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9. Cross-border mergers and acquisitions

Isil Erel, Yeejin Jang, and Michael S. Weisbach

1 INTRODUCTION

One of the most consequential events in any firm's lifetime is a major acquisition. For the target, being acquired means the end of its existence as a separate entity; and for the acquirer, merging with a different firm usually requires a substantial change in the way that firm operates. Acquisitions redraw the boundaries of firms, change the merging firms' cultures, create (or destroy) synergies, and affect the ability of both the former acquirer and the target to access capital markets. They affect every aspect of the management of a business.

Because of their importance, acquisitions have been an enormous area of research. However, the vast majority of this research has focused on domestic deals. Cross-border acquisitions, however, constitute about 30 percent of the total number and 37 percent of the total volume of acquisitions around the world in recent years (see Figure 9.1). This percentage has increased as the world's economy has become increasingly integrated. While many cross-border deals occur for the same reasons as domestic ones, there are some factors that motivate cross-border acquisitions but not domestic ones. A new strand of research has been developed to understand the role of these factors leading to cross-border acquisitions.

This chapter surveys the literature on cross-border mergers and acquisitions (M&As). There are a number of excellent surveys of the literature focusing on domestic mergers and acquisitions (see, for example, Jensen and Ruback, 1983; Jarrell et al., 1988; Betton et al., 2008; and Mulherin et al., 2017). Here, in contrast, we discuss the literature studying international factors that affect cross-border deals but not domestic ones. One survey focusing on cross-border deals is Chari (2021), who documents detailed statistics on the ownership of firms across borders and discusses incentives that drive firms to operate across borders.¹ As cross-border mergers and acquisitions become more common, these factors are likely to be increasingly important in the future.

We begin by presenting a set of facts about cross-border mergers and acquisitions in Section 2. The number of cross-border deals has increased from about 1,500 per year in the early 1990s to around 4,000 in recent years. These deals represent between 26 and 33 percent of the total; the fraction increases to between 24 and 52 percent value-weighted since cross-border deals are, on average, larger than domestic ones. Similar to most studies of cross-border acquisitions, there appears to be a small positive stock price reaction for acquirers, and a larger positive one for targets.

Section 3 then presents and discusses the literature on international factors that can affect cross-border acquisitions. One such factor is differences in the way a country's laws and institutions protect the interests of a firm's shareholders. If legal rules protecting shareholders' rights can increase a firm's ability to access capital markets, and market estimates of the firm's future cash flows, then the improvements in legal protection could

provide a motive for a cross-border acquisition. We discuss a number of papers that have addressed the extent to which legal or regulatory reasons lead to cross-border acquisitions in Subsection 3.1.

Cross-country differences in corporate governance are not the only international factors that can lead to acquisitions. Differences in regulation also lead firms to merge with other firms in different countries and transfer their regulatory environment to the more favorable one. Papers studying the regulatory arbitrage motive with regard to banking, labor, and climate regulations are discussed in Subsection 3.2.

A potential impediment to merging firms in different countries is the protection of intellectual property (IP). If a firm uses proprietary technology in its products, it can be risky to share that technology in countries that allow other companies to appropriate it without sufficient compensation. Consequently, the potential infringement of intellectual property rights could be one factor that lowers the incidence of cross-border mergers. We discuss several papers that provide empirical support for this idea in Subsection 3.3.

Cultural factors can also affect the successful merger of two firms, especially if the firms are from different countries. If the employees at two firms come from very different cultures, then combining the two firms into one can be difficult. Subsection 3.4 summarizes several papers that estimate the extent to which cultural factors affect the likelihood and profitability of acquisitions.

Another important factor that can affect the likelihood and value of cross-border acquisitions is political differences. If there is tension between two countries, it would be more difficult to consummate a merger between firms from those countries than if the countries get along well. Politics within a country can also affect firms' abilities to complete deals: nationalistic pressures can potentially make it harder for a firm to be acquired by a foreign bidder if the domestic firm is considered important to the national interest. Subsection 3.5 discusses a number of papers that explore these ideas.

Opportunities to reduce corporate taxes can also lead to cross-border acquisitions. One way in which firms avoid taxes is by using transfer pricing and other strategies to move their income to subsidiaries in "tax havens," where tax rates are particularly low. But, to adopt such a strategy, a firm must have such a subsidiary in a country with favorable tax rates. Subsection 3.6 examines work studying the way in which cross-border acquisitions are motivated by the desire to acquire subsidiaries in tax havens.

Finally, the desire to expand a firm's specialized product internationally can lead to cross-border acquisitions. To expand internationally a firm could, in principle, set up new operations outside its home country and grow organically. However, for a number of reasons, it can be more efficient for a firm to acquire a local firm in a foreign country than to establish its own subsidiary overseas. Subsection 3.7 discusses research suggesting that cross-border acquisitions can be used for such expansion of specialized product lines.

While Section 3 considers factors that could either lead to or deter cross-border acquisitions, Section 4 focuses on the process of structuring the deals. It surveys literature discussing the ways in which investors can help identify cross-border targets and complete such acquisitions. Institutional investors can have both information advantages and connections in foreign countries. Subsection 4.1 considers institutional investors and discusses work that evaluates the extent to which they help minimize information asymmetries and regulatory difficulties firms have in completing cross-border acquisitions.

Particularly important to institutional investors are private equity investors, which include both buyout funds and venture capital funds. These investors play an active role in the management of their portfolio companies and are specialists in adding value to them, in part by knowing about potential overseas acquisition targets and the process of buying them. Subsection 4.2 discusses several papers that examine this idea and the way in which venture capitalists can affect overseas innovations through acquisitions.

Much work on cross-border acquisitions concerns the valuation of the merging firms, which is discussed in Section 5. Pricing, both of acquirers and targets, can affect the choice of deals. If a firm is more highly valued, it will face a lower cost of capital and be more likely to make acquisitions. In addition, if a firm is undervalued, it can be an attractive target. Since a large fraction of stock price movements is country-specific, it seems likely that many price-driven acquisitions are cross-border ones. Subsection 5.1 evaluates work studying the impact of stock prices on the choice of cross-border mergers and acquisitions.

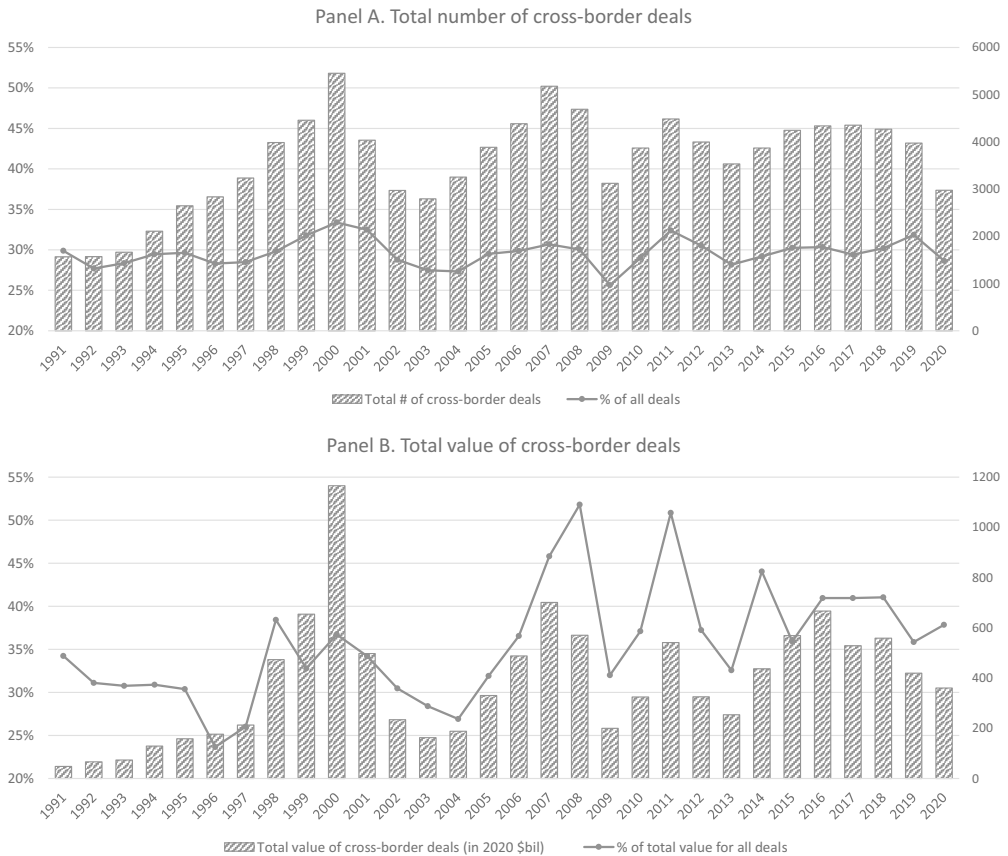
An important stylized fact about diversified firms across industries is that they trade at a discount compared to single-segment ones, holding other things constant. This finding is commonly interpreted as diversifying acquisitions being inefficient. Similar logic applies internationally: if internationally diversified firms trade at a discount, cross-border acquisitions are likely wealth-decreasing. Subsection 5.2 considers work studying this issue.

