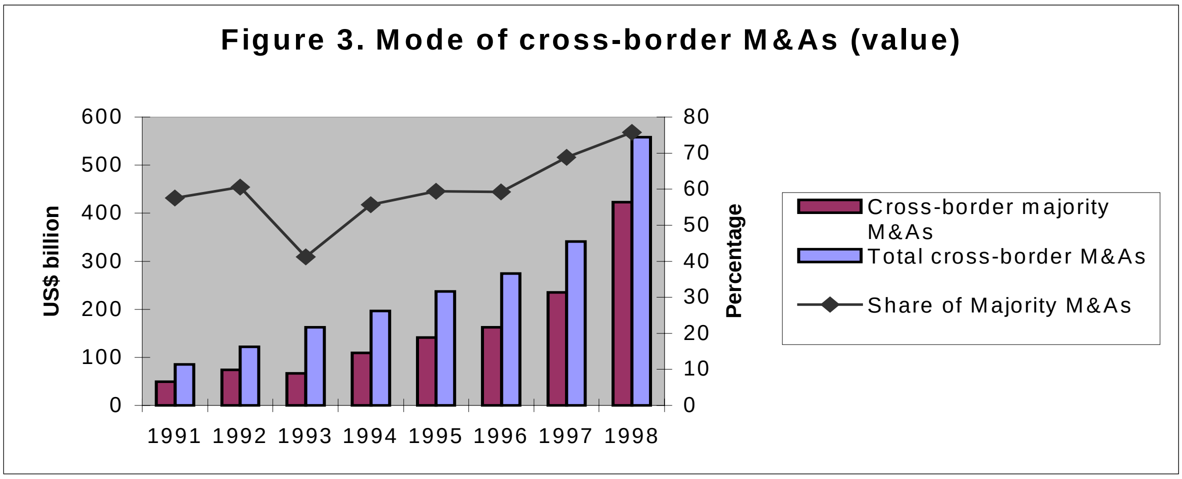
When undertaking direct investment in a foreign country, a firm can choose between different modes of entry. Broadly speaking, the alternative options can be divided into mergers and acquisitions or greenfield investment (Caves, 1982). That is, a firm may either acquire an existing local firm (M&A mode) or establish a new plant (greenfield mode) in the host country. Furthermore, in the case of M&A mode, a firm can either acquire more than 50% of the shares of the acquired firm (majority M&A) or engage in an acquisition of a minority share-holding (minority M&A).

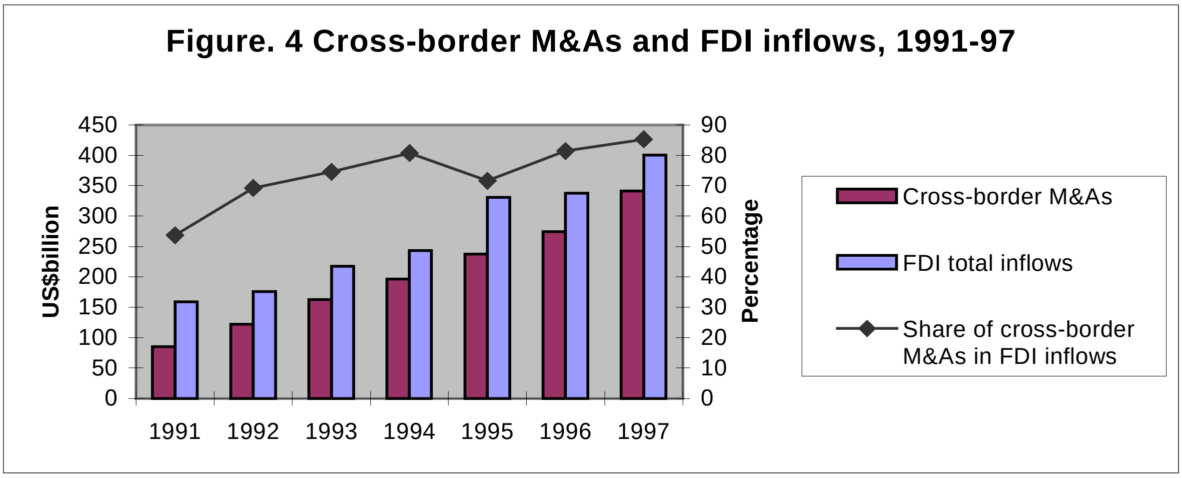
Although entry modes for direct investment depend on a variety of firm and industry characteristics, there has been a marked tendency towards more mergers and acquisitions – in particular, more majority M&As – and less greenfield investments in the 1990s (UNCTAD, 1998). For example, the share of majority M&As in world cross-border M&As continued to increase throughout the 1990s, in terms of both number and value. The share of majority M&As in cross-border M&As in terms of number of deals increased rapidly from 48% in 1991 to 73% in 1998 (**Figure 2**). In terms of deal value, the share of majority M&As in cross-border M&As also increased from 58% in 1991 to 76% in 1998 (**Figure 3**). Furthermore, the value of all cross-border M&As in relation to world foreign direct investment (FDI) inflows rose from 53.7% in 1991 to 85.3% in 1997 (**Figure 4**). This means that cross-border M&As are playing a dominant role in increasing flows of foreign direct investment in the1990s.

Modes of inward FDI

Analysis of the modes of entry for FDI across countries shows quite different patterns between developed and developing countries. Cross-border M&As, in particular majority M&As, play a dominant role in FDI inflows for developed countries, but other modes of FDI inflows such as greenfield investment are more important for developing countries. That is, as an entry mode into markets, cross-border majority M&As are preferred to minority M&As and greenfield investment in developed countries, while in developing countries, greenfield investment and cross-border minority M&As are preferred to cross-border majority M&As.







In developed countries, majority M&As tend to be the prevailing mode for inward cross-border M&As. The share of majority M&As in inward cross-border M&As in developed countries averaged 75% during the period 1991-98 (**Table 8**). For most of the developed countries, the share of majority M&As in inward cross-border M&As was more than 70%: for Western Europe, 72% and for North America, 82%. A prominent exception is Japan, in which the share of majority M&As was just 58% during the same period. On the contrary, minority M&As are dominant in inward cross-border M&As in developing countries. The share of majority M&As in inward cross-border M&As in developing countries was only 32% during the period 1991-98: 55% in Latin America, 17% for Asia, and 29% for Central and Eastern Europe (**Table 8**). However, since 1997, majority M&As have been rapidly increasing in developing countries, in particular in Asia and Latin America. The share of majority M&As in inward cross-border M&As in Asia and Latin America increased to 51% and 76%, respectively, in 1998.

The value of inward cross-border M&As in relation to total FDI inflows is also much different between developed countries and developing countries. In developed countries, the value of cross-border majority M&As in relation to FDI inflows during the period 1991-97 was 62% (**Table 9**). However, in developing countries, the value of cross-border majority M&As in relation to FDI inflows during the same period was only 18% (**Table 10**). When including minority M&As in inward cross-border M&As, the importance of inward cross-border M&As in FDI inflows becomes more prominent, in particular, in developing countries: the value of all inward cross-border M&As in relation to FDI inflows from 1991 to 1997 in developed countries and developing countries increased to 84% and 70%, respectively. Several explanations are possible for the different patterns of entry modes for FDI across countries. For example, in a highly developed country, there should be a relative abundance of target firms for cross-border M&As. However, it is much more difficult to find appropriate firms to acquire in less developed countries. Furthermore, more restrictions on take-overs, particularly on majority take-overs, may exist in developing countries than in developed countries. Hence, greenfield investments are preferred in less developed countries, while M&As are preferred in developed countries (Svensson, 1998).

Table 8. Share of majority M&As in total inward cross-border M&As (%)

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98
Developed countries	65.2	73.6	56.2	74.9	76.6	76.4	82.0	77.3	75.4
Western Europe	63.6	74.9	54.4	67.8	70.4	73.5	81.1	70.9	71.6
France	52.7	76.1	74.5	70.9	80.1	49.7	86.7	74.5	72.6
Germany	53.4	68.9	26.0	60.7	85.9	80.5	86.5	46.1	61.2
Netherlands	54.1	85.6	39.3	52.9	93.7	83.5	96.6	88.2	76.5
United Kingdom	74.5	80.4	59.0	75.4	69.9	80.3	92.3	85.8	81.6
Switzerland	96.0	29.2	95.6	92.6	82.3	76.9	95.1	100.0	90.1
North America	75.1	73.1	57.4	83.0	83.6	86.9	87.2	83.7	82.0
United States	75.0	75.1	57.0	82.6	83.0	86.3	90.5	83.0	82.0
Canada	77.0	67.9	59.7	86.4	87.1	91.1	69.5	92.8	81.8
Other countries	29.9	60.8	64.7	60.4	74.4	50.0	67.5	79.7	65.4
Japan	6.0	39.9	29.0	77.0	43.3	28.8	32.5	76.7	58.2
Australia	34.3	48.4	63.7	55.6	83.4	39.2	78.9	89.3	68.2
New Zealand	45.6	86.1	81.1	46.3	77.1	43.4	93.9	69.4	66.3
Developing countries	18.2	31.8	18.4	18.9	18.4	23.1	41.8	66.7	31.9
Latin America	24.4	59.3	27.9	21.1	53.1	50.2	58.4	75.9	54.6
Asia/Pacific	5.0	8.8	15.3	12.9	7.7	7.1	27.6	51.0	17.1
Central & Eastern Europe	31.2	61.5	11.7	41.7	21.6	38.1	41.2	21.1	28.4
World	57.5	60.5	41.2	55.7	59.3	59.3	69.3	75.8	63.7

Source: KPMG Corporate Finance, 1999.

