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A STUDY ON OUTBOUND CROSS-BORDER M&AS OF EUROPEAN FIRMS TARGETS BY CHINESE AND INDIAN FIRMS

ABSTRACT

The Chinese and Indian automobile industries have shown tremendous growth during the last decade. Globalization has led to a relocation of production activities and new regions have become significant sites for international competitiveness. The rise of the Chinese and Indian automobile industries cannot be understood independently of the global geographical shifts in the automobile industry and changing roles of governments, and this can be seen as one of the most significant aspects of China and India's modernization. More than 300 cross borders M&A deals European targets of Chinese, Indian and European acquirers during the periods 200 to 2015 have been examined for this study. This study measure how Indian and Chinese companies' acquisitions of European targets perform in comparison to intra-European deals. Moreover, I investigate which factors influence the value creation of these deals for acquiring company shareholders. Conducting this research study, it finds that all geographical sub-samples show significant positive cumulative abnormal returns (CARs). Furthermore, it also finds that intra-European automotive merger & acquisition deals develop more value for acquirers than ones involving Indian and Chinese bidders. Chinese acquirers could benefit from positive spillover effects generated by targets residing in countries that have strong legal protection of outside investors.

KEYWORDS : Automobile, India, china, CAR, European, M&A

INTRODUCTION

The Chinese and Indian automobile industries have shown tremendous growth during the last decade. Globalization has led to a relocation of production activities and new regions have become significant sites for international competitiveness. The rise of the Chinese and Indian automobile industries cannot be understood independently of the global geographical shifts in the automobile industry and changing roles of governments, and this can be seen as one of the most significant aspects of China and India's modernization.

The most dramatic shift in the global automobile industry is the sharp growth of newly industrializing countries in production and sales, notably China, India, and Brazil. The triadic structure of the automobile industry is now changing. The automobile industry has been under pressure since the financial crisis in 2008. The pressures requiring changes within the industry, such as stringent emission and safety regulation and increasing requirements for quality management standards, accompanied by severe cost competition has inevitably led to the massive restructuring of the automobile industry worldwide. The changes in manufacturing architecture, based on tier-layered and increasingly modularized production, have also affected the global geography of automobile production. In automobile manufacturing, China has emerged as the fastest-growing producer, surpassing Germany in 2006, the United States in 2008 and Japan in 2009, China produced 19.31

million in 2012 (22.80% of total world production). India has also emerged as a large producer, and production reached 4.14 million (4.90% of the total world production) in 2012. Together, these two account for roughly 27.7% of the total. Against that, the figure for the United States and Japan, which accounted for more than 40% of world production in 1997, fell to 23.98% in 2012. At the same time, China and India are also the fastest-growing markets for vehicles. China's domestic sales reached 19.30 million units in 2012, making it for two consecutive years the largest car market in the world. Sales of automobiles in India have also risen to 3.58 million in 2012, making it the sixth largest market in the world.

The domestic and foreign producers which are able to provide the market with products meeting the demand do renew and expand the range of their production. Entry mode matters for foreign producers, which can arbitrate either for JV and M&A or building directly new facilities (greenfield investments) directly assembling car with local content or following fully or partially knock own strategies. This depends on the nature of property rights and institutional measures. Domestic and foreign suppliers, in this particular industry, play an important role both in the value and the quality chain. The industry, in mature market economies, is particularly externalized; outsourcing is important and parts makers are essential partners (both in line production as in design and development). Final assemblers have to set up a reliable network of suppliers able to supply firms just in time with quality and low cost products. This explains the massive presence, in the Chinese and now Indian markets and assembling chains, of US, European and Asian (South Korea, Japan) sub-contractors.

SIGNIFICANCE OF THE STUDY

This research study helps companies who are interested in M&A in area of technology transfer knowledge, experienced technical work force, obtain new market, to sustain in competitive arena, introducing new products, reduced less risk factor in term of failure in most of the cases

Research paper will also help Investor to see how such deals affected share market based on such deals and future of the company. Economist will also benefited based on our research to examine economy condition of country after such big M&A. In education field MBA schools, Management Institutions this research will help to modify their course modules and if applicable can add new chapters based on corporate governance, technology transfer, shareholder issues, Economy, Government policy etc.