After a deal is identified and the firm is acquired, the ultimate consequence of the deal is to affect the value of the acquired firm. The most common way to study cross-border (and other) acquisitions is to perform “event studies” designed to measure the abnormal change in value around the announcement of cross-border acquisitions. These studies generally find that the deals do increase the value of acquirers. Subsection 5.3 surveys these papers.

2 FACTS ABOUT CROSS-BORDER ACQUISITIONS

A large fraction of worldwide acquisitions is of firms based in countries other than that of the acquirer. In Figure 9.1, we plot the number (Panel A) and transaction value (Panel B) of the cross-border deals by deal completion year over the period 1991–2020. Our sample includes M&A deals across 48 countries that were announced between 1991 and 2020 and completed by the end of 2020, obtained from the Securities Data Company (SDC) Mergers and Corporate Transactions database.² We exclude partial equity stake acquisitions, acquisitions of the remaining interest, and deals where either the target or the acquirer is a financial firm (SIC codes 6000–6999) or a utility firm (SIC codes 4900–4999). We define a deal as a cross-border deal if the target’s nation is different from that of the acquirer’s ultimate parents.

Panel A of Figure 9.1 shows that the total number of cross-border deals has increased from about 1,500 to about 4,000 annually in recent years. These deals typically represent between 26 percent and 33 percent of the total deal volume. Panel B shows that cross-border deal volume increased from less than \$48 billion to almost \$1,165 billion of total deal value in the 2000s. The ratio of cross-border to total deal value has fluctuated between 24 percent and 52 percent in the past three decades. The fact that the fraction of cross-border deals is higher when deals are value-weighted than when equally weighted implies that cross-border deals tend to be larger than domestic ones.



Note: This figure plots the number (Panel A) and the aggregated transaction value in 2020 dollars (Panel B) of the cross-border M&A deals by the year 1991–2020. The sample includes mergers and acquisitions deals in 48 countries, announced between 1991 and 2020 and completed by the end of 2020, obtained from the mergers and acquisition deals from the SDC Mergers and Corporate Transactions database. LBOs, spin-offs, recapitalizations, self-tender offers, exchange offers, and repurchases are excluded. We further exclude partial equity stake acquisition, acquisitions of the remaining interest, and deals where either the target or the acquirer is a financial firm (SIC codes 6000–6999) or a utility firm (codes 4900–4999). A deal is defined as a cross-border deal if the target's nation is different from that of the acquirer's ultimate parents. The bars represent the numbers or values of cross-border acquisitions in a given year, and the solid lines represent the fraction of cross-border acquisitions relative to the total number of aggregated deal value of all domestic and cross-border acquisitions. In Panel B, the sample is further restricted to the deals with deal value information available in the SDC database.

Figure 9.1 Distribution of domestic and cross-border acquisitions, 1991–2020

2.1 Who Buys Whom?

Which countries' firms tend to merge with which other countries' firms? To provide a detailed answer to this question, Table 9.1 presents statistics on 361,630 mergers and acquisitions across 48 countries between 1991 and 2020. The columns represent the countries of the acquirers, while the rows represent those of the targets. The diagonal entries

in the matrix are the number of domestic deals in a particular country, and the off-diagonal entries are the number of cross-border deals between two countries. As expected, the largest numbers are on the diagonals since the number of domestic deals generally exceeds the number of cross-border ones. For example, only about 19 percent of U.S. acquirers have non-U.S. targets. However, this ratio varies by country: for instance, it drops to about 7 percent for Russian acquirers but increases to above 75 percent for Ireland and Luxembourg.

Table 9.2 presents statistics on some characteristics of cross-border acquisitions. Public firms are the most common acquirers, with around 46 percent. However, the majority of targets are private at the time they are acquired: 60 percent of the targets are private firms, and another 35 percent are subsidiaries of other firms. Consequently, many studies relying on samples of public firms' acquisitions of other public firms are not likely to be reflective of acquisitions more broadly since they rely on a small fraction of deals (3 percent).³

Panel B of Table 9.2 presents the number and percentage of deals by acquirer and target countries classified as emerging or developed based on the Morgan Stanley Capital International (MSCI) definition. Firms from developed countries are more active acquirers in the cross-border acquisition market, making up 91 percent of all acquisitions. These acquirers most often acquire firms from developed countries, with developed-to-developed country acquisitions constituting 75 percent of cross-border acquisitions. Firms in developed countries do acquire firms in emerging markets as well, with this type of deal amounting to about 15 percent of cross-border acquisitions.

Panel C summarizes important deal characteristics of cross-border acquisitions. In the sample of announced cross-border deals, 97 percent are completed. The majority of cross-border acquisitions are cash deals (75 percent), that is, where more than 50 percent of the price is paid in cash. The sample is evenly split between diversifying and related deals – 48 percent of cross-border transactions are diversifying, meaning that the acquirer and the target in these deals are not in the same two-digit SIC. Hostile deals are rare in the cross-border M&A market (less than 1 percent). Acquirers are substantially larger than targets, with the average transaction value being only 14 percent of the acquirer's market value, and the median is just 5.2 percent.

Next, we present statistics on the industry composition of acquirers. The ratio of diversifying acquisitions appears to vary with the industry. In Figure 9.2, we present the industry composition of the cross-border deals in our sample of 48 countries. The top industries in terms of the total number of cross-border deals are business equipment (with over 20,000 acquisitions) and manufacturing (with over 15,000 acquisitions). While only 38 percent of acquirers in the business-equipment industry engage in diversifying acquisitions, this number increases to 59 percent for acquirers in manufacturing.

2.2 Valuation

In this section, we calculate the changes in acquirers' and targets' stock market valuations on the announcement of cross-border acquisitions. Table 9.3 presents the cumulative announcement returns (CARs) of merging firms over the three and five days around the announcement. The CARs are calculated based on a market-adjusted model in which abnormal returns are defined as stock returns in excess of the overall stock market return,

Table 9.1 Number of cross-border acquisitions by country pair

Target Country	Acquirer Country																		
	ARG	AUS	AUT	BEL	BRA	CAN	CHL	CHN	COL	HRV	CYP	CZE	DNK	FIN	FRA	DEU	GRC	HKG	HUN
	IND	IDN	IRL	ISR	ITA	JPN													
Argentina (ARG)	322	15	3	3	82	95	29	7	4				6	2	63	27	2	2	4
Australia (AUS)	1	10,039	10	25	11	315		135			1	1	21	22	113	143	1	88	77
Austria (AUT)		11	660	11		22		11	1		1	5	19	18	55	398	3	2	5
Belgium (BEL)		24	19	979	4	39	2	7					22	26	374	160	4	3	20
Brazil (BRA)	45	56	10	36	2,110	133	42	26	9				18	14	234	123		14	1
Canada (CAN)		181	21	65	15	12,991	4	74	5	1			31	29	258	139	5	32	3
Chile (CHL)	11	49	1	7	16	95	262	2	7				5	3	20	16		1	4
China (CHN)		63	8	18	2	91	1	9,634					8	17	102	67	1	779	16
Colombia (COL)	9	11	1	2	22	91	20	4	154				5	1	33	11			3
Croatia (HRV)		1	30	3		1			83			2	4	3	12	20	1		3
Cyprus (CYP)		2				5		1			66		1	1	2	1	16	3	1
Czech Republic (CZE)		4	51	21	2	7		10	3		1	514	14	17	71	151	1	1	12
Denmark (DNK)		14	12	22		26	1	12	1		2		1,540	80	83	158	1	9	8
Finland (FIN)		10	11	10		40		7	1		2	1	115	2,473	50	88	1	6	2
France (FRA)	3	56	49	393	7	198	2	80	1			10	64	53	10,643	634	9	30	3
Germany (DEU)	1	75	448	168	8	158	3	181	2		2	32	158	194	763	10,394	16	44	7
Greece (GRC)		2	3	12		3		2			11		5	1	8	16	548	2	2
Hong Kong (HKG)		50	2	6	2	44		292					8	4	22	24	3	890	9
																			2
																			2
																			2
																			5
																			4
																			83