Table 9. Inward cross-border M&As and FDI inflows in developed countries

	1991	1992	1993	1994	1995	1996	1997	1991-97
Inward majority M&As (US$ billion)	46.5	61.6	55.0	96.7	127.9	142.3	191.0	720.9
Total inward M&As (US$ billion)	71.4	83.7	97.8	129.1	167.0	186.2	232.9	968.2
FDI total inflows (US$ billion)	114.8	120.3	138.9	141.5	211.5	195.4	233.1	1155.4
Share of majority M&As in FDI (%)	40.5	51.2	39.6	68.3	60.5	72.8	81.9	62.4
Share of total M&As in FDI (%)	62.2	69.6	70.4	91.3	79.0	95.3	99.9	83.8

Source: UNCTAD,1998 and KPMG Corporate Finance, 1999.

Table 10. Inward cross-border M&As and FDI inflows in developing countries

	1991	1992	1993	1994	1995	1996	1997	1991-97
Inward majority M&As (US$ billion)	2.5	12.2	11.9	12.7	13.0	20.3	43.8	116.3
Total inward M&As (US$ billion)	13.8	38.2	64.5	67.2	70.3	88.3	108.1	450.4
FDI total inflows (US$ billion)	41.7	51.1	72.5	95.6	105.5	129.8	148.9	645.2
Share of majority M&As in FDI (%)	6.0	23.8	16.3	13.3	12.3	15.7	29.4	18.0
Share of total M&As in FDI (%)	33.2	74.7	88.9	70.4	66.6	68.0	72.6	69.8

Source: UNCTAD, 1998 and KPMG Corporate Finance, 1999.

In general, foreign investment into the United States increasingly reflects a desire by foreign investors to gain access to the advanced and growing technological capabilities of the United States, to integrate operations vertically and to enter new markets (US Department of Commerce, 1999). Foreign investors generally prefer M&As to greenfield investment as an entry mode into US markets in order to take advantage of existing facilities and capacities. In fact, the share of inward cross-border M&As in total FDI inflows during the period 1991-98 was 86%, while the value of greenfield investments in total FDI inflows was only 14% (**Table 11**). Furthermore, the share of inward cross-border M&As in total FDI inflows has tended to increase in recent years: 86% in 1996, 87% in 1997 and 90% in 1998. In terms of number of investments, the dominant role of inward cross-border M&As in FDI remains unchanged. The number of inward cross-border M&As was 4 826 during the period 1991-98, which accounted for 57% of the total number of foreign direct investments (8 526) in the United States during the same period (**Table 12**).

Table 11. Value of FDI inflows into the United States

		1991	1992	1993	1994	1995	1996	1997	1998	1991-98
M&A investments	US$ billion	17.8	10.6	21.8	38.8	47.2	68.7	60.7	180.7	446.3
	Percentage	69.7	69.2	83.0	84.9	82.5	86.0	87.1	89.9	85.7
Greenfield investments	US$ billion	7.7	4.7	4.5	6.9	10.0	11.2	9.0	20.3	74.3
	Percentage	30.3	30.8	17.0	15.1	17.5	14.0	12.9	10.1	14.3
Total FDI inflows	US$ billion	25.5	15.3	26.2	45.6	57.2	79.9	69.7	201.0	520.6
	Percentage	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: US Department of Commerce, 1999.

Table 12. Number of foreign direct investments in the United States

		1991	1992	1993	1994	1995	1996	1997	1998	1991-98
M&A investments	Number	561	463	554	605	644	686	640	673	4826
	Percentage	51.4	49.2	56.5	58.4	57.3	59.4	57.6	61.9	56.6
Greenfield investments	Number	530	478	426	431	480	469	472	414	3700
	Percentage	48.6	50.8	43.5	41.6	42.7	40.6	42.4	38.1	43.4
Total FDI investments	Number	1091	941	980	1036	1124	1155	1112	1087	8526
	Percentage	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: US Department of Commerce, 1999.

Modes of outward FDI

As in inward cross-border M&As, majority M&As tend to be the prevailing mode for outward cross-border M&As in developed countries. The share of majority M&As in outward cross-border M&As in developed countries was 69% during the period 1991-98 (**Table 13**). For most developed countries, the share of majority M&As in outward cross-border M&As was more than 60%: 68% for Western Europe and 69% for North America. One exception is again Japan, in which the share of majority M&As in outward cross-border M&As was only 29% during this period. However, minority M&As are dominant in outward cross-border M&As in developing countries. The share of majority M&As in outward cross-border M&As in developing countries was only 38% during 1991-98: 63% for Latin America, 33% for Asia, 14% for Central and Eastern Europe (**Table 13**). The prevailing mode of minority M&As by developing countries may reflect a motivation based on technological sourcing by capturing spillovers from host countries (Neven and Siotis, 1994; Miotti and Sachwald, 1999).

Unlike the case of inward cross-border M&As, the value of outward cross-border M&As in relation to FDI outflows is quite similar between developed and developing countries. The value of all outward cross-border M&As in relation to FDI outflows during the period 1991-97 in developed countries and developing countries were 70% and 73%, respectively (**Tables 14 and 15**). And the value of cross-border majority M&As in relation to FDI outflows during the same period in developed countries was 44%, while that of developing countries was only 27%. These figures imply that outward cross-border M&As play an important role in FDI outflows for both developed and developing countries. That is, as an entry mode into markets, outward cross-border M&As are preferred to greenfield investment for both developed and developing countries. However, cross-border majority M&As are preferred by companies based in developed countries, while cross-border minority M&As are preferred by developing countries.

Table 13. Share of majority M&As in total outward cross-border M&As (%)

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98
Developed countries	59.3	59.3	44.0	61.5	62.4	63.6	72.6	76.6	66.8
Western Europe	63.2	63.6	47.5	70.6	65.0	62.9	75.7	75.2	68.9
France	70.3	62.4	63.8	53.4	60.7	68.9	57.8	65.3	63.2
Germany	62.4	63.1	48.5	64.6	68.7	44.2	64.8	55.4	57.4
Netherlands	56.3	23.1	39.1	54.2	62.1	80.6	87.9	83.7	71.9
United Kingdom	73.0	66.3	48.9	81.0	73.5	64.4	81.8	86.2	77.0
Switzerland	78.5	94.3	44.2	79.9	80.2	58.3	94.8	81.7	83.9
North America	53.8	60.9	44.3	55.6	64.9	69.5	72.7	80.1	68.7
United States	10.2	63.1	40.5	56.9	60.3	64.4	68.6	75.4	63.5
Canada	54.0	47.2	65.2	48.8	85.5	84.7	86.2	94.9	83.3
Other countries	46.5	43.6	22.3	32.4	42.0	43.9	51.6	70.9	45.5
Japan	41.0	33.4	6.1	10.9	24.2	32.6	35.2	51.9	29.2
Australia	78.8	58.4	39.5	36.3	87.4	78.9	67.5	75.6	68.0
New Zealand	90.8	71.1	40.7	0.0	91.5	21.9	59.5	100.0	54.2
Developing countries	31.8	65.8	27.4	27.4	34.1	29.4	42.0	49.2	37.6
Latin America	17.7	89.2	65.7	29.2	75.6	80.7	59.5	71.4	62.6
Asia/Pacific	31.8	59.1	21.8	27.8	29.4	19.9	42.1	34.5	32.6
Central & Eastern Europe	0.0	100.0	10.4	0.0	0.9	1.9	33.9	2.6	13.6
World	57.5	60.5	41.2	55.7	59.4	59.2	68.9	75.8	63.7

Source: KPMG Corporate Finance, 1999.

Table 14. Outward cross-border M&As and FDI outflows in developed countries

	1991	1992	1993	1994	1995	1996	1997	1991-97
Outward majority M&As (US$ billion)	47.4	58.8	59.3	100.2	132.3	152.2	217.3	767.5
Total outward M&As (US$ billion)	79.9	99.2	134.9	163.0	212.2	239.3	299.3	1227.7
FDI total outflows (US$ billion)	189.8	180.0	205.8	241.5	306.5	283.5	359.2	1766.2
Share of majority M&As in FDI (%)	25.0	32.7	28.8	41.5	43.2	53.7	60.5	43.5
Share of total M&As in FDI (%)	42.1	55.1	65.5	67.5	69.2	84.4	83.3	69.5

Source: UNCTAD, 1998 and KPMG Corporate Finance, 1999.