This study will also be useful to analyze the general impact of FDI on host economies. This paper will hypothesize that overall cross-border M&A deals have a positive impact on host economies. This perspective will have two positive effects towards investment liberalization and facilitation among the APEC member economies. First, it will enable member economies to expedite cooperative policies related to M&A deals through lowered barriers. Second, it will help evoke favorable responses towards M&A deals from the general public of member economies, lowering the emotional entry barriers to member economies' markets.

RESEARCH OBJECTIVE

1. To study how cross border M&A deals impacted by Economy, Culture difference.
2. To investigate do intra-European automotive deals create more value for acquirers than ones involving Chinese or Indian bidders?

LITERATURE REVIEW

Operating synergies refer either to revenue-enhancements or cost-reductions (Gaughan, 2002). Revenue enhancing operating synergies are harder to achieve than cost reductions since they are not immediately identifiable and are defined as "newly created or strengthened product or service that is formulated by the fusion of two distinct attributes of the merger partners and which generates immediate and/or long-term revenue growth" (Berk & DeMarzo, 2007, p. 877). The potential reasons for revenue growth can be considered deal-dependent and vary from being a result of an extended product line, which enables each firm to sell more to their customer base, to deriving from cross-marketing of the individual products or services from the respective partner. Another reason might be the combination of two favorable factors. For instance, one firm has products with high market potential and merges with another company that has a highly developed distribution network but no special product (Gaughan, 2002).

Transaction cost theory relates mainly to M&A on a vertical level and involves a target in the same industry that is either closer to the source of supply, or to the end consumer (Brealey et al.). Vertical M&A can be split into forward- and backward integration. Forward integration describes the merger with a purchaser, whereas backward integration is the merger with a supplier (Picot & Franck, 1993, p. 180). When separate units have business relationships, different types of transaction costs occur, and their magnitude is unclear (Picot, 1982).

If the independent contractual party is acquired and the long-term conditions for the source of supply or demand are fixed, transaction costs are reduced since the uncertainty factor and coordination effort is eliminated (Brealey et al., 2008; Gaughan, 2002). Depending on the type of relationship, transaction costs can account for a significant amount, particularly if the underlying good is specialized, technologically advanced and requires a customized production flow. In this case, price discovery can cause problems since no market with comparable products is available. In addition, the purchaser is highly depended on the supplier since he cannot easily switch to other firms. Dependability on the supplier is an important factor since it ensures quality and timely delivery for just-in-time management (Gaughan, 2002). Quality control is a major benefit of vertical integration. If correctly implemented, technologically advanced products can be produced at significantly cheaper cost (Reed et al., 2007, p. 19). An external firm that manufactures specialized products might require long-term contracts and a fixed compensation for the initial costs (Gaughan, 2002). For the supplier, this bears opportunities and risks at the same time. On the one hand, he faces the risk of high dependency towards one major client, on the other hand he sets high entrance barriers for potential competitors. For the customer, high dependency towards the supplier's Research & Developments (R&D) capabilities, resource management and long-term business interest exist (McIvor et al., 1998, p. 87; Mentz, 2005).

METHODOLOGIES FOR VALUE CREATION ANALYSIS

The most widely spread and generally accepted theoretical framework used to value companies is the discounted cash flow method (DCF). It assumes that the value to an owner is constituted by the cash flows that she can expect to receive during the period of possession.

Value implications of particular investments, in our case corporate takeovers, can hence theoretically be assessed by looking at the incremental effect of a particular investment, i.e. the "incremental cash flows"

(Bild, 1998) of each investment separated from a stand-alone case of the parent company. These cash flows are discounted by an appropriate rate, taking into account the time value of money and riskiness of the cash flows. A merit of the incremental approach often mentioned is that it is applicable ex-ante as well as ex-post and can thus be used to compare target and actual performance of investments and takeovers. In the corporate takeover literature, the theoretical approach to corporate valuation is hence described as the ideal research method.

However, there are limitations to this theoretically sound approach. Problems for instance arise when incremental cash flows from a particular takeover cannot be separated from cash flows arising from other parts of a business. I believe that a good example of separation issues can be found in situations in which synergies are evaluated. Synergies are not always mutually exclusive, i.e. they arise in different levels of organizational entities, and are hence hard to allocate to different investment decisions.