Target Country	Acquirer Country																							% cross- border deals	
	LUX	MYS	MEX	NLD	NZL	NOR	PER	PHL	POL	PRT	RUS	SGP	ZAF	KOR	ESP	SWE	CHE	TWN	THA	TUR	GBR	USA	VEN		Total
Argentina (ARG)	11		32	25	4	3	5			1	1		6	2	69	18	19		1		87	300	6	1,301	75%
Australia (AUS)	12	67	2	108	216	23		18		1	2	198	108	12	26	71	108	5	29	3	668	1,473		14,512	31%
Austria (AUT)	11		3	37		12			2	2	4	2	8	1	6	32	90	5	1	2	65	139		1,725	62%
Belgium (BEL)	29	2	1	301	1	12			3	3	3	8	6	1	18	63	51	1	2	2	198	339		2,838	66%
Brazil (BRA)	24	4	61	60	6	27	3	2	2	46	5	12	18	4	125	33	62	3	1	1	168	776	2	4,560	54%
Canada (CAN)	12	15	21	108	10	29	4	5	5	2	12	17	23	26	22	68	114	17	4	3	516	4,349	1	19,561	34%
Chile (CHL)	2		22	14	10	8	16		1	2		1	5		52	12	8				27	143	2	858	69%
China (CHN)	4	67	3	34	7	3		9	1	2	3	176	2	81	15	26	38	123	10	2	119	581		12,379	22%
Colombia (COL)	4	1	37	4	1	17		1					4	1	36	5	15				25	101	5	638	76%
Croatia (HRV)			1	5				1	7	1	6			1	2	10	11			1	15	10		249	67%
Cyprus (CYP)						5			2		19	4	3	1			3			1	11	13		165	60%
Czech Republic (CZE)	9		1	49		18			34	3	17		4	6	16	42	37	3			64	131		1,377	63%
Denmark (DNK)	8	2	1	80	1	213			5		2	7	3	2	9	383	46	2	1		198	323		3,336	54%
Finland (FIN)	12	1		47		109			1	1	9	7	2	1	11	513	39	4	1	1	101	221		4,002	38%
France (FRA)	71	2	6	274	5	51			7	20	8	16	12	10	196	196	258	5	10	3	836	1,520		16,350	35%
Germany (DEU)	91	18	13	602	9	84			41	16	29	34	43	37	109	312	749	30	13	21	974	2,372	1	18,962	45%
Greece (GRC)	3			9		3			1	1	4		1	1	3	6	10			3	23	32		736	26%
Hong Kong (HKG)	1	94		8	1	1		4			3	98	8	15	1	7	13	27	10	1	91	245		2,080	57%

Table 9.1 (continued)

Target Country	Acquirer Country																		
	ARG	AUS	AUT	BEL	BRA	CAN	CHL	CHN	COL	HRV	CYP	CZE	DNK	FIN	FRA	DEU	GRC	HKG	HUN
	IND	IDN	IRL	ISR	ITA	JPN													
Hungary (HUN)	1	48	8			7		3				8	5	10	36	92	3		289
India (IND)	33	10	10	1	33			16	1			12	12	12	129	112	1	17	
Indonesia (IDN)	61		3		30			24						2	10	12	1	21	
Ireland (IRL)	19	3	10	1	41			5				11	5	5	51	29	2	5	
Israel (ISR)	5	12	2	3	1	36		14			2	4	1	24	27			1	
Italy (ITA)	25	53	50	9	49			62			1	26	41	376	352	15	21	6	
Japan (JPN)	7		6	3	23			68	1			3	5	52	50	5	32		
Luxembourg (LUX)			28		3			5				2	1	39	24	2			
Malaysia (MYS)	32		1	1	8			26				5	3	15	15		35		
Mexico (MEX)	6	15	1	5	16	316	10	12	9			7	4	36	42	3	5		
Netherlands (NLD)	36	41	233	4	101	2	48	2	2	4	56	61	276	418	7	12	1	37	
New Zealand (NZL)	472	2	4		64		19				2	4	27	27				7	
Norway (NOR)	15	14	15	5	39	1	10		1	4	1	176	108	50	84	4	2	2	
Peru (PER)	3	20	1	3	10	136	30	6	4		1			7	3		2		
Philippines (PHL)	22	1	1		13		2				1			8	4		12		
Poland (POL)	6	24	12		25		3			4	3	11	35	27	100	143	6	2	
Portugal (PRT)	1	5	2	11	6	15	2	3	1		1	7		81	38		3	2	
Russia (RUS)	2	6	13	16		33	12		1		48	3	9	54	68	104	7	6	
Singapore (SGP)	81	2	2		17		71					8	3	34	31	68		68	
South Africa (ZAF)	2	85	3	7	1	66	12				7	11	48	60	2	11	29	9	

Target Country	Acquirer Country																							% cross- border deals	
	LUX	MYS	MEX	NLD	NZL	NOR	PER	PHL	POL	PRT	RUS	SGP	ZAF	KOR	ESP	SWE	CHE	TWN	THA	TUR	GBR	USA	VEN		Total
Hungary (HUN)	3			47		7			12		5	4	6			2	11	18	1	2	1	34	91	789	63%
India (IND)	10	38	3	32	2	9		3	1	1	6	61	12	17	18	26	54	3	5		193	617	4,620	36%	
Indonesia (IDN)	2	99	1	10		3		6				131	4	31	2	2	10	1	21	1	32	52	1,140	60%	
Ireland (IRL)	1	2	8	17	4	12			3	1	3	6	6	1	10	19	14		1		431	389	1,827	63%	
Israel (ISR)	2	1	1	7			1				2	3	2	2	4	6	12	1		2	37	432	1,036	65%	
Italy (ITA)	41	4	2	132	1	17	1		8	5	17	7	9	9	104	96	141	5	2	16	294	687	6,266	46%	
Japan (JPN)	5	10		26				1			2	25	2	62	4	18	25	36	7	1	79	333	17,513	5%	
Luxembourg (LUX)	29		3	11	1	1			1				2	3	2	4	4				24	30	235	88%	
Malaysia (MYS)	1	2,777	1	9	3	3		7			1	238	2	11	6	5	9	12	11		46	88	3,507	21%	
Mexico (MEX)	3		434	21	5	2	1	2				2	3	1	67	13	10	2			51	473	1	1,637	73%
Netherlands (NLD)	33	12	6	3,079	4	46		1	6	2	13	10	17	4	46	142	124	6	6	6	568	811	2	6,558	53%
New Zealand (NZL)	5	20		15	1,204	3		2		1		32	12	3	1	10	17	1	5		105	263	2,401	50%	
Norway (NOR)	5	3	2	47		1,817		1	5	1	2	10	2	6	10	484	32	1	4	1	208	253	3,482	48%	
Peru (PER)		2	18	4			159			1	1	1	2		33	1	6				16	74	554	71%	
Philippines (PHL)		12	3	2				265				24	2	6	1	1	2	1	8		17	57	516	49%	
Poland (POL)	24			61		30			1,054	7	2	3	17	6	34	56	25	3		3	88	145	2,056	49%	
Portugal (PRT)	7		1	14		8			1	386	1	1	1	1	133	12	19		3		66	86	956	60%	
Russia (RUS)	15		1	57	1	25			15	1	3,786	1	4	11	8	28	31		2	3	100	156	4,703	19%	
Singapore (SGP)	3	179	1	13	3	20		6	1		1	1,128	10	14	6	10	15	19	27	1	91	222	2,355	52%	
South Africa (ZAF)	3	5		20	1	4		1			3	6	1,456	6	7	34	38	2		1	225	189	2,409	40%	

Table 9.1 (continued)