Table 15. Outward cross-border M&As and FDI outflows in developing countries

	1991	1992	1993	1994	1995	1996	1997	1991-97
Outward majority M&As (US$ billion)	1.7	14.9	7.5	9.1	8.5	10.3	17.5	69.6
Total outward M&As (US$ billion)	5.4	22.7	27.4	33.4	25.1	35.1	41.7	190.9
FDI total outflows (US$ billion)	8.3	20.7	34.9	42.5	45.6	49.2	61.1	262.4
Share of majority M&As in FDI (%)	20.6	72.1	21.5	21.5	18.6	21.0	28.6	26.5
Share of total M&As in FDI (%)	64.6	109.7	78.6	78.5	55.0	71.5	68.3	72.7

Source: UNCTAD, 1998 and KPMG Corporate Finance, 1999.

CROSS-BORDER M&As BY SECTOR

Sectoral trends

Cross-border M&As are actively taking place across a large number of sectors, manufacturing as well as services. Petroleum, automobiles, pharmaceuticals, banks and telecommunications are examples of industries experiencing some very large cross-border M&As (**Table 16**). More and more cross-border M&As are taking place in service industries, which now account for 60-70% of GDP and employment in OECD countries. The share of manufacturing industry in all cross-border M&As decreased from 55% in 1991 to 35% in 1998, giving way to an increase of activity by service industries, such as finance, telecommunications, business services and electricity, from 41% in 1991 to 52% (**Table 17**). Service industries accounted for more than half of all cross-border M&As during the period 1991-98, while manufacturing industry accounted for 40%. When only cross-border majority M&As are taken into account, an even more rapid increase in the share of service industries can be observed: from 36% in 1991 to 54% in 1998 (**Table 18**). This implies that majority M&As are playing a more important role, particularly in cross-border restructuring in service sectors (**Table 19**).

Table 16. Top ten industries for cross-border M&As in 1998

Industry	Sector	Deal value (US$ billion)	Number of deals
Extraction of mineral oil and natural gas	Primary	76.2	100
Manufacture of motor vehicles and parts thereof	Manufacturing	50.9	147
Banking and finance	Services	50.9	326
Postal services and telecommunications	Services	50.4	235
Manufacture of paper and paper products; printing and publishing	Manufacturing	41.0	235
Production and distribution of electricity, gas and other forms of energy	Services	40.3	118
Business services	Services	38.2	888
Insurance, except for compulsory social security	Services	37.9	129
Chemical and pharmaceuticals industry	Manufacturing	26.2	364
Retail distribution	Services	18.0	155

Source: KPMG Corporate Finance, 1999.

Table 17. Sectoral distribution of cross-border M&As (%)

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98
Primary	3.5	2.7	15.0	4.9	9.4	8.5	7.0	13.9	9.5
Manufacturing	55.1	52.5	39.3	55.6	44.5	35.0	34.5	34.6	40.3
Services	41.4	44.7	45.8	39.5	46.1	56.5	58.6	51.5	50.2
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: KPMG Corporate Finance, 1999.

Table 18. Sectoral distribution of majority cross-border M&As (%)

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98
Primary	3.3	1.1	2.3	3.4	2.5	4.0	5.8	16.5	8.0
Manufacturing	60.8	59.3	55.0	61.0	48.6	36.6	37.2	29.4	41.0
Services	35.9	39.6	42.7	35.6	48.9	59.4	57.1	54.1	51.0
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: KPMG Corporate Finance, 1999.

Table 19. Sectoral share of majority M&As in total cross-border M&As (%)

	1991	1992	1993	1994	1995	1996	1997	1998	1991-98
Primary	54.4	24.7	6.5	39.2	15.6	28.1	57.5	90.3	54.3
Manufacturing	63.4	68.4	57.6	61.1	64.8	61.9	74.6	64.3	64.9
Services	50.0	53.6	38.4	50.2	63.0	62.3	67.5	79.6	64.8
Total	57.5	60.5	41.2	55.7	59.4	59.2	68.9	75.8	63.7

Source: KPMG Corporate Finance, 1999.

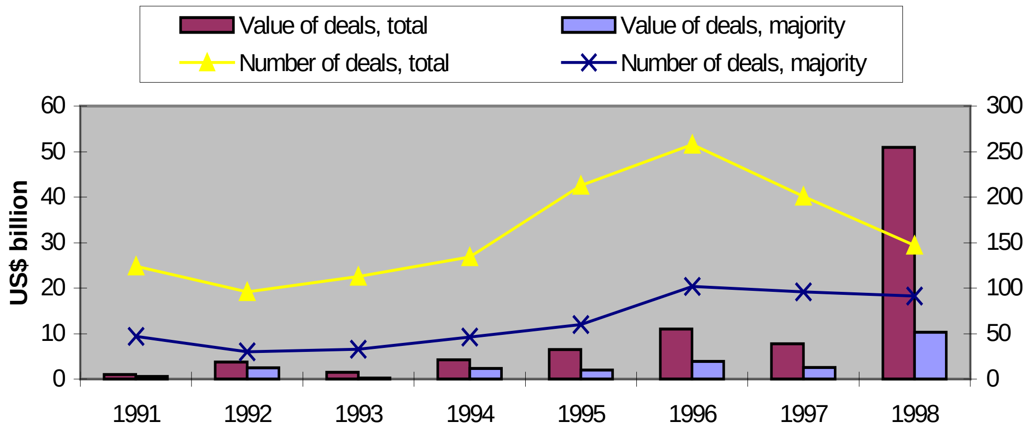
The sectoral analysis below focuses on five different industries where recent merger and acquisition activity has been particularly marked: the automotive, steel, telecommunications, petroleum, and pharmaceutical industries. These sectors are interesting from several perspectives. First, they provide examples of important recent mergers, which also evidence a trend towards consolidation within industries rather than across sectors. In the case of the automotive and steel industries, this may be a ripple effect as a supplier industry consolidates in response to increasing globalisation and concentration among its clients. The selected sectors have also been of strong national interest to policymakers in many countries and have in the past been prime targets for political intervention in the form of ownership and regulation. Recent market developments in these sectors are influenced by important reforms in the regulatory area in the 1990s, albeit to a varying degree. Other sectors such as finance and business services which are also experiencing increased M&A activity are not examined here since some recent developments in the financial sector are covered by OECD/DAFFE (*e.g.* OECD, 1999c) and other sectors lack appropriate data for analysis.

Automobiles

Recent mergers and acquisitions in the automotive industry are largely driven by a combination of excess capacity, the increasing costs of innovation and technical development, and regulatory changes. 1998 turned out to be a record year for M&As within the automotive industry. In fact, more than 600 deals were undertaken, with disclosed values exceeding US$80 billion (PriceWaterhouseCoopers, 1999*a*). Of the total value, more than two-thirds arose from cross-border M&As, dominated by the "mammoth merger" between Chrysler and Daimler-Benz which alone accounted for US$39 billion.

The rapid restructuring of the automotive industry has attracted a great deal of attention. The merger between the US company Chrysler and Daimler-Benz of Germany together with other large-scale deals – Volkswagen's take-over of Rolls Royce, Ford's take-over of Volvo's car division, and the alliance between Renault and Nissan – is evidence of an industry consolidating at an accelerating speed. The merger wave is also affecting all parts of the automotive industry: vehicle companies, component suppliers and retail sectors, and is to a large extent taking place across national borders. **Figure 5** shows the increase in deals in the motor vehicle and parts manufacturing industry.

Figure 5. Motor vehicles & parts manufacturing: Cross-border M&As 1991-98



Source: KPMG Corporate Finance, 1999.

Consolidation and internationalisation are far from new to the automotive industry, and especially to vehicle producer companies. The vehicle market is already highly concentrated, with some ten leading companies accounting for more than 50% of the total market. However, the current restructuring trend is taking place in a somewhat new context: markets have been liberalised and new and different countries have entered both on the consumer and producer sides. Spatial reorganisation is needed to achieve cost savings and reach new markets.

In addition, there are several factors increasing competitive pressures in the automotive industry. One is excess capacity – estimated at some 20 million vehicles per year (PriceWaterhouseCoopers, 1999*a*). This problem was aggravated as the financial crisis in Asia removed what was considered to be an important growth market. The emergence of the Internet as a new interface with customers, and the introduction of a common currency in Europe, are both leading to increasing transparency in main markets, as customers' transaction and information costs to a large extent are removed. Regulatory changes in the present or in the near future, such as the removal of selective distribution arrangements, are also playing an important role. To this must be added the longer-term challenges of competing technical innovations and societal preferences. For example, developing the next generation of cars, especially environmentally clean cars, is likely to add substantially to the costs and risks companies have to bear. As a result, companies are seeking partners to amass sufficient financial resources and spread risks.

Steel

Cross-border M&As in the steel sector appear to be driven by both unfavourable market conditions and the fact that national governments have reduced their stake in and control over the companies. Since the 1970s, the steel industry has experienced significant changes regarding growth rates, organisation, technology, regulation and employment. For example, global steel production has risen by approximately 30% in the past 25 years. Employment, however, has been almost halved in the same period in the major steel producing countries, excluding China. Steel jobs have declined most radically in EU member countries, where estimated employment today is around one-third of that in 1975.

