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Domestic versus cross-border acquisitions: which impact on the target firms' performance?

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Abstract

This article investigates the effects of horizontal acquisitions on the performance of target firms in the 1990s. Using French manufacturing firm-level data, we examine two main indicators of performance: the profit and the productive efficiency. We distinguish domestic from cross-border acquisitions. To evaluate the impact of take-overs, we implement appropriate difference-in-difference estimation techniques associated to a matching propensity score procedure. We find that Mergers & Acquisitions (M&A) do not increase the profit of French target firms, even on the long run. However, they clearly raise the productivity of target firms. These results suggest that firms probably redistribute efficiency gains at the upstream and/or downstream production stage. There is no evidence of an increase in market power. In addition, the consequences of domestic and cross-border M&A significantly differ. Efficiency gains are stronger for

cross-border M&A. This conclusion is however true only for extra-European Union operations. The achievement in the European economic integration certainly explains the absence of difference between European and domestic acquisitions. Finally, our results cast some doubt on the frequent discrimination attitude towards foreign takeovers and the fears of their impact on firms' performance and the host country's welfare.

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Notes

[1] An abundant literature in finance explored the impact of M&A on shareholders' wealth using event studies (see Meschi (1997), Andrade et al. (2001) or Pautler (2003)). It converges to say that M&A improve the combined value of buyer and target firms. However, target shareholders take profit from M&A while buyers just break even. In contrast, the cited literature in the remainder of the article is based on accounting data.

[2] See Caves (1989) for a survey.

[3] The productivity indicator can be measured for each single input or for all inputs simultaneously. Although the TFP is the best way of estimating efficiency performance, labour productivity is frequently examined because of data constraint.

[4] Some studies analysed the effects of M&A on companies' market shares. Mueller (1985) or Baldwin and Gorecki (1990) found declines in market shares. Goldberg (1973), McDougall and Round (1986), Jenny and Weber (1980) or Cable et al. (1980) came to no significant variation in market shares.

[5] Healy et al. (1992) or for example Cosh et al. (1980) also got the result of a positive impact respectively in the US and the UK market. Empirical evidence for other countries arrives to mixed conclusions too. For instance, merging firms' profits increased in Canada (Baldwin, 1995) and Japan (Ikeda and Doi, 1983), but decreased in Holland (Peer, 1980) and Sweden (Ryden and Edberg, 1980).

[6] A Greenfield Investment is defined as the establishment of a new production facility in contrast to a cross-border M&A where a firm purchases shares of an existing foreign firm.

[7] For instance, in the UK market, Davies and Lyons (1991), Driffield (1977), Girma et al. (2000) or Griffith and Simpson (2001) confirmed the productivity superiority of foreign-owned firms. The MNE's profit is more seldom examined. For France, Houdebine and Topiol-Bensaïd (1999) pointed out that MNE's profits were higher.

[8] Citations are not claimed to be exhaustive, many of works on this subject being not published yet, and some of them focusing on very specific sectors, such as pharmaceutical or banking industry.

[9] In a related paper, Girma and Görg (2003) evaluated the impact on the survival prospects of UK target firms. Take-overs decreased their lifetime in both electronics and food sectors.

[10] Event studies also explored the consequences of cross-border M&A. Harris and Ravenscraft (1991) or Swenson (1993) underlined that US target firms' shareholders benefited more from a foreign M&A than a domestic operation. Markides and Ittner (1994) focused on US outward cross-border M&A. Cross-border operations were on average welfare-improving for the US buyers.

[11] The first four M&A wave were mainly confined to the United States and Great Britain. The fifth and last M&A wave encompassed all major industrial countries.

[12] We define inward cross-border M&A as the sales of domestic firms to foreign investors. In the opposite, outward cross-border M&A correspond to the purchases of foreign firms by domestic firms.

[13] This list includes ten French industries, varying from biotechnologies, secure information systems, casinos to the production of vaccines.