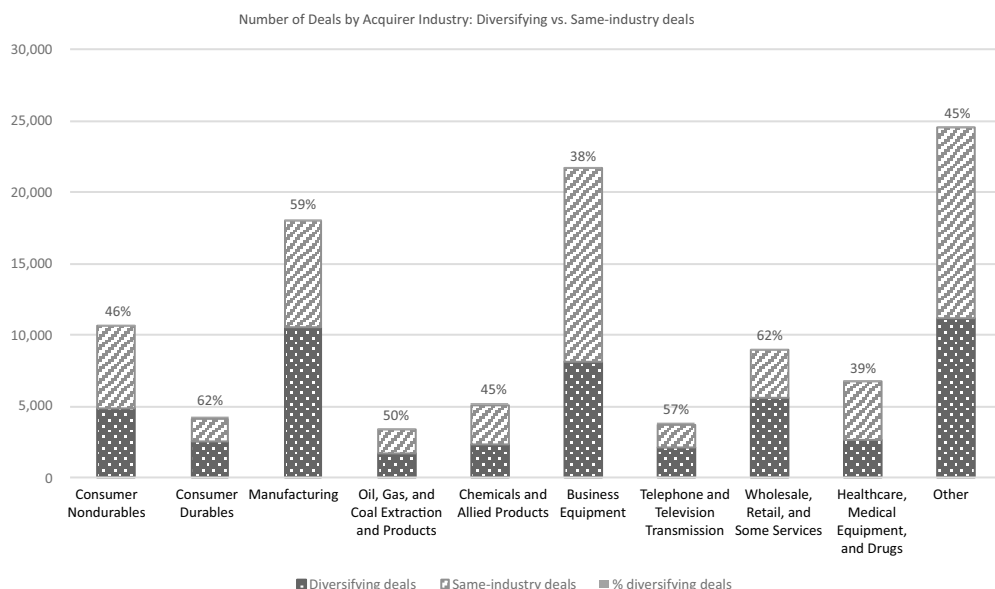
Target Country	Acquirer Country																							% cross-border deals	
	LUX	MYS	MEX	NLD	NZL	NOR	PER	PHL	POL	PRT	RUS	SGP	ZAF	KOR	ESP	SWE	CHE	TWN	THA	TUR	GBR	USA	VEN		Total
South Korea (KOR)	2	3	2	12	2						1	17	3	3,209	4	15	20	7			41	197		3,817	16%
Spain (ESP)	23	1	47	194	2	26	2		14	76	8	10	10	3	4,560	86	92	1	4	4	392	519	1	7,634	40%
Sweden (SWE)	14	1		109		424		1	5	1	4	8	4	4	9	3,879	72	4		1	327	519	2	6,744	42%
Switzerland (CHE)	21	4		69	2	15		2	8	1	13	20	15	4	13	79	2,169	5	2	2	163	460		4,346	50%
Taiwan (TWN)	4	6		1				2				22	1	9		8	2	513	3		11	132		866	41%
Thailand (THA)		41		9	2	1		1	1			53	4	11		6	3	8	486		32	57		922	47%
Turkey (TUR)	6	7	2	21		3		1	6	4	9	9	13	4	10	26	23		2	482	62	103		1,119	57%
United Kingdom (GBR)	53	40	9	406	24	152	3	7	9	5	23	86	181	28	128	380	229	19	45	6	23,719	5,232	1	35,642	33%
United States (USA)	100	42	171	731	68	163	3	31	10	6	57	215	131	185	206	654	712	143	19	14	4,616	1,08,169	15	1,30,132	17%
Venezuela (VEN)	1		2	1							1		1		7	1	4			1	6	51	82	219	63%
Total	720	3,582	922	6,942	1,598	3,394	215	380	1,272	600	4,088	2,713	2,190	3,853	6,151	7,909	5,603	1,019	746	590	36,260	1,33,955	121	3,61,630	
% cross-border deals	96%	22%	53%	56%	25%	46%	26%	30%	17%	36%	7%	58%	34%	17%	26%	51%	61%	50%	35%	18%	35%	19%	32%		

Note: This table presents the number of acquisition deals by the acquirer–target country pair, using the sample of M&A deals in 48 countries announced between 1991 and 2020 and completed by the end of 2020. The columns represent the countries of the acquirers and the rows represent those of the targets. The diagonal entries of the matrix are the number of domestic deals in a particular country, and the off-diagonal entries are the number of cross-border deals between two countries.

Table 9.2 Characteristics of cross-border acquisitions

Panel A. Acquirer and target type					
Acquirer Type		Target Type			
		Private	Public	Subsidiary	Total
Private	N	13,107	447	8,118	21,672
	Percent (%)	12.7	0.4	7.9	21.0
Public	N	28,871	2,783	16,119	47,773
	Percent (%)	27.9	2.7	15.6	46.2
Subsidiary	N	20,300	1,470	12,210	33,980
	Percent (%)	19.6	1.4	11.8	32.9
Total	N	62,278	4,700	36,447	103,425
	Percent (%)	60.2	4.5	35.2	100.0
Panel B. Emerging vs. developed country					
Acquirer Country		Target Country			
		Emerging	Developed	Total	
Emerging	N	2,537	7,240	9,777	
	Percent (%)	2.4	6.7	9.1	
Developed	N	16,707	81,295	98,002	
	Percent (%)	15.5	75.4	90.9	
Total	N	19,244	88,535	107,779	
	Percent (%)	17.9	82.1	100.0	
Panel C. Deal Characteristics					
Variable					
Completion rate		97.12%			
		N	Mean	Median	Std. Dev
Payment method					
Cash deal		20,390	0.749	1.000	0.434
Stock deal		19,751	0.186	0.000	0.389
Diversifying deal		106,857	0.483	0.000	0.500
Friendly deal		107,779	0.990	1.000	0.101
Relative Size of Target					
Transaction Value/Acquirer Book Value		17,789	35.444	9.721	63.398
Transaction Value/Acquirer Market Value		12,655	0.141	0.052	0.210

Note: This table shows the characteristics of cross-border acquisitions. The sample includes mergers and acquisitions deals in 48 countries, announced between 1991 and 2020 and completed by the end of 2020, obtained from the mergers and acquisition deals from the SDC Mergers and Corporate Transactions database. LBOs, spin-offs, recapitalizations, self-tender offers, exchange offers, and repurchases are excluded. We further exclude partial equity stake acquisition, acquisitions of the remaining interest, and deals where either the target or the acquirer is a financial firm (SIC codes 6000–6999) or a utility firm (SIC codes 4900–4999). A deal is defined as a cross-border deal if the target's nation is different from that of the acquirer's ultimate parents. Panel A categorizes acquisitions based on the acquirer and target types. Panel B shows the number and the percentage of deals by acquirer and target countries. A country is categorized as an emerging or developed country based on the MSCI definition. Panel C shows a list of deal characteristics of cross-border acquisitions. The completion rate is calculated based on the sample of completed and withdrawn deals. A deal is defined as a cash (stock) deal if more than 50% of the deal value is paid in cash (stock). A deal is classified as diversifying deal if target firms are not in the same industries as acquirers based on the 2-digit SIC code. Relative size of the target is winsorized at 5% and 95%.



Note: This figure presents the number of diversifying and same-industry merger deals and the percentage of diversifying deals by the acquirer industry. We use the Fama–French 12 industry classification for the acquirers. A deal is defined as a diversifying deal if the first two-digit SIC code of a target is different from that of the acquirer's ultimate parent, and as a same-industry deal if the acquirer's ultimate parent and target have the same SIC two-digit code.

Figure 9.2 Distribution of cross-border acquisitions by acquirer industry

Table 9.3 Cumulative announcement returns of cross-border acquisitions

	N	Mean (%)	Std. Dev (%)	p25 (%)	Median (%)	p75 (%)
<i>Acquirer</i>						
CAR[–1,+1]	39,500	0.65	4.21	–1.52	0.27	2.40
CAR[–2,+2]	37,906	0.73	5.14	–2.00	0.37	3.03
<i>Target</i>						
CAR[–1,+1]	11,585	4.28	11.84	–1.27	0.84	4.74
CAR[–2,+2]	11,037	4.67	12.87	–1.64	1.00	5.70

Note: Stock returns are obtained for ultimate parents of acquirers and targets (or ultimate parents of targets if targets are subsidiaries). CAR is calculated based on the market-adjusted model in which abnormal returns are defined as stock returns in excess of stock market returns, assuming a market beta of one. Extreme values are trimmed at 1% and 99%.

which implicitly assumes a beta of one. As discussed above, there are fewer targets than acquirers that are publicly traded.

Statistics for the three-day or five-day acquirer CARs around the acquisition announcement show a small positive effect. This is similar to many findings in the literature, where abnormal returns for the cross-border acquirers are typically positive but small (see

Section 5.3). In addition, as is usual in the M&A literature, targets have positive reactions. The mean target CAR is 4.3 percent (4.7 percent) over three (five) days around the announcement of the acquisition.

3 REASONS FOR CROSS-BORDER ACQUISITIONS

The underlying reason for any merger is that the participants believe the two firms will be more valuable as a combined entity than as separate firms. However, the principle of conservation of value means that merging two firms does not in itself create value. To make a merger profitable after paying the legal, investment banking, and other costs there must be something that causes the cash flows of the combined firms to be strictly greater than the sum of what the cash flows of the two separate firms would be if they had not merged. In other words, every merger should have an identifiable source of value; otherwise, the firms would be better off not merging.

The sources of value in many cross-border acquisitions are the same as the sources of value in domestic ones. These include operational or financing synergies, acquiring innovation or labor, wealth transfers from workers and governments, and creation of monopoly rents, among other factors. These motives for mergers and acquisitions have been extensively studied in the literature and have been the subject of a number of excellent surveys, the most recent of which is Mulherin et al. (2017).

In this chapter, we focus on potential sources of value that are unique to cross-border acquisitions. Several papers propose such reasons that are relevant for cross-border deals but not for domestic deals. In this section, we discuss the way in which each motivation can lead to merger gains, as well as the literature that has evaluated it empirically.