These changes reflect a variety of factors influencing competitiveness in the steel market. One is changes in steel-making processes and technologies. For example, technological advancement now enables much smaller units (so called mini-mills) to operate economically. A second relates to new entrants. While developed countries still account for the bulk of steel production, new countries, notably China, Korea, and India, have entered the market and are now among the ten largest producers worldwide. A third factor is changes in political intervention: the steel industry has seen a sharp reduction of state ownership and subsidies. The transfer from the public sphere of influence to private ownership is a relatively recent phenomenon. In the 15 EU member countries, state ownership has been reduced from 50% to 5% (in terms of crude steel output) during the 1990s. Subsidies have consequently fallen dramatically but remain an issue in several countries.

Long-run trends notwithstanding, the steel industry has seen some drastic developments in the last two years. In particular, the financial crisis which hit Asia in 1997 and Russia and Latin America in 1998 led to a deterioration in market conditions as steel demand contracted and imports were reduced. The collapse in domestic demand meant that Asian countries could no longer absorb exports from the NIS and the European Union. Russian exports were re-directed to destinations in North America and the EU. Prices for key steel products plunged in 1998. The massive shift in market conditions and in regional focus dealt a major blow to the steel trading system.

Market conditions are therefore putting pressure on steel companies to offer a wider range of products, exploit synergies and reduce costs. These competitive pressures are reflected in a wave of mergers and acquisitions. In Europe, the consolidation trend, including several cross-border deals, is particularly remarkable. The recent merger between British Steel and Dutch Hoogovens (**Box 2**) follows a wave of mergers on the European continent. In the past two years, two German firms have merged (Thyssen and Krupp); Usinor, a French company, has taken over Belgium’s Cockerill Sambre; British-Indian ISPAT has bought parts in Thyssen; and Arbed from Luxembourg has bought parts of Spanish Aceralia. With the BS-Hoogovens merger, Europe will have four globally very important steel groups.

The current consolidation in the European steel industry results from several factors. First, unfavourable market conditions are forcing companies to enhance cost effectiveness. Second, privatisation and a move away from state involvement are opening up more avenues for foreign investment. Third, the introduction of the euro is expected to put additional downward pressure on steel prices in the EU by introducing more transparency in pricing as well as integrated financial markets.

Box 2. British Steel and Hoogovens

In June 1999, British Steel announced an all-paper bid for Hoogovens. The deal between the British giant and the Dutch company followed a series of mergers in the European steel market: Thyssen and Krupp (Germany), Usinor (France) and Cockerill Sambre (Belgium), and Arbed (Luxemburg) and Aceralia (Spain). The new merger makes British Steel-Hoogovens the largest steelmaker in Europe.

The British Steel-Hoogovens merger is not merely a reaction to a recession in markets and overcapacity in the steel market: both companies had already undertaken cost cuts and considerably restructured their businesses during the 1990s. For example, British Steel had shed 7 000 jobs in the previous two years. Instead, the following have been cited as the main reasons for the merger:

- *A highly internationalised customer group driving the need for a global presence. In particular, globalisation in the automotive industry is seen as a major impetus to increase regional coverage and the ability to service clients wherever needed.*

- *The increasing need for R&D and technological innovation to deliver steel products adapted to customer need – lighter, more environmentally friendly, better design, etc.*

The merger is expected to lead to an integration of technical expertise and an enlarged range of products, increased cost efficiency through exploitation of synergies, wider geographic spread and with it a better distribution and service centre network as well as diversification of currency risk. In particular, British Steel, whose exports have been harmed by the strength of the British pound in recent years, is likely to benefit from a portfolio partly based on sales in euros.

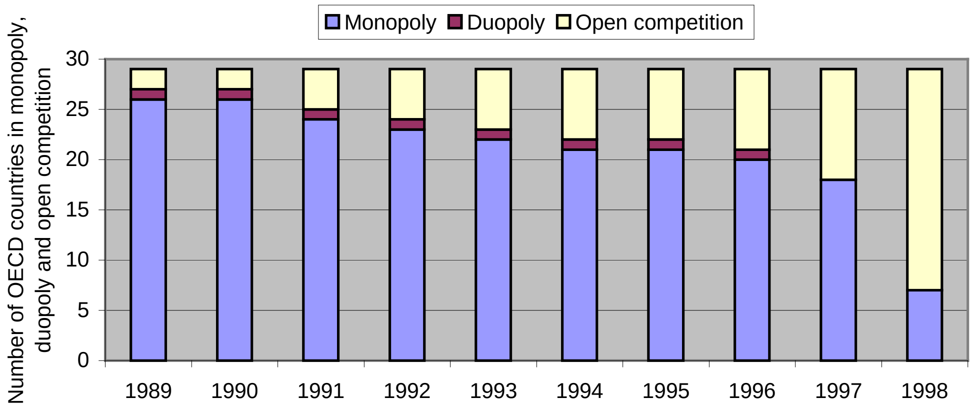
However, the ongoing concentration in steel production might also be a consequence of the structure of production and ownership in customer markets. The main steel clients are the construction, automotive and domestic appliance industries. The two latter are characterised by a global presence and a high degree of concentration. As mentioned, the top ten producers in the automotive industry now represent over 50% of global production, whereas in the steel sector the equivalent is around one-third. As a consequence of globalisation in industries on the demand side, steel producers are being moved to organise global delivery of services. Because of concentration in those industries, moreover, there is from the perspective of steel producers an imbalance in bargaining power, which in turn is affecting prices and terms of delivery.

Telecommunications

The telecommunications sector is the best example of how rapid technological developments in combination with regulatory reform both enable and force companies to seek new partners across national and technical borders. The telecommunications market is becoming increasingly complex in terms of products and services as well as actors. Technological advances and regulatory reform are changing the traditional borders of who is doing what and where. Incumbents in the telecommunications market are having to deal with or adapt to new technologies (*e.g.* ATM switches) and new communication patterns and means (*e.g.* Internet replacing conventional telephony). In addition, competition, stimulated by regulatory reform, has meant that the incumbent former monopolies need to respond to customer needs and shareholder demands. The telecommunications sector is also becoming "denationalised" since many countries have opened up partly or wholly to foreign ownership.

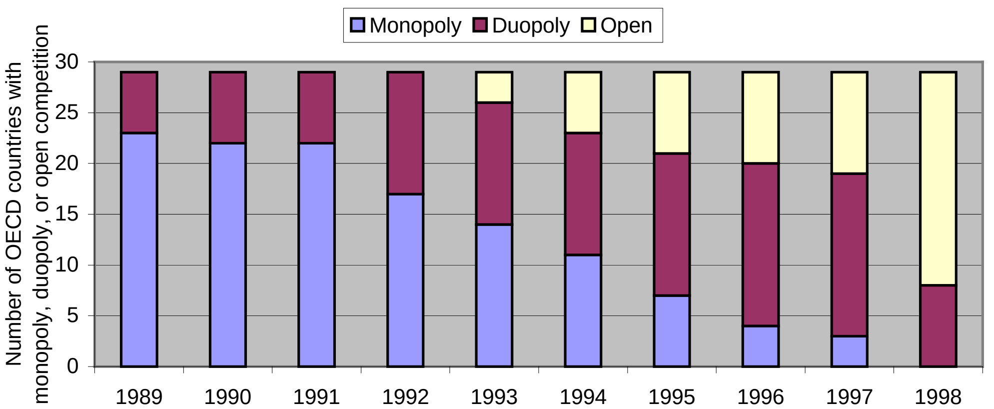
The telecommunications market structure has changed dramatically in the last decade. Several OECD Member countries have opened up or are in the process of opening up their fixed network infrastructure markets to competition as well as issuing licences to new entrants in the cellular mobile communication market. **Figures 6 and 7** illustrate the liberalisation trend during the 1990s in these two segments in OECD countries. Whereas in 1989, a majority of OECD countries had state-owned monopolies, by 1998, a majority had open competition in both the fixed network and cellular mobile markets.

Figure 6. Fixed network infrastructure: Competition structure in OECD



Source: OECD, 1999d.

Figure 7. Cellular mobile communication infrastructure: Competition structure in OECD



Source: OECD, 1999d.