SAMPLE SIZE

For this study 167 M&A deals in automotive sector by Indian and Chinese acquirers targeted to European companies during the period 2000 to 2015 have been included, furthermore I have also included 166 non-automotive M&A deals of European companies' targets from Indian and Chinese acquirers during the period 2000 to 2015.

DATA ANALYSIS

Comparison of CARs for different (sub-)samples										
Event Window		Findings1	**1. China, India & Europe All**		**2. China & India All**		**3. China All**		**4. India All**	
			CAR	t-statistic	CAR	t-statistic	CAR	t-statistic	CAR	t-statistic
(-1, 0)	ALL SECTORS	1. & 2: China & India All > Total Sample > 0	0.87%	4,12***	1.17%	4.01***	0.86%	2,08**	1.45%	3.48***
		3. & 4: India All > China All > 0								
(-1, +1)		1. & 2: China & India All > Total Sample > 0	1.11%	4,35***	1.47%	4.16***	1.53%	2,05**	1.94%	3.71***
		3. & 4: India All > China All > 0								
(-5, +5)		1. & 2: Total Sample > China & India All > 0	1.05%	2,42**	0.79%	1.27	0.49%	0.55	1.02%	1.19
(-10, +10)		Not Significant	0.56%	0.96	0.06%	0.07	0.20%	0.18	-0.04%	-0.04
(-20, +20)		Not Significant	0.98%	1.2	0.31%	0.28	0.96%	0.56	-0.16%	-0.11
			5. Europe Automotive		**6. China & India Automotive**		**7. China Automotive**		**8. India Automotive**	
			CAR	t-statistic	CAR	t-statistic	CAR	t-statistic	CAR	t-statistic
(-1, 0)	AUTOMOTIVE	Not Significant	0.32%	1.2	0.70%	0.87	1.73%	1.13	0.14%	0.15
(-1, +1)		Not Significant	0.60%	1.67	0.73%	0.88	3.28%	1.45	-0.25%	-0.28
(-5, +5)		5. & 6. Europe Automotive > China & India Automotive	1.35%	2.45**	0.33%	0.27	4.78%	1.46	-1.38%	-0.99
(-10, +10)		Not Significant	1.28%	1.61	-0.85%	-0.62	1.03%	0.29	-1.60%	-1.33

(-20, +20)		Not Significant	1.94%	1.68*	1.29%	0.51	0.48%	0.11	1.81%	0.56

			9. China & India Automotive		10. China & India Non-Automotive		11. China - Non-Automotive		12. India Non-Automotive	
			CAR	t-statistic	CAR	t-statistic	CAR	t-statistic	CAR	t-statistic
(-1, 0)	AUTOMOTIVE / NON-AUTOMOTIVE	9. & 10: China & India Non-Automotive > China & India Automotive 11. & 12: India Non-Automotive > China Non-Automotive	0.70%	0.87	1.36%	4.17***	0.90%	2.01**	1.77%	3.75***
(-1, +1)		11. & 12: India Non-Automotive > China Non-Automotive , 8. & 12: India Non-Automotive > India Automotive	0.73%	0.88	1.69%	4.27***	0.90%	1.76*	2.44%	4.05***
(-5, +5)		Not Significant	0.33%	0.27	1.00%	1.42	0.34%	0.34	1.69%	1.64
(-10, +10)		Not Significant	-0.85%	-0.62	0.20%	0.22	0.08%	0.07	0.27%	0.2
(-20, +20)		Not Significant	1.29%	0.51	0.20%	0.16	1.06%	0.57	-0.44%	-0.26

CONCLUSION

The joint sample of Chinese and Indian cross-border acquisitions in Europe shows highly significant positive CARs shortly after the announcement date. The combined Chinese and Indian automotive sample's CARs are partly negative and insignificant. Comparing separately the Chinese and Indian deals, the Chinese CARs are higher in all periods, however not statistically significant. Furthermore, Chinese CARs are always positive and Indian CARs are mostly negative. Non-automotive deals have higher CARs than automotive deals in India. Indian non-automotive deals have higher CARs than Indian automotive deals. European automotive deals have higher CARs than both the combined Chinese and Indian automotive deals and country specific ones.

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Dr. Gurudutta P. Japee
HOD, Accountancy Department
Shree K.K. Shashtri Government Commerce College,
Ahmedabad.