3.1 Legal Protections of Shareholders' Rights

Much work on cross-border acquisitions has focused on a firm's legal system and how it protects shareholders' rights. Legal protection can have a substantial impact on a firm's corporate financial decisions. Shleifer and Vishny (1997) and La Porta et al. (1998) started a strand of literature contending that there are substantial differences across countries in the way in which legal systems protect shareholders' rights. These differences in shareholder protection, as well as other country-specific regulations, can materially affect not only firms' abilities to raise capital but also firms' financial policies and valuations. This literature mostly focuses on differences between common law and civil law as determinants of legal protection; but, even for countries with the same legal system, there can be noticeable differences in shareholder rights, which has implications for cross-border acquisitions. If, as the literature supposes, better protection increases firm value, then being acquired by a firm from a country with better shareholder protection could lead to an improvement in the value of the target firm. For this reason, the potential improvement in shareholder protection coming from being owned by a firm from a country with a different legal system could be a source of value in a cross-border acquisition.

The first paper to explore this idea is Rossi and Volpin (2004), who gather a large, international sample of acquisitions and evaluate the extent to which corporate governance considerations are a motivation for them. The authors find that, both within countries

and across countries, corporate governance appears to be an important reason for acquisitions. Their main finding about cross-border acquisitions is that, holding other factors constant, such deals are more likely when the acquirer is from a country with better shareholder protection than the target country. This finding suggests that better protection is one potential source of value in cross-border deals.⁴

Bris and Cabolis (2008) extend this work and evaluate the extent to which improved governance appears to be a source of value in cross-border acquisitions. These authors rely on merger premiums as a measure of the value creation in any particular deal. Their main finding is that premiums are higher when corporate governance differences are higher. This pattern holds not only for country-level governance measures, mostly due to legal differences, but also for firm-specific measures of governance, focusing on the accounting standards of the firms. Subject to caveats about the selection of deals in their sample and the lack of data on changes in governance around the time of the acquisition, Bris and Cabolis interpret their findings as supportive of the view that governance is an important motive for cross-border mergers. In addition, Chari et al. (2010) document positive and statistically significant stock price reactions to acquisitions of firms in emerging markets with weaker investor protection by multinational firms from developed countries with stronger investor protection. Ahmad et al. (2022) show that cross-border mergers involve acquirers from more democratic countries than their targets.

Consistent with these findings, Ellis et al. (2017) study stock price reactions to over 37,000 cross-border acquisitions between 1990 and 2007. They show that acquirers' gains are higher when target firms are from countries with worse governance. The authors also find that no other acquirer country characteristics explain this effect.

Starks and Wei (2013) also study stock price reactions to cross-border mergers, and differentiate deals paid with stock as the method of payment. They find that the value gains to acquirer stockholders are increasing in the quality of corporate governance for stock offers, and that acquirers from countries with better corporate governance are more likely to make stock offers. The authors also find that premiums offered to the targets are decreasing in the quality of the acquirer's country-level governance. This result implies that acquirers compensate target shareholders when the merger creates exposure to weaker country-level corporate governance.

One way to identify the impact of country-specific corporate governance on cross-border acquisitions is to measure how changes in corporate governance regulations affect acquisition patterns. Kim and Lu (2013) use this approach to evaluate the extent to which corporate governance reforms in the acquirer's country affect the incidence of cross-border acquisitions. These authors find that, following reforms that improve the corporate governance in a country, firms from that country make more and higher-quality cross-border acquisitions. This supports the view that improvements in governance are a source of value in cross-border deals.

An important implication of the idea that better corporate governance from the acquirer country creates value in cross-border acquisitions is that corporate governance of the target improves following cross-border deals. Albuquerque et al. (2019) provide an empirical test of this hypothesis. This paper considers a firm-level sample of cross-border acquisitions from 64 countries between 2005 and 2014, and evaluates whether the governance in non-target firms in target countries improves after acquisitions. Albuquerque et al. focus on non-target instead of target firms because the latter are typically delisted. The

authors measure governance quality using an index based on 16 governance attributes drawn from Bloomberg's Environmental, Social, and Governance (ESG) database, and find that this index of governance does, in fact, increase following cross-border acquisitions. They also find that cross-border deals improve the investment and valuation of non-target firms in the same country of firms that are acquired.

While differences across countries in corporate governance-related regulations can lead to acquisitions that improve the governance in target firms, these differences can also deter potential value-improving combinations. Investors from one country are likely to avoid deals in which their legal rights are reduced, and potentially not recognized by a foreign court. For this reason, countries can agree to "Bilateral Investment Treaties" (BITs), which stipulate that countries treat foreign investors the same as home-country investors: they must not expropriate foreign-owned assets without appropriate compensation, and must litigate disputes through an independent arbitration body. A recent paper by Bhagwat et al. (2021) examines these treaties, and finds that they appear to facilitate cross-border acquisitions.

3.2 Other Regulatory Motives for Cross-Border Acquisitions

The idea that acquisitions allow firms to take advantage of other countries' regulations is known as "regulatory arbitrage" and it can be applied to other types of regulations than those affecting corporate governance. One industry where regulatory arbitrage is particularly important is banking. In most countries, banks are supervised and subject to a number of regulations (e.g., regulatory capital requirements, reserve and liquidity requirements) as well as restrictions on their non-banking activities, such as securities trading and underwriting. Importantly, the extent and stringency of these regulatory requirements for banks vary across countries, creating incentives for them to explore ways to move their funds to countries with weaker regulatory regimes (see Houston et al., 2012).

Karolyi and Taboada (2015) evaluate the extent to which regulatory arbitrage can explain cross-border banking mergers. Using a sample of over 7,000 domestic and 900 cross-border deals between 1995 and 2012, the authors examine whether banks from countries with strict regulations acquire from countries with weaker regulations. The authors find that acquiring banks are more likely to be from countries with stronger supervision, more stringent capital requirements, and more restrictions on banking activities. In addition, they show that these bank acquisitions are not value-destroying. In contrast, target and aggregate abnormal returns around deal announcements are positive and are larger in magnitude when acquiring banks are subject to more stringent regulation. Karolyi and Taboada interpret these findings as evidence of a benign regulatory capital arbitrage, with banks escaping from a costly regulatory environment.

Another potential set of regulations that could lead to cross-border mergers concerns labor practices. If a firm acquires a target in a country with lower labor regulations, it can potentially move some of its operations to the target firm and lower its labor costs. In this situation, reductions in labor costs could provide a motive for acquisition, especially if the same cost savings cannot be achieved through a contractual relationship between the firms. The advantage of an acquisition over a contractual relationship normally comes from relationship-specific investments, for which hold-up problems can prevent efficient contracting.⁵

Levine et al. (2020) provide empirical evidence suggesting that a country's lax labor regulations make firms in that country more attractive to potential acquirers. They find that when firms make acquisitions in countries with lower labor protection, they earn higher abnormal returns and have better post-deal performance gains. In addition, this relation is more pronounced among firms in labor-dependent industries, suggesting that weak labor regulation is an important factor in the post-merger labor restructuring and the realization of cost synergies. In contrast, Alimov (2015) argues that tighter labor market regulation could affect the likelihood of inbound cross-border acquisitions as it typically would lead to substantial labor force restructuring. Tighter labor protection could decrease firms' valuations, making them more attractive to acquirers. Consistent with this idea, Alimov finds that, following increases in labor protection, firms become more likely to be cross-border targets.

A type of regulation that has become increasingly common concerns climate change, with some countries adopting rules, for example, that limit CO₂ emissions by firms in that country. While these regulations may be socially desirable, they potentially make the country less attractive to foreign investors. Li et al. (2022) test this idea, and find that stronger climate regulations in a country indeed lower the incidence of cross-border acquisitions of that country's firms.

3.3 Protection of Intellectual Property

While regulatory arbitrage motivates cross-border acquisitions, there are several country-specific differences that deter deals. One potential impediment is that, whenever a firm operates outside its home country, its private information and intellectual property can be compromised. The protection of intellectual property is particularly important in industries where technology is important. The potential loss of intellectual property is a cost of making cross-border acquisitions, especially if it is necessary for the merged company to use technologies based on this intellectual property outside the home country.

Two papers evaluate whether a potential loss of intellectual property deters cross-border acquisitions. Hasan et al. (2017) examine whether better intellectual property protection facilitates cross-border technology mergers. They find that better intellectual property protection in a country does, in fact, lead to more cross-border technology mergers. They also find that premiums are higher when the target comes from a country with better intellectual property protection, suggesting that such protection makes companies more valuable to potential acquirers.

This finding is complemented by Alimov and Officer (2017), who do essentially the same test in first differences by considering how changes in intellectual property protection in a country lead to changes in the number of cross-border acquisitions of firms in that country. This increase is only in industries that the authors classify as "intellectual-capital intensive." The findings in these two papers strongly suggest that the protection of intellectual property rights is an important concern of potential acquirers in industries reliant on intellectual property.