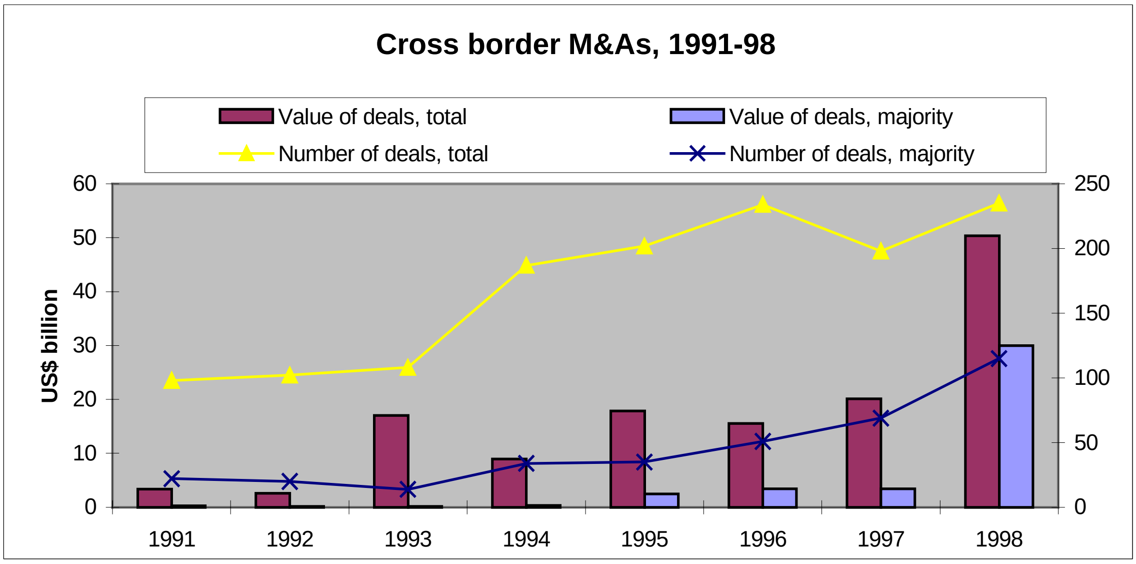
Changing telecommunications structures result from rapid technological changes but even more so from regulatory reform. The main reasons for the regulatory changes were to improve economic performance, stimulate the diffusion of new services and innovations, and because a number of new technologies made it less and less sustainable to maintain existing monopoly coverage of services intact. The abolishment of public telecommunications operator monopolies has, among other things, been crucial for the spread of Internet use. At the same time, traditional telecommunications companies have been able to tap into a new growth area by providing Internet services.

The challenge for new entrants with technologically advanced high capacity networks is to reach and win over customers in a market where brand-name and position tend to be very important. Incumbents, often former monopolies, in contrast, may need to absorb new technology. The need for operators to supply a widening range of services has led to more joint ventures and alliances as well as mergers and acquisitions by companies wishing to gain in size and influence. However, in view of the rapidly changing environment, the number of mergers and acquisitions across borders has remained relatively low, although there are many cross-border agreements and various forms of alliances in place. These alliances are in large part a consequence of the globalisation of service industries (*e.g.* banking and finance) and a need to provide multinationals with an end-to-end service.

A large share of telecommunications mergers have taken place in the United States, where partnerships are created among regional and long-distance carriers to achieve economies of scale. The deregulation of the US telecommunications industry in 1996 was intended to increase competition but has in fact resulted in a rush towards consolidation which is transforming the communications industry. MCI was taken over by Worldcom (long distance) in 1998, Nynex merged with Bell Atlantic (regional), Bell Atlantic and GTE are proposing to merge, as are SBC Communications and Ameritech (regional). AT&T has taken over TCI and MediaOne group (two important US cable companies). It is important to note that while mergers and take-overs are taking place within the telecommunications industry, it is an industry which is undergoing constant change in terms of products, services and participants, largely due to technological developments.

Cross-border mergers in telecommunications and related information technology industries are also growing due both to deregulation and the drive to obtain technology. While the value of total cross-border M&As doubled between the periods 1991-94 and 1995-98, the total value of concluded majority cross-border mergers and acquisitions within the post and telecommunications sector in the period 1995-98 was almost ten times that of the period of 1991-94, largely due to the intense activity in 1998 (**Figure 8**). In 1999, AirTouch Communications Inc. (US) was taken over by Vodafone Group PLC (United Kingdom) – the value of the deal amounted to almost US$70 billion. This was the largest recent cross-border merger in this sector, but only one of many trans-Atlantic M&As. During the first half of 1999, there were an estimated 93 other acquisitions of US information technology concerns by European buyers, with a total value of US$72 billion, nearly triple the level of the year before. Many large European telecommunications firms desire US technology – particularly that related to the Internet – in order to be competitive worldwide. France’s Alcatel has made five acquisitions in the United States, mostly in broadband technologies that allow high-speed data transmission over networks. General Electric Co. of the United Kingdom has made three acquisitions, including the purchase of Fore Systems (United States), another advanced broadband firm. Phillips Electronic NV (Netherlands) and Ericsson (Sweden) have also been active. In Scandinavia, Telia of Sweden and Telenor of Norway have decided to join forces. In 1999, Deutsche Telekom made a bid for a merger with Telecom Italia but lost it to the Italian company Olivetti. These deals and bids are believed to be just a flavour of large-scale M&A activity in the telecommunications sector yet to come.

Figure 8. Post and telecommunications



Source: KPMG Corporate Finance, 1999.

Oil and gas

Market trends and a need for restructuring are driving the increasing number of large-scale deals between companies in the oil and gas industry. Being of fundamental strategic importance to producer countries, the oil industry has gone through various stages of ownership and organisational structures. The 1970s saw the age of nationalism, where natural resources were nationalised, foreign concessions taken over and consortia halted, and the OPEC cartel regulated supply. In the 1980s followed an age of hostile take-overs and rescuing “white knights” – in fact, the still-standing record for deals in the oil industry dates back to 1984 when Texaco took over Getty Oil, Gulf was overtaken by Chevron, and Mobil acquired Superior Oil. A privatisation trend throughout the 1990s has brought private capital and foreign investors back into the arena and led to several mega-mergers (although it should be noted that the public sector often still plays a large role in the oil sector). Today, as oil prices remain low, managers are hard pressed to improve financial performance.

The oil industry accounted for the largest mergers of all in 1998. The deal between British Petroleum and Amoco of the United States amounted to US$55 billion (**Box 3**). Recent years have seen the formation of several joint ventures as well as the mega-mergers by BP-Amoco, Total-Fina, and Nisseki-Mitsubishi. These deals were taking place as oil prices reached their lowest level in ten years in 1998. Other than (but related to) cost pressures, the oil and gas industry has seen some new features with strong implications for industry structure and the way of doing business. Among the most important factors are technological advancements which have increased competitive pressures in several ways. On the one hand, improved extraction techniques keep up supply, which in turn puts pressure on prices. On the other hand, technology has made gas cheaper as a substitute for oil, and gas better meets environmental concerns.

Regulatory reform has also had a major impact: during the 1990s, several petroleum-rich countries privatised and deregulated their oil and gas industry (*e.g.*, Argentina, Malaysia, Venezuela), and some have opened up to foreign companies to participate in the extraction of national resources. In addition, the Asian crisis has prompted restructuring in the oil sector. The Asian region was, before 1997, the most rapidly growing source of demand for oil; however, demand has fallen considerably in the wake of the economic difficulties experienced by the region. Moreover, the OPEC cartel has not been able to repeat the supply cuts of the 1970s, and today there are more non-OPEC-based low-cost producers willing to increase production in the event of higher prices.

Box 3. British Petroleum and Amoco

In 1998, British Petroleum of the United Kingdom and Amoco of the United States merged their oil-related businesses. The deal put two companies, who as separate entities were considered to be in the top of the second division in terms of size, among the super oil and gas companies Exxon and Royal Dutch/Shell. The new company will be the world's largest petroleum producer – but still with only 2% of the market.

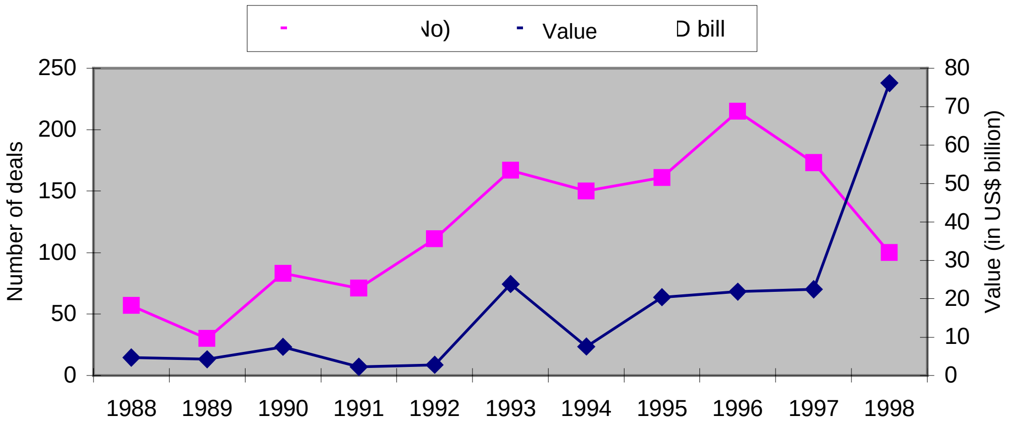
The merger is expected to deliver both cost efficiencies amounting to US$2 billion in the coming two years and increased market opportunities. BP has already cut its workforce by half since the beginning of the 1990s, and additional cuts are planned to reduce overlaps and benefit from synergies. For BP, the deal marks a need to increase its presence in geographical and product markets with better growth potential. With Amoco, BP captures an important part of the US petroleum market and also strengthens its position in gas extraction in North and South America. There is also improved vertical integration. The strength of BP lies in upstream activities – finding and extracting oil – whereas Amoco is considered to be better at the downstream part of the oil business, *i.e*. refining, distribution and marketing. BP-Amoco are expecting to increase competitiveness through the exchange of complementary intangible assets across the organisation.

The new company is now expected to acquire Arco, an US oil and gas company, in an acquisition which would amount to US$26 billion. This acquisition, in turn, would lead to a further penetration of the gas business in the United States. Total savings are expected to amount to US$1 billion.

