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# Why Half of China's Overseas Acquisitions Could Not Be Completed

Jianhong Zhang and Haico Ebbers

**Abstract:** About half of China's overseas acquisition attempts have not been completed; the chance of success is much lower than worldwide. This study provides an overview of China's overseas acquisition, and investigates the reasons behind the low likelihood that an acquisition deal is completed. By using a sample that consists of 1,324 overseas acquisition attempts by Chinese firms, the study found that multi-level determinants influence the outcome of China's overseas acquisitions. Based on the findings, we conclude that the distinctive social and economic environment of acquirers; ownership and low competitiveness of these acquirers; lack of global experience; and sensitiveness of the industry all hamper Chinese acquisition deals.

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**Keywords:** China, overseas acquisition, deal completion, institutions, ownership

**Dr. Jianhong Zhang** earned her Ph.D. in international economics at the University of Groningen. She works at Nyenrode Business University in the Netherlands, and Yunnan University of Finance and Economics in China. Her research interests are international trade and business and regional development. She is actively involved in researching China's integration into the world economy.

E-mail: <j.zhang@nyenrode.nl>

**Prof. Dr. Haico Ebbers** is professor of international economics at Nyenrode Business University in the Netherlands. He is chairman of the Europe China Institute at Nyenrode and co-programme director of the international MBA. Besides his work at Nyenrode, he is guest professor at various national and international universities, including some top universities in China. He teaches globalization and economics. In his latest publications he has focused on China's integration in the world economy and the impact on international operating companies.

E-mail: <h.ebbers@nyenrode.nl>

## Introduction

China has integrated into the world economy very quickly since 1978, when economic reform started.<sup>1</sup> It emerged in the world market first as an exporter and foreign direct investment (FDI) recipient, then as an investor as well, and in recent years it has also acted as an acquirer. In response to these trends, studies on “China goes global” first focused on the global trade flows and comparative advantage as a manufacturing location (e.g. Lardy 2001; Zhang and Song 2000; Chun 2003). Since the start of the 21<sup>st</sup> century, the rise of Chinese direct outward investment has been increasingly investigated with a focus on motivation, determinants and strategy (e.g. Deng 2004, 2007, 2009; Buckley et al. 2007; Morck, Yeung, and Zhao 2008; Yamakawa, Peng, and Deeds 2008). In recent years, it has become obvious that an increasing number of Chinese firms are engaged in overseas acquisition. The completed and uncompleted foreign acquisitions by Chinese, such as MinMetals, CNOOC, Haier, Lenovo, TCL and Nanjing have grabbed headlines. However, the understanding of cross-border acquisitions by Chinese firms remains incomplete. In particular, it is not clear why many of China’s overseas acquisitions could not be completed. This paper aims to answer this question by investigating the factors that influence the outcome of China’s overseas acquisition attempts.

In June 2005, China National Offshore Oil Corp (CNOOC) proposed to acquire all outstanding shares of Unocal for 67 USD per share, or a cash total of 18.5 billion USD. Unocal, an independent natural gas and crude oil exploration and production company, received the acquisition proposal from CNOOC. However, CNOOC withdrew its bid for Unocal in early August due to strong political opposition in the United States of America. CNOOC’s competitor Chevron completed its acquisition of Unocal by mid-August, even though its offer was worth 700 million USD less than CNOOC’s bid (National Petroleum News 2005).

Similarly, Haier Group (a major Chinese fridge and washing-machine manufacturer) made a bid to acquire Maytag Corporation in June 2005. The bid was for 1.28 billion USD, or 16 USD per share, and started a bidding war with the US companies Ripplewood and Whirlpool, who in turn offered to pay 14 USD per share and 17 USD per

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1 Portions of this research have been reported in Chinese with title “Determinants of success and failure of China’s overseas acquisitions”, in: *World Management*, March, 2010.

share, respectively. In July, Haier announced it withdrew from the contest. Some analysts suggest that Haier dropped out of the bidding due to difficulties in integrating Maytag's business with its own (*China Daily* 2005).

In April 2005, China Mobile Communications Corporation announced a bid for Pakistani telecommunications operator Paktel Ltd. However, it could not win the contest because another bidder, Etilsat, offered a better price (ITP.net 2005).

The reasons for the failure of a proposed acquisition can only be analyzed sensibly on a case-by-case basis. However, we believe that Chinese acquirers share