3.4 Cultural Reasons

Cultural differences can be a hurdle that must be overcome when combining two firms from different countries. If the employees of one firm approach things in a very different fashion culturally from those of another, merging the two firms can be fraught with difficulties. A famous example of a merger that failed for cultural (and other) reasons is Daimler–Chrysler.⁶ The notion that mergers can face difficulties because of cultural issues is consistent with the economics literature that emphasizes the role of culture and trust in business relationships (see, e.g., Guiso et al., 2006). Consequently, it is possible that, when countries have very different cultures, firms from those countries are less likely to merge. This hypothesis is tested by Ahern et al. (2015) and Lawrence et al. (2021). Measuring culture using a variety of methods, these authors find that firms from culturally different countries are less likely to merge. For example, Ahern et al. use measures of the distance in “cultural” space along three dimensions commonly identified in sociology and economics: trust vs. distrust; hierarchy vs. egalitarianism; individualism vs. collectivism. They find that the greater the cultural distance along each of these dimensions, the smaller the volume of mergers.

However, unlike the Daimler–Chrysler case, when culturally distant firms do merge, Chakrabarti et al. (2009) find that those deals perform better than other deals. The likely explanation is that firms from countries with very different cultures are so reluctant to merge with one another that they do so only when the synergies are expected to be particularly large. In the relatively rare circumstances in which the synergies are large enough to overcome substantial cultural differences, they end up leading to unusually good performance for the combined firm.

3.5 Trade and Politics

In addition to cultural differences, a number of other factors can affect the desirability of combining two firms. Erel et al. (2012) find that the geographic distance and the amount of trade between two countries affect the likelihood that firms from those countries merge. Presumably, a greater distance impedes an efficient combination of two organizations. The trade between two countries probably reflects several factors that all affect cross-border mergers, including the quality of the relationship between the countries and the costs of making the actual trade, as well as cultural and geographic differences.

One component of trade costs, tariffs, can actually be a reason for making a cross-border acquisition. The international trade literature has emphasized that foreign direct investment (FDI), either through greenfield investments or acquisitions, can allow firms to bypass tariffs that countries impose on imports.⁷ This “tariff-jumping” argument suggests that, when tariffs are sufficiently high, firms will make cross-border acquisitions or greenfield investments to avoid paying them. For example, a major reason why Jushi, the Chinese fiberglass company, built a plant in South Carolina in 2019 was to avoid the tariffs being imposed at the time by President Trump.⁸ Hijzen et al. (2008) evaluate whether such tariff jumping motivates cross-border acquisitions by comparing horizontal and non-horizontal deals. These authors find that the impact of trade costs on deal volume is lower for horizontal deals, which they interpret as consistent with the tariff-jumping argument.

An important factor affecting the ease of doing business across countries is the extent to which the countries have good relations with one another. There are a variety of reasons why a company spanning two countries that do not get along can be difficult to manage, from personnel reasons to financial ones. To evaluate whether the quality of relations between two countries affects cross-border merger activity, Aleksanyan et al. (2021) consider whether state visits between countries affect the likelihood of deals between firms from those countries. Presumably, the existence of a state visit indicates that the two countries are on relatively good terms. The authors find that state visits between countries predict a higher number of cross-border acquisitions between firms from those countries, consistent with the idea that firms are more likely to merge if their countries have a good relationship with one another.

In addition to relations between countries, internal politics can influence whether firms from that country are targets in cross-border acquisitions. Often, the public does not like it when their country's firms are acquired by foreign companies. This is known as "economic nationalism," and is especially prevalent when the firms targeted by foreign acquirers are important to a country's economy or are thought to be symbolic of the country's wealth or power.⁹

Dinc and Erel (2013) evaluate the importance of economic nationalism in explaining cross-border acquisitions. The authors focus on acquisitions within the European Union (EU) between 1997 and 2006 because, under the EU treaty, the European Commission, rather than domestic governments, is the anti-trust regulator for large international mergers in all industries except defense and the media. Despite this treaty, Dinc and Erel find that, holding other factors constant, governments are more likely to support deals when the acquirer is from their own country, and are significantly more likely to oppose foreign bids. Moreover, this effect is larger when preferences for natives over foreigners in social, political, and economic domains are stronger. For example, economic nationalism increases with the vote share of extreme right-wing parties that advocate protectionist, anti-globalization economic policies, and it is larger against acquisition bids from countries with which the target country has little affinity. These findings thus support the economic nationalism interpretation.

Another way that politics can affect acquisition decisions is by creating uncertainty about government policies and how foreign companies will be treated. While, in general, firms do not like uncertainty about future government policies, such uncertainty is particularly problematic if it comes from a foreign government over which the firm has no influence. If concerns about future government policy in a particular country are sufficiently large, they can deter a firm from acquiring a target in that country. Cao et al. (2019) evaluate this idea, using national elections as an exogenous event that affects policy uncertainty. Their main finding is that, when a country is about to hold national elections, there are fewer acquisitions of firms from that country by foreign acquirers. This effect is particularly large when the host country has high expropriation risk. The paper provides support for the view that uncertainty about government actions is an important factor affecting cross-border acquisitions.

Bonaimé et al. (2018) also study regulatory and policy uncertainty, and find that acquiring firms are more likely to seek targets abroad when this uncertainty increases. The authors interpret this pattern through the risk-management channel. When the risk of a policy-related shock in domestic markets is high, firms partially hedge against

such shocks by acquiring firms from other countries that are less exposed to the policy in question.

3.6 Tax Havens

A number of countries have become known as “tax havens”—countries that attract capital with low tax rates, leading companies to use a variety of methods to move income to subsidiaries in these countries.¹⁰ To take advantage of these tax havens, however, a firm must have a subsidiary in a tax-haven country. The desire to acquire such subsidiaries is a potential motivating factor for cross-border acquisitions.

Meier and Smith (2020) measure the incidence of cross-border acquisitions that appear to be motivated by the creation of tax-haven subsidiaries. They compare the number of cross-border acquisitions of firms in tax-haven countries with the number predicted by a “gravity” model that is commonly used in the international economics literature. Using a sample of about 13,300 cross-border tax-haven acquisitions (with \$4.1 trillion in total deal value) from 1990 to 2017, Meier and Smith’s estimates suggest that these companies’ value is \$2.4 trillion more than it would have been without tax considerations. In addition, much of this activity, about \$1 trillion, involves companies based in small tax havens such as Bermuda or the Cayman Islands.

3.7 International Expansion of Specialized Firms

When a firm produces a unique, specialized product there can be demand for it internationally since there will be no foreign competitors producing the same product. To expand internationally, the firm will have to transfer specialized, often proprietary, assets overseas. Such assets tend to be intangible, such as trade secrets or the “know-how” to make a particular product. In addition, the firm will often have to contract with a foreign firm to market and distribute the product in a foreign country. However, because of hold-up problems, contracting specialized assets can be problematic (see Klein et al., 1978). Under such circumstances, it can be more efficient to merge the two firms than to rely on arm’s-length contracting to consummate the relationship.

Frésard et al. (2017) examine this idea, and suggest that one reason for cross-border acquisitions is the extension of the markets of specialized products. They consider a large sample of cross-border deals, and find that more specialized acquirers tend to purchase targets that are less specialized but in the same industry. Moreover, this effect appears to be larger when contracting inefficiencies and export costs limit potential arm’s-length contractual relationships. Overall, the findings are consistent with the view that specialized firms use cross-border acquisitions as a way of expanding internationally.

4 THE PROCESS OF ACQUIRING COMPANIES INTERNATIONALLY

To this point, we have focused our discussion on the reasons for cross-border acquisitions. While many of the sources of value in cross-border deals are the same as those for

domestic deals, there are a variety of potential motives for cross-border deals that are not relevant to domestic ones. Section 3 discussed a number of possible sources of value for cross-border acquisitions, as well as the academic literature that documents the extent to which it explains real-world transactions.

Regardless of the reasons, however, once a firm identifies a target in another country that it would like to acquire, international considerations can complicate the process of consummating the deal. Identifying the expected synergies associated with a potential target is more difficult when the firms being considered are in another country. Cross-border deals can face unfamiliar regulations as well as political opposition that can make government approval more difficult than in domestic deals. Consequently, institutions that facilitate acquisitions by reducing information asymmetries and finessing regulatory hurdles can help facilitate cross-border deals. Particularly important are institutional investors and venture capitalists.