The current market situation is thus requiring the oil industry to reinvent and restructure itself. Indeed, whereas global M&A activities have gained momentum throughout the 1990s, the surge in oil sector M&As took place in the last few years during which oil prices have plunged (**Figure 9**). It is still a comparatively fragmented market. Today, however, oil companies are forced to look for partners to exploit synergies, access new sources and reduce overheads. Oil companies are also buying into other fuels, especially gas. The deals are sometimes defensive in nature in that, as a result of hard times, there is a need to achieve maximum cost efficiency and create lean companies. At the same time, companies, and especially second-tier companies, have a choice to make: either to find a suitable partner for merger and join ranks with the handful of mega-companies or to focus on a special geographical or technical niche (and risk being taken over). In short, oil companies are now being forced to choose in which league they want to compete.

There may also be a case for size in the oil industry, *i.e.* that there are economies of scale in the production and distribution of oil. Cross-border mergers between companies with different regional outreach will result in the spreading of political and financial risk. More capital will increase the ability to bid for large deals without having to look for partnerships for each occasion. Increased size increases the ability to take risks in exploration and production. In addition, mergers may give access to newer and cheaper oil fields generally outside Europe and North America.

Figure 9. Extraction of mineral oil and natural gas: Cross-border M&As 1988-98



Source: KPMG Corporate Finance, 1999.

Pharmaceuticals

The continued drive towards internationalisation and consolidation among pharmaceutical companies is more than anything a result of a pressing need to achieve cost savings and speed up innovation. Larger pharmaceutical companies, in particular, have been seeking partners in order to amass the resources needed for financing research and development for new drugs and products. In fact, between 1994 and 1997, all of the top fifteen pharmaceutical companies were involved in merger and acquisition transactions (PriceWaterhouseCoopers, 1999*b*).

In the 1970s and 1980s, the pharmaceutical industry recorded double-digit growth. However, pharmaceutical companies have not been able to replicate these figures in the 1990s. There are long lead times, high risks and high costs involved in developing new product lines – in fact, the financing of R&D amounts to an average 20% of total sales. The slow-down poses several challenges, especially as several of the best-selling drugs will lose patent protection in the next few years. There is little doubt that the increase in mergers and acquisitions within the pharmaceutical industry, including cross-border unions, is inversely related to current growth prospects. With new entrants in the market, increasing financial needs for research as well as for marketing and distribution, pharmaceutical companies are under pressure to improve their bottom line. In addition, horizontal mergers between companies of equal size have provided a means of avoiding an unwelcome take-over by competitors, who in turn are looking for suitable targets.

THE DRIVING FORCES BEHIND CROSS-BORDER M&As

Firms engage in cross-border M&A activity for several reasons: among them, to strengthen their market position, expand their businesses, seek useful resources such as complementary intangible assets or realise efficiency gains by restructuring their businesses on a global basis (UNCTAD, 1998). The growth in cross-border M&As is part of an overall surge in M&As at both national and international levels due to their inherent advantages over other forms of investment. Through M&As, investors can exploit synergetic effects between their own assets and those of already-established firms. M&As enable firms to quickly realise new market opportunities and establish an immediate critical mass in a particular market. They can also serve to eliminate actual or potential competitors which, at the international level, are becoming more important as barriers to trade and investment fall. Virtually all developed countries and many developing countries have competition laws which prohibit anti-competitive mergers; horizontal mergers, particularly those occurring in highly concentrated markets, are generally subject to fairly close scrutiny by competition authorities to verify efficiency effects, although this may not always be 100% effective (OECD, 1996*a*).

Mergers and acquisitions are not a new phenomenon, although their motives and characteristics may change over time. They have tended to occur in waves throughout this century, with periodic increases in M&A activity when stock market prices were high (Mueller, 1989). Economic recessions or booms can affect the level of global M&A activity and its regional focus. Industry characteristics such as growth prospects, market structure and competition are a strong influence on cross-border mergers. Slow growth, over-capacity and increased competition in global markets typically drive industrial restructuring and often make M&As preferable to greenfield investments. Increased competitive pressures can push companies to seek equal partners where costly overlaps can be reduced and synergies exploited.

Technological change works both as a pull and push factor for cross-border M&As: by promoting international expansion through falling communication and transport costs; by creating new businesses and markets; by rapidly changing market conditions; or by increasing the costs of research and development. Technical competence and market know-how, flexibility and ability to innovate increasingly are becoming corporate strategic assets, while at the same time the speed of technological development is pressing on. Companies are being forced to look for partners from whom intangible assets such as these can be obtained and absorbed. In addition, government policies such as liberalisation, privatisation and regulatory reform influence cross-border unions by opening up opportunities and increasing the availability of favourable M&A targets. These driving forces behind cross-border M&As can be loosely grouped into factors at the macroeconomic, industry and firm-level, as well as technological and government-related factors.

Macro-level factors

Economic growth influences both the supply of and demand for cross-border M&As. Economic expansion in home countries increases earnings and equity prices and hence the pool of capital available for investment abroad. Similarly, an economic boom in host countries increases the short-term profitability of potential target firms for acquisition. The prolonged economic expansion in major countries such as the United States and the United Kingdom has played an important role in the continued and rapid increase of both inward and outward cross-border M&As in the 1990s. In fact, the United States and the United Kingdom became the largest merger investors and recipients in the 1990s as their economies strengthened.

Conversely, slower economic growth tends to work against cross-border mergers. As the Japanese economy continued to experience recession, outward FDI from Japan, including outward M&A purchases, rapidly slowed in the 1990s. Outward acquisitions by Asian countries, which experienced a serious economic recession due to the currency crisis of 1997-98, also sharply decreased in 1998. At present, inward M&As are increasing in Japan and many Asian countries, particularly Korea, due to falling asset prices as well as changes in business practices and an environment more favourable to foreign acquisitions. The level and direction of international M&A activity is influenced by a host of factors including drivers at the level of the industry and firm.

Industry-level factors

Although cross-border M&As are taking place actively across almost all industries, recent large-scale unions have tended to be concentrated in a few major sectors, such as petroleum, automobiles, finance and telecommunications. These are the sectors which are experiencing intensified global competition and market pressures from falling commodity prices (petroleum), excess capacity in key markets (automobiles), and/or deregulation and rapid technological change (banks and telecommunications).

Unlike the M&A deals of the 1980s, which were often about capturing new markets or supposedly undervalued and unrelated businesses, many of the international mega-mergers of the 1990s take place within the same industry for the purpose of restructuring. This kind of union typically involves consolidation and scrapping of capacities on a global scale to improve international efficiency and competitiveness. Intensified global competition and market pressures are forcing firms to concentrate on their core business activities. The trend towards cross-border mergers and acquisitions partly results from growing sales of non-core operations or affiliates and the acquisition of similar operations (divisions, affiliates or firms that have similar businesses) beyond national borders (UNCTAD, 1998).

Firm-level factors

According to theories of trade and industry location, a firm needs to have a firm-specific competitive advantage (ownership advantage) in foreign markets in order to successfully undertake foreign direct investment (Dunning, 1977). This competitive advantage generally arises from the existence of firm-specific intangible assets such as production knowledge and skills, marketing capabilities and brand names or superior management capabilities. These intangible assets are quasi-public goods with large economies of scale and scope, and hence can be applied repeatedly and simultaneously to multiple locations and businesses in a non-rivalry manner. Thus, as a firm accumulates more and more intangible assets, the firm has stronger incentives to exploit them through geographical diversification (FDI) or other modes of internalisation (Morck and Yeung, 1999).

Empirical research identifies several firm-level factors that influence the choice of entry modes in making foreign direct investments. First, it has been observed that M&As are more desirable the greater the organisational and managerial skill of a firm, while greenfield operations are more preferable the greater the technological skill of the firm (Andersson and Svensson, 1994). Here, organisational and managerial skill is associated with the ability to absorb and utilise existing knowledge, while technological skill is related to technology development and the ability to innovate with respect to investment in research and development. Since the international experience of a firm is generally related to organisational and managerial skills, firms with more international experience tend to favour take-overs. A firm’s previous presence in a host country also increases the attractiveness of take-overs. That is, if a firm already has established affiliates in the host country, this increases the benefits of take-overs relative to greenfield operations, since a new investment in plant and equipment may increase capacity and competition in the host country market which may lead to lower prices and profits, hurting the firm's existing affiliates. This result implies that as multinational operations increase, the trend toward increased use of take-overs may be strengthened.

Firm strategies *vis à vis* competitors may further affect the modes of entry. If a firm does not possess sufficient intangible assets to be competitive, it may seek them in the asset bundle of an existing local firm through acquisition. On the other hand, if a firm has technological and competitive advantages that it firmly wishes to retain control over, it may prefer greenfield investment to M&A (Yamawaki, 1994; Andersson, 1993). For instance, it has been observed that Japanese MNEs when entering Europe have continued to rely on greenfield investments in industries where they have superior competitiveness, whereas their reliance on M&A in an industry tends to be stronger the higher the relative competitiveness of the European industry. Furthermore, the former investments have tended to be undertaken in European countries with relatively low competitiveness in these sectors, whereas the latter have been undertaken in the countries which are more competitive, *e.g.*, greenfield investment in semiconductors and transport targeting particularly the United Kingdom compared to M&A in chemicals focusing on Germany and the Netherlands.

A recent study concentrating on cross-border M&As between the United States and four European countries (Vasconcellos and Kish, 1998) outlines the factors which might motivate cross-border M&As at the firm level. One impetus is risk spreading: in order to reduce risk, firms acquire companies in other economies on the basis that the covariance of industry returns across economies is likely to be smaller than within one economy. *De facto* differences in cyclical conditions at a specific point in time can also favour acquisitions – for example, a relatively strong stock market increases the means available to companies for purchases and renders foreign targets cheaper. However, this may only be true when the economies in question are not highly integrated. Companies which are unable to develop technology in-house due to time or resource constraints can also choose M&A as a means for acquiring technological and human resources. Among the factors which might deter acquisitions are information asymmetries – lack of reliable information about prospective acquisitions may dissuade potential buyers. Such information gaps can be more serious across borders. Where potential targets have monopolistic power, take-over attempts are also likely to be resisted.

Technology-related factors

Technological change has had different types of effects in stimulating cross-border M&As. On the one hand, falling communication and transport costs have favoured international expansion of firms seeking to exploit and consolidate their competitive advantages. In particular, recent developments in information technology tend to expand the range and span of corporate control, making the optimum size of firms larger than previously possible. Multinational enterprises can expand their size and achieve more dominant market positions through acquisitions beyond national borders, while maintaining efficiency and flexibility in their management through new information and communications technologies. On the other hand, the soaring costs of R&D, coupled with the uncertainties of technological change, have forced firms to co-operate with others in global markets through various unions and strategic alliances in order to fund research expenditures for new products. For example, the large R&D costs required to develop new generations of drugs is considered the major driving force for recent M&As in the pharmaceuticals sector.

Technological change tends to shorten product life cycles and promote new entrants with innovative technology, which alters competitive conditions and market structure as seen in the case of telecommunications and steel. Technological change also creates new businesses and markets, such as in telecommunications and information-related industries. Mergers and acquisitions can be a quick and easy way to react to competitors and acquire entry into new sectors and markets. The recent surge of cross-border alliances in the telecommunications, media and information industries reflects the efforts of firms to capture new markets created by new technologies, particularly the growth of the Internet, and to provide more integrated global services. Furthermore, investors in many sectors tend to prefer foreign acquisitions rather than greenfield investments because local firms may provide intangible assets such as a distribution network, an established brand name or market share, and/or in-depth knowledge of local customs and regulations.

Government-related factors

Liberalisation of international capital movements and investments coupled with new investment incentives have promoted the rapid increase and spread of foreign direct investment, particularly cross-border M&As. For example, in the case of Korea, all remaining restrictions on acquisitions by foreign investors were repealed in 1998 as one of the structural reforms in the wake of the economic crisis. As a result, the share of M&A investments in total FDI inflows into Korea increased to 53% in 1998. Regulatory reform and deregulation in such industries as telecommunications (the WTO agreement on basic telecommunications services came into effect in 1998), electricity and finance are playing an important role in the dramatic increases in M&As in both developed and developing countries. These industries are beginning to open up to foreign investors in many countries and full or majority ownership by foreigners is gradually being allowed. Privatisation is also contributing to cross-border merger activity by increasing M&A targets and opening up economies to increased competition. Significant increases in inward M&As in Latin America and in Central and Eastern Europe are linked to privatisation of state enterprises in telecommunications, energy and other sectors. In the case of Brazil, partly due to the privatisation of public enterprises, inward M&As increased rapidly in recent years: from US$4.7 billion in 1996 to US$12.6 billion in 1997 and US$24.8 billion in 1998.

The promotion of regional integration, as in Europe and North America, also provides opportunities for expansion through cross-border M&As. In particular, the introduction of the euro may accelerate the current widespread wave of M&As throughout the business sector of the euro-zone. Cross-border M&As in Western Europe reached US$229 billion in 1998 compared to US$138 billion in 1997. The new common currency will reduce exchange rate risk and transaction costs across the European Union which will support trade and business expansion. On the other hand, the euro will increase transparency of prices across the European Union, which will add to competition and price discipline and promote industrial restructuring, including the cross-border merger of firms. However, fundamental location decisions for foreign investment and mergers in Europe will likely remain dependent on factors linked to economic geography, including the relative cost of production factors and the proximity to core markets (Miyake and Thomsen, 1999).

PERFORMANCE EFFECTS OF CROSS-BORDER M&As

The general effect of cross-border M&A activities tends to be a re-organisation of industrial assets and production structures on a global basis. This can lead to greater overall efficiency without necessarily significantly greater production capacity (OECD, 1996*b*). Cross-border M&As facilitate the international movement of capital, technology, goods and services, and the integration of affiliates into global networks. Furthermore, such M&As can bring about efficiency gains through economies of scale and scope. Studies of the performance effects of foreign direct investment, which increasingly consists of M&As, confirm economy-wide positive benefits particularly as regards improved productivity in host countries.

Cross-border M&As can also have positive impacts on growth and employment, particularly if governments have policies which facilitate the associated industrial restructuring. In general, M&As can have the following types of economic effects from the perspective of host countries (as compared to greenfield investments):

- ***Capital accumulation*:** Greenfield investments contribute to capital accumulation in the nearer term by establishing new plants, while M&As can contribute in the longer term. As new foreign owners expand their businesses in host countries, they may undertake new investments in plant and equipment. M&As may also contribute to capital accumulation in a broader sense, *i.e.* in terms of intangible capital such as advanced technology and management skills, rather than merely physical capital.

- ***Employment creation*:** Similarly, greenfield investments tend immediately to create new jobs, while M&As undertaken for the purpose of restructuring often incur layoffs but may contribute to employment gains in the longer term. M&A deals sometimes succeed by cutting capacity, which may mean a loss of product lines and jobs but which could also be essential for the survival of operations. In the long run, new foreign owners may expand their businesses in the host country after successful restructuring, creating new employment opportunities.

- ***Technology transfer*:** M&As as well as greenfield investments can incur positive spillovers by promoting the transfer of new technology, advanced management skills and other forms of intangible assets to the host country. Foreign direct investment, in general, can have a favourable influence on industrial innovative capacity through technology transfer and dissemination.

- ***Competition*:** Greenfield investments increase competition in the host country by adding new entrants into markets, while initially M&As may decrease competition or at best may not alter market structure. However, firms acquired by foreign investors may initiate competition with incumbents in the host country with the help of financial resources and advanced management know-how from parent companies. Furthermore, if inefficient target firms, which otherwise may be forced to exit, are acquired and restructured by foreign investors, M&As may enhance competition in the host country.

- ***Efficiency gains*:** M&As and greenfield investments can enhance efficiency in the host country through technology transfer, industrial restructuring and enhancing competition. For example, according to one study of foreign take-overs of British firms, foreign acquisitions raised productivity (output per employee) as well as real wages, mainly due to higher investment per employee by the new foreign owners.

The gains from M&As for individual firms may differ from their overall economic effects, with findings to date somewhat mixed. In terms of shareholder value, there is broad evidence that mergers entail a gain for the acquired firm, whereas the shareholders of the acquiring firm may break even at best (Caves, 1989). There is a tendency for the shares of the acquiring firm to rise in the year of the merger, only to subside and fall to zero or negative values in subsequent years. According to past studies, many mergers seem to have negative effects on productivity *ex post*; the observed gains from sell-offs and spin-offs of businesses may be related to the removal of the inefficiencies associated with assembling them in the first place. It is important to bear in mind, however, that many of these results pertain to mergers undertaken for the purpose of corporate diversification, with technical and managerial inefficiencies increasing when the acquiring companies lacked necessary competence in the particular industry of the acquired firm.

Earlier studies of mergers and acquisitions in the 1960s, 1970s and 1980s suggest that mergers were more closely linked to excess funds than to cost savings or marketing synergies. Studies of US conglomerate mergers, where companies often lack a complete understanding of the firms they are acquiring, have shown that more than half of the acquired companies are sold off or liquidated within a decade. Studies of mergers in Japan, where managers have traditionally preferred internal growth and looser forms of alliances, show that the M&A trend increased in the 1980s, but there was no evidence that the mergers improved profitability or growth for acquiring firms (Odagiri and Hase, 1989). Similar reviews in European countries prompted doubts about M&As as generators of improved company performance (Mueller, 1980).

However, the bulk of these studies of the performance effects of M&As examined the period before 1990. For most of these studies, questions have also been raised about the ability to accurately measure the full benefits (or costs) of mergers. There are difficulties in estimating how the firms concerned would have performed in the absence of a merger. For example, firms may face a strategic choice in a race to be the first mover or to be acquired. There are problems in using profitability or share value as a test of efficiency gains. And there are contradictory findings for conglomerate mergers *vs.* horizontal mergers where the former tend to show more negative results. Moreover, these results relate to mergers and acquisitions at the national level, and it is unclear to what extent they would be relevant to cross-border M&As.