[14] In the past, two major waves of M&A took place in France, the first one happening in the 1960s and the 1970s, the second one in the middle of the 1980s (Derhy, 1999).

[15] Horizontal M&A are defined as operations between firms within the same industry.

[16] The spatial economics literature examines the relationship between M&A, market power and local competition (Levy and Reitzes, 1992, 1995).

[17] A firm fearing retaliation in one market (i.e. a price war) is incited to moderate its pricing behaviour in another market (Bernheim and Whinston, 1990).

[18] Empirical works are more ambiguous (Conyon et al., 2002).

[19] Since the economic context shapes the firms' innovation capabilities, the heterogeneity of merging firms may reflect country disparities.

[20] Capron and Mitchell (1998) define resource redeployment as the use by the buyer or the target firm of the other firm's resources.

[21] These data provide information on worldwide markets from publicly announced M&A. They comprise all transactions valued at US $1 million or more. In order to construct this database, different sources are used, such as stock exchange commissions, trade publications, law firms, surveys of investment banks, etc.

[22] Cross-border acquisitions strongly predominated over mergers in the 1990s (UNCTAD, 2000). Mergers represented less than 3% of M&A (in number). Most of them, specially cross-border acquisitions, consisted in friendly operations. Only less than 5% in value (and 0.2% in number) of completed cross-border M&A were hostile.

[23] It collects each year accounting information on the inputs and outputs of individual firms. This dataset includes all French manufacturing firms of more than 20 employees.

See Table A1 in Appendix A2 for more descriptive statistics.

[24] See Van Biesebroeck (2003) for a discussion of the different ways to estimate productivity.

[25] As explained later, a newly acquired firm i is associated with a nontarget firm within the same year t.

[26] The matching method is a nonparametric method. No particular specification is assumed.

[27] We use the ‘caliper’ matching method to select the control firm.

[28] The matching is performed in Stata Version 8 implementing the software provided by Sianesi (2001).

[29] We use the French industry classification NAF16.

[30] We checked that there is neither a too high statistic correlation, nor multi-collinearity among selected variables.

[31] For each independent variable, the difference between target and control firms is checked, employing T-test on the differences within bands of the propensity score.

[32] The bias could be defined as the difference of the sample mean in the treated and nontreated sub-samples divided by the square root of the average of the sample variances in the treated and nontreated groups.

[33] This nonsignificance may come from a size effect. Large firms with lower profits could be more likely to be acquired. By buying out a large firm, a company increases more quickly its business activity, taking profit from economies of scale and scope: it is precisely an advantage of external growth strategies over those of internal growth.

[34] However, such a view has been mitigated by Ravenscraft and Scherer (1989) or Jensen (1986). M&A are an ambivalent phenomenon. They sometimes reflect managers’ power. In addition, investors could be incited to take over high-performing firms in order to benefit from their technological and managerial knowledge.

[35] Conyon et al. (2002) and Piscitello and Rabbiosi (2003) only take into account changes in labour productivity.

[36] Our results partly differ, for instance, from Conyon et al. (2002). They did not find any significant increase in productivity for domestic M&A.

[37] The difference between domestic and European M&A is not significant even at a threshold of 10%.

[38] The inclusion of firm dummies makes the interactive variable not significant for domestic operations. However, the consequences of foreign operations still remain positive and significant, confirming a higher efficiency for cross-border M&A, especially nonEuropean M&A.

[39] The interactive variable could be significant in 3, but not in 2, 4 or 5. This change is then not really conclusive, all the more as the significance is not robust to a modification in estimations. More generally, we have to interpret it with caution since our sample is reduced with a narrower timing window.

[40] Theoretically, three main parameters determine the extent to which efficiency gains reduce consumers' prices: the intensity of competition after merging, the characteristics of the demand function and the production cost.

[41] See Caves (1996) for an overview on this question.

[42] They could modify the prices assigned to internal transactions, by under-pricing exports and over-pricing imports.

[43] All indexes (source: INSEE) are calculated at a sector-level (base 100 in 1995).