4.1 Institutional Investors

Ferreira et al. (2010) evaluate the role of institutional investors in facilitating cross-border acquisitions, and outline several ways in which institutional investors can affect the process of acquiring firms in other countries. First, the presence of institutional investors tends to be associated with more concentrated ownership, which tends to make deals easier to complete by lowering free-rider problems between shareholders when responding to bids.¹¹ Second, institutional owners, especially those from the country of a potential bidder, can help minimize information asymmetries for a foreign acquirer. Third, Ferreira et al. suggest that foreign institutional investors will be more likely than domestic investors to accept value-increasing bids from foreign companies rather than favor domestic acquirers who offer lower premiums to shareholders.

Ferreira et al. (2010) also estimate the impact of foreign institutional ownership on cross-border acquisitions, and find that higher foreign institutional ownership increases the probability that the firm is acquired by a foreign company. Moreover, they directly link the acquisitions to ownership by institutions from the particular country where the bidder is located. The paper argues that this finding provides direct evidence of the facilitation role played by institutions when the nationality of the target shareholders coincides with the nationality of the bidders.

Ferreira et al. (2010) and Aggarwal et al. (2011) suggest that, in addition to facilitating cross-border acquisitions, foreign institutional owners can help improve corporate governance. These papers provide evidence that foreign institutional investors bring better governance practices from their home country to the countries in which they are investors.

Institutional investors also affect cross-border acquisitions in other ways. Chen et al. (2019) evaluate how different kinds of large blockholders affect cross-border deals. These authors argue that banks, because they continually solicit business, are sensitive to pressure from management and unlikely to monitor management. Mutual funds, in contrast, are not subject to such pressure, and are more likely to monitor management. Chen et al. perform several tests, the results of which are largely consistent with these hypotheses.

Governments or sovereign wealth funds also drive acquisitions around the world. To understand the role of governments and sovereign wealth funds in acquisitions, Karolyi

and Liao (2017) consider a sample of acquisitions by government-controlled acquirers between 1990 and 2008, with a total value of \$619 billion. They compare these deals with deals by corporate acquirers, and find that government-led acquisitions involve larger targets with greater growth opportunities. However, the targets of government-controlled acquirers tend to have more financial constraints. In addition, these deals are less sensitive to economic development and institutional differences between countries.

4.2 The Role of Private Equity

Private equity investors, who either make venture investments in new companies or private placements in existing ones, are likely to be particularly valuable in easing frictions associated with international borders. Private equity investors are almost always actively involved in management decisions, usually holding board seats and other control rights for which they negotiate at the time they make their investments. In addition, private equity investors are likely to be knowledgeable about potential cross-border acquisition targets, as well as any regulatory or political hurdles facing such deals.

Humphrey-Jenner et al. (2017) provide evidence on the role of private equity investors in facilitating cross-border acquisitions. These authors find that, when private equity-backed companies make cross-border acquisitions, the stock price reaction to the announcements is larger than for similar cross-border deals by firms that are not backed by a private equity company. This pattern is stronger when the target is in a “poor information environment” and when the private equity fund has more experience of doing deals in the target firm’s country. In addition, they find that private equity-backed acquirers improve the operating performance of cross-border targets when the target is classified as being in a poor information environment. These results are all consistent with the view that, when a private equity fund invests in a company, one of the ways in which they add value is by helping the company identify potential profitable cross-border acquisitions. The results therefore suggest that private equity investors can help facilitate cross-border acquisitions.

Another way in which private equity investors, especially venture capitalists, add value to their portfolio firms is by helping them innovate (see, for example, Kortum and Lerner, 2000; Bernstein et al., 2016; and Lerner and Nanda, 2022). Consequently, it seems likely that one source of value in cross-border acquisitions by venture-backed companies is the returns from the subsequent innovation by their targets.

An issue of concern with cross-border acquisitions and other foreign investments in innovative industries, however, is that innovations can sometimes be so important to the national interest that governments want them kept secret. Policymakers can be reluctant to allow foreign investors to own part of these companies. Foreign investment in innovative sectors, especially in those areas related to national security, has been somewhat controversial because of this possibility. Akcigit et al. (2020) model this idea formally. In their model, foreign investments allow U.S. companies to pursue technologies that they could not otherwise, but this investment comes at the cost of knowledge spillovers to the foreign investor’s home country. Cross-border investments are more likely to happen if the industries in the investor’s home country lag behind the same industries in the U.S. Akcigit et al. document that there are, in fact, such knowledge spillovers associated with investments in innovative industries. Consequently, there appears to be a role for

government restrictions on foreign ownership of innovative firms, either through regulatory barriers or taxes, which can affect the process of acquiring a company in another country.

5 VALUATION

Much research about cross-border mergers and acquisitions concerns valuation in one way or another. Share prices of acquirers or potential targets could affect acquisition decisions. A higher price, reducing its effective cost of capital, could make a firm more likely to be an acquirer (Shleifer and Vishny, 2003). Alternatively, a decrease in the share price of a potential target would make the firm “cheaper” if the price reduction is not justified by the firm’s fundamentals (Edmans et al., 2012). While valuation affects the desirability of cross-border deals, the deals also have consequences for firm valuations. A large body of literature documents a “diversification discount” for firms that have divisions in different industries. Whether there is such a diversification discount across countries is an interesting question that has implications for the overall efficiency of cross-border mergers and acquisitions. Finally, the largest collection of papers in the field of cross-border mergers and acquisitions has examined stock price reactions to the announcement of deals. The average abnormal stock price reaction to deal announcements indicates whether cross-border deals tend to increase or decrease the value of acquirers.

5.1 Do Price Levels Affect the Choice of Acquisition Targets?

One reason for acquiring a firm (or any other asset) is that its market price is lower than its true value. Alternatively, a potential acquirer’s valuation could affect its choice of acquisitions: holding cash flows constant, a higher share price means that the discount rate is lower, which would encourage firms to make acquisitions. Consequently, the aggregate level of equity prices in a country is a potential factor that could affect cross-border acquisitions both to and from that country.

In a cross-border context, there are country-level factors that affect the country’s stock market price and its exchange rates, as well as other factors that could potentially affect the pricing of potential acquisition targets. Baker et al. (2009) evaluate this argument using foreign direct investment, the majority of which occurs through cross-border acquisitions. The authors find that FDI flows are positively related to the market-to-book ratio in the source country (i.e., where the money comes from) but not the host country (where the money goes to). They conclude that the higher prices in source countries are associated with a lower cost of capital, which drives the increase in FDI.

Erel et al. (2012) consider whether recent movements in stock market valuations and exchange rates are associated with the incidence of cross-border mergers. They find that cross-border mergers are more likely following increases in the acquirer country’s stock market valuation relative to the target country’s, and also when the acquirer’s home currency has appreciated relative to the target’s home currency. This pattern is consistent with mispricing being a determinant of deals, with acquirers being overvalued relative to targets. In addition, it is also consistent with acquirers applying lower discount rates when

evaluating potential deals when they are in a country with a high stock price and a currency that has recently appreciated.

A related issue concerns the relative pricing of cross-border and domestic deals. Does crossing a border to make an acquisition lead to a higher price than a purchase of a similar domestic firm? A recent paper by Hammer et al. (2021) says that the answer is “yes.” Using a large sample of private equity buyouts, these authors find that cross-border buyouts are associated with higher valuation multiples, which they attribute to informational disadvantages of foreign buyers – although higher competition for cross-border deals could also potentially explain part of their finding.

5.2 Diversification Discounts

An empirical regularity in the corporate finance literature that is commonly attributed to inefficient acquisitions is known as the “diversification discount” (see Lang and Stulz, 1994; Berger and Ofek, 1995). This refers to the phenomenon whereby firms that are diversified across industries are worth less than comparable firms that focus on a single industry. The most common interpretation of this finding is that diversifying acquisitions are value-destroying – although this interpretation has been disputed by some authors (see Campa and Kedia, 2002).

Denis et al. (2002) provide an interesting study that considers the possibility of a similar pattern occurring across countries. These authors compare the valuation multiples of firms that are diversified internationally with comparable domestic firms, and find that diversified firms trade at lower multiples than domestic firms. Their findings are consistent with the view that cross-border mergers are, on average, inefficient and that the costs of doing them outweigh the benefits. This is an intriguing hypothesis and worthy of future study.¹²

5.3 Stock Price Reactions to Announcements of Cross-Border Acquisitions

By far the largest strand of research about cross-border acquisitions has examined the stock price reaction to their announcements. Under the efficient markets hypothesis, the change in stock price at the time of the announcement should reflect the market’s expectation of the change in the present value of the firm’s cash flows brought on by the acquisition. Consequently, event studies, which calculate the risk-adjusted abnormal return around the time of the acquisition announcement, have become a standard way to evaluate the quality of acquisitions, both domestic and cross-border.

There is an extensive literature analyzing acquirers’ abnormal returns for domestic mergers. The stylized fact, which has been well known since early surveys by Jensen and Ruback (1983) and Jarrell et al. (1988), is that, on average, acquirers have a small negative return. However, most studies documenting this finding are based on acquisitions of large, publicly traded U.S. companies. Acquisitions of smaller and private companies tend to be associated with positive acquirer returns (see Netter et al., 2010; Mulherin et al., 2017). Most likely, acquisitions of large, publicly traded companies generate more competing bids than smaller private ones, driving up acquisition prices.

Table 9.4 summarizes the findings of several event studies that examine acquirer returns in cross-border acquisitions, as well as other interesting findings from each paper.

Table 9.4 Summary of event studies on cross-border acquisitions

Paper	Sample	Acquirer's Return	Effect on Targets	Other
Doukas and Travlos (1988)	301 M&As with U.S. acquirers. Range: 1975–1983 Source: public announcements	Abnormal return for acquirers is zero; U.S. multinationals not operating in the target firm's country experience daily abnormal return of 0.31% on announcement day		
Doukas (1995)	463 M&As of U.S. bidding firms engaged in international acquisitions Range: 1975–1989 Source: Mergers and Acquisitions, Dow Jones Retrieval Service database	CAR (–1,0) of US bidders with high Tobin's Q = 0.41%, with low Tobin's Q = –0.18%		Bidder returns inversely related to free cash flow for low Q bidders, but not for high Q bidders
Eckbo and Thorburn (2000)	1846 acquisitions with Canadian target firms and domestic and US bidders: 1261/1846 bidders are from TSE and 390/1846 from NYSE Range: 1964–1982 Source: Merger Register of the Canadian Department of Consumer and Corporate Affairs	Average monthly abnormal return for TSE acquirers: 3.64% during [t–12, t], and 1.27% in the announcement month US bidders: abnormal return is zero	Average monthly abnormal return for TSE targets: 11.40% during [t–12, t] and 3.59% in the announcement month	
Kiymaz (2004)	355 US targets and 391 US bidders involved in international M&As of financial institutions Range: 1989–1999 Source: Mergers and Acquisitions	For US bidders single-factor CAR (–1,1) = 0.38%, significant at 10% level	For US targets single-factor CAR (–1,1) = 3.41%, significant at 1% level	Determinants of wealth gains: foreign and US economic conditions; level of economic development of target country; exchange rate volatility; effectiveness of the foreign government; relative size of participants, and control of the target

Table 9.4 (continued)

Paper	Sample	Acquirer's Return	Effect on Targets	Other
Moeller and Schlingemann (2005)	4,430 M&As of US public firms that acquire either the equity or assets of domestic or foreign companies; 4047 domestic and 383 cross-border Range: 1985–1995 Source: SDC Platinum	CAR (–1, 1) for cross-border acquirers = 0.31%, for domestic = 1.17%		
Francis et al. (2008)	9,109 M&As with US firm as the acquirer Range: 1990–2003 Source: SDC Platinum	CAR (–1, 1) for cross-border US acquirer = 0.96%, for domestic US acquirer = 1.49%, with difference being significant		Firms acquiring segmented-market targets (rather than integrated) experience higher abnormal returns Acquirer's CAR (–1, 1) for cross-border with segmented-market target = 1.31%, integrated = 0.90%
Bhagat et al. (2011)	698 cross-border M&As by firms from emerging countries: Brazil, China, India, Malaysia, Mexico, Philippines, Russia, South Africa Range: 1991–2008 Source: SDC Platinum	CAR (–1, 1) for acquirer = 1.72%		Acquirer return is higher for target countries with better governance

The samples in each paper differ greatly. For example, Doukas and Travlos (1988) and Doukas (1995) consider samples of U.S. acquirers; Bhagat et al. (2011) rely on a sample in which the acquirers are from emerging markets; Eckbo and Thorburn (2000) sample Canadian targets; and Kiyamaz (2004) only includes acquisitions made by financial institutions. Nonetheless, in each study, the abnormal return to acquirers is positive and statistically significant.

The positive acquirer returns for cross-border deals suggest that these deals add value to acquirers. Most of the studies in Table 9.4 do not report returns of targets, presumably because the majority of cross-border targets are private.¹³ The positive acquirer returns are similar to those reported for domestic acquisitions of private firms. This result suggests that cross-border deals tend to be negotiated rather than auctioned, with some of the rents created by them captured by acquirers.

6 CONCLUSION

Roughly one-third of all acquisitions are of firms from different countries than their new parents. While some of these acquisitions occur for the same reasons as domestic ones, there are also several international factors that can provide motives for cross-border deals. This chapter summarized the academic literature on cross-border mergers and acquisitions, focusing on the reasons for them that do not also explain domestic deals.

Many of the papers we discuss propose cross-country factors that could potentially lead cross-border mergers to increase, or possibly decrease, the values of two firms in different countries if they are combined into one. Consequently, these factors can serve as motives or deterrents to cross-border deals.

Many papers focus on the idea that a target can benefit from an acquirer from a country with better legal shareholder protection, which would enhance value through improved corporate governance. In addition, cross-border acquisitions can be motivated by “regulatory arbitrage,” where the acquirer takes advantage of weaker regulations in the target country (e.g., regarding banking, labor, or the environment). Firms can also facilitate tax avoidance by acquiring firms in tax havens and improving their distribution systems by acquiring a downstream firm in a country in which they want to sell their goods. The literature has evaluated these ideas and found evidence consistent with them.

On the other hand, a technology firm might think twice about acquiring a firm in a country that does not protect intellectual property well, for fear of losing valuable secrets. A firm considered a national treasure can run into “economic nationalism” and become difficult to sell to a firm from another country. Trade and cultural factors work both ways: if countries get along well and/or have similar cultures, then cross-border deals become more likely between the two countries. In contrast, if the countries have tense relationships or are culturally different, cross-border acquisitions become less likely. The literature has also examined these ideas and found empirical support for them.

Relative to domestic deals, cross-border acquisitions can be more difficult to consummate for a variety of reasons, including information asymmetries and regulation. The literature has examined factors that can ease these barriers. It turns out that large shareholders, especially private equity investors, can play a valuable role in this process.

Valuation does influence cross-border acquisitions and can make deals either more or less attractive. When valuations are high in a country, either through exchange rate movements or changes in stock prices, those countries' firms are less likely to be bought. In contrast, when valuations are low, a country's firms become targets more often. Valuations affect the likelihood of being acquirers in the opposite way from targets: the likelihood of a firm being an acquirer increases in its country's market valuation relative to other countries' valuation.

Cross-border deals do appear to create value on average. Many papers have documented a small increase in stock prices for public acquirers in cross-border acquisitions and a larger increase for targets. Our own empirical analysis based on the largest, most up-to-date sample confirms these findings.

In recent years, many mergers and acquisitions combine firms from different countries. These deals are potentially affected by many factors that are not relevant to domestic deals. This chapter has surveyed the literature documenting the impact of these factors on cross-border mergers and acquisitions. As the world becomes more integrated and cross-border mergers and acquisitions more prevalent, these factors are likely to become increasingly important in the future.

NOTES

1. See also an older survey study, Shimizu et al. (2004), and its follow-up by Wiedemann and zu Knyphausen-Aufseß (2022).
2. In addition, we exclude leveraged buyouts (LBOs), spin-offs, recapitalizations, self-tender offers, exchange offers, and repurchases. In Panel B, the statistics are based on deals with transaction values available from the SDC.
3. See Netter et al. (2011) and Erel et al. (2012) for more on this point.
4. The finding is also consistent with the very interesting idea proposed by Coffee (1998) – that market forces will lead to convergence across countries in corporate governance standards. For more discussion and evidence on this point, see Stulz (1999), Reese and Weisbach (2002), Doidge et al. (2004), and Benos and Weisbach (2004).
5. This idea was originated by Klein et al. (1978) and further developed by the “Grossman/Hart/Moore” literature, which is summarized in Hart (1995). A recent empirical test of this idea is provided by Bena et al. (2021).
6. See “Why Daimler Chrysler Never Got Into Gear,” Michael Watkins, *Harvard Business Review*, May 18, 2007.
7. See the discussion in Hijzen et al. (2008) for references to this literature.
8. See Lerner et al. (2019).
9. Economic nationalism has a long history in economics, dating at least to Feiler (1935).
10. For detail on tax havens and the way they operate, see Desai et al. (2006) and Dharmapala and Hines (2009).
11. Shleifer and Vishny (1986) provide a classic analysis of how concentrated ownership can lead to takeovers.
12. A related issue concerns the diversification of the advisors. Rajamani et al. (2016) provide an interesting study suggesting that internationally diversified advisors actually give their clients worse advice, leading to lower announcement returns.
13. Two exceptions are Eckbo and Thorburn (2000) and Kiymaz (2004), both of which report positive returns to targets

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