The existence of unprofitable mergers might also be explained by the fact that factors other than maximising shareholder value are driving strategic decisions. There is a substantial literature suggesting that managerial incentives and objectives may differ from those of shareholders. For example, although profitability decreases, mergers can help to maximise firm size or permanence and reduce business risk, all of which tend to be important objectives for managers if not for shareholders. In fact, acquisitions driven by diversification and growth motives tend to result in lower acquirer returns (Morck *et al.*, 1990). In sum, M&As may be undertaken for strategic reasons without being in the interest of either the firm or the overall economy.

There has been little analysis of the performance effects of cross-border M&As or comparing the effects of cross-border mergers to those of greenfield investments abroad. Recent M&As have tended to be among same-sector firms rather than among those in different sectors (which could alter observed impacts). Different factors, particularly the quest for global-level efficiency and the desire to merge intangible assets, are now driving a large share of M&As. Recent research shows that intangibles such as technological capacity may have an important influence on merger outcomes. The possession or lack of firm-specific intangible assets – including human and managerial resources, research capacity and technology, and product marks and brand names – can affect the performance of companies undertaking mergers. Geographic and cross-industry diversifications tend to increase firm value in the presence of intangible assets but decrease firm value in their absence (Morck and Yeung, 1999). In addition, the full efficiency effects of M&As across international borders can only be assessed in the longer term. Cross-border M&As motivated by the desire to restructure in response to the globalisation of markets and a need for economies of scale should have positive efficiency effects for OECD firms and economies in the presence of properly functioning product and labour markets. However, the competition effects of such mergers must also be carefully monitored.

CONCLUSIONS

In the 1990s, cross-border M&As are increasing in both frequency and size. The current wave of M&As, while involving a wider range of countries, is mostly taking place in the OECD area. Cross-border unions are occurring in all sectors, with some of the larger mergers seen in mature industrial sectors where adjustment to over-capacity and reduced growth prospects is urgently needed. Cross-border M&As are appearing in many high-technology sectors in order to pool resources and abilities to remain competitive and innovative. They are particularly characteristic of service sectors which, as a result of regulatory reform, privatisation and liberalisation of trade and investment regimes, are now able to restructure more freely at both the national and international levels. Unlike previous decades, these mergers are motivated by the desire to consolidate capacities to serve global markets and fully benefit from scale economies. The concentration of resources on core competencies and the full utilisation of intangible assets are key to the competitive strategies of multinational firms. These are aims that may be better achieved through cross-border M&As than through other types of foreign investment.

Cross-border M&As can yield dividends in terms of company performance and profits as well as benefits for home and host countries when successful industrial restructuring leads to greater efficiency without undue market concentration. International M&As can play a role in revitalising ailing firms and local economies and creating jobs through the restructuring process, acquisition of technology and productivity growth. Yet, countries have differed widely in their openness to foreign direct investment, including cross-border M&As, and in the benefits they have realised from the ongoing globalisation of industry. Government policies and corporate culture caused some countries to be largely closed to foreign acquisitions until recently. Japan, Korea and some European countries have been slow to encourage industrial restructuring through cross-border M&A although this is changing. Other countries, such as the United States and the United Kingdom, may realise efficiency improvements through such merger activity in the nearer term. Regulatory reform, privatisation and more equitable treatment of foreign firms in public procurement and other government programmes now signal a new openness which is encouraging more international merger activity. The ongoing liberalisation of foreign investment regimes indicates that a broader range of countries could realise benefits from cross-border M&As.

However, countries which are hosts to a high level of cross-border M&A activity may not all benefit equally. The government policies and related framework conditions to garner positive spillover effects from inward and outward foreign investment may not be in place. Poorly functioning factor and product markets could impede industrial restructuring through M&As and dampen any favourable impacts in terms of economic expansion and job creation. Flexible labour markets are essential for facilitating the contraction, expansion and alterations of activities and employment which may stem from cross-border M&As. The challenge for governments is to have appropriate frameworks in place to attract foreign investment, including M&As, and to realise efficiency gains and positive spillovers from the interconnections between domestic and foreign firms.

Globalisation of industry through cross-border mergers and acquisitions has broader implications for industry-related policies. As more domestic firms are taken over by foreign companies or acquire foreign companies and the interdependency of national economies increases, the relevance and effectiveness of national policies may decrease. Through international mergers, the nationality of firms is becoming even more vague. Multinational firms are more than ever footloose, with terms such as *home* and *host* countries becoming meaningless. The firms themselves have facilities and employees in diverse countries, serve many national markets and purchase supplies and components worldwide. They are showing less loyalty to particular countries and increasing resentment towards country-level regulations and restrictions which may hinder their activities and prevent them from realising the gains from cross-border investments. The growing wave of cross-border M&A – driven by intangible as well as tangible factors – will demand greater co-operation among countries in formulating industry-related policies which take into account the ever-increasing international nature of firms.

BIBLIOGRAPHY

ANDERSSON, T. (1993), *Managing Trade Relations in the New World Economy*, Routledge, London.

ANDERSSON, T. and R. SVENSSON (1994), "Entry Modes For Direct Investment Determined by the Composition of Firm-specific Skills", *Scandinavian Journal of Economics 96(4)*, pp. 551-560.

CAVES, R.E. (1982), *Multinational Enterprise and Economic Analysis*, Cambridge University Press, Cambridge.

CAVES, R.E. (1989), "Mergers, Takeovers, And Economic Efficiency: Foresight vs. Hindsight", *International Journal of Industrial Organization*, 7:1, pp. 151-174.

DUNNING, J.H. (1977), "Trade, Location of Economic Activity and the MNE: A Search for an Eclectic Approach", in B. Ohlin, P.O. Hesselborn, and P.M. Wijkman (eds), *The International Allocation of Economic Activity: Proceedings of a Nobel Symposium held at Stockholm*, Macmillan, London, pp. 395-418.

KPMG Corporate Finance (1999), *Worldwide Statistics on Cross-border M&A from 1988 to 1998*.

MIYAKE, M. and S. THOMSEN (1999), "Recent Trends in Foreign Direct Investment", *Financial Market Trends*, No. 73, June.

MIOTTI, L. and F. SACHWALD (1999), "Foreign Direct Investment as a Technology Sourcing Strategy: The Case of Korean Multinationals", paper presented at the International Conference on Multinational Firm Strategies, Paris, 17-18 June.

MORCK, R., A. SCHLEIFER and R. VISHNY (1990), "Do Managerial Objectives Drive Bad Acquisitions?", *Journal of Finance*, Vol. 45, pp. 31-48.

MORCK, R. and B. YEUNG (1999), "Why Firms Diversify: Internalization *vs*. Agency Behavior", paper presented at the OECD International Symposium on Intellectual Capital, Amsterdam, 9-11 June.

MUELLER, D. (1980), *The Determinants and Effects of Mergers*, Gunn and Hain, Cambridge, MA.

MUELLER, D. (1989), "Mergers: Causes, Effects and Policies", *International Journal of Industrial Organization*, 7:1, pp. 1-10.

NEVEN, D. and G. SIOTIS (1994), "Technology Sourcing and FDI in the EC: An Empirical Evaluation", Working Paper.

ODAGIRI, H. and T. HASE (1989), "Are Mergers and Acquisitions Going to be Popular in Japan Too?: An Empirical Study", *International Journal of Industrial Organization*, 7:1, pp. 49-72.

OECD (1988), *International Mergers and Competition Policy*, OECD, Paris.

OECD (1994), *Merger Cases in the Real World: A Study of Merger Control Procedures*, OECD, Paris.

OECD (1996*a*), "Efficiency Claims in Mergers and Other Horizontal Agreements", OCDE/GD(96)65, OECD, Paris.

OECD (1996*b*), *Globalisation of Industry: Overview and Sector Reports*, OECD, Paris.

OECD (1999*a*), "Foreign Direct Investment and International Trade: Complements or Substitutes", STI Working Paper.

OECD (1999*b*), *Globalisation of Industrial R&D: Policy Implications*, OECD, Paris.

OECD (1999*c*), *Financial Market Trends*, No. 73, June, OECD, Paris.

OECD (1999*d*), *OECD Communications Outlook, 1999*, OECD, Paris.

PRICEWATERHOUSECOOPERS (1999*a*), *Global Automotive Deals Survey 1998*.

PRICEWATERHOUSECOOPERS (1999*b*), *Pharmaceutical Sector Market & Deal Survey*.

SVENSSON, R. (1998), "The Choice of Entry Mode in Foreign Direct Investment", in P. Braunerhjelm and K. Ekholm (eds.), *The Geography of Multinational Firms*, pp. 156-168, Kluwer Academic Publishers, Stockholm.

UNCTAD (1998), *World Investment Report: Trends and Determinants*.

US DEPARTMENT OF COMMERCE (1999), "Foreign Investor's Spending to Acquire or Establish US Business", Bureau of Economic Analysis (BEA) News Release.

VASCONCELLOS, G.M. and R.J. KISH (1998), "Cross-Border Mergers and Acquisitions: The European-US Experience", *Journal of Multinational Financial Management*, 8:4, pp. 431-450.

YAMAWAKI, H. (1994), "International Competitiveness and the Choice of Entry Mode: Japanese Multinationals in the US and European Manufacturing Industries", Working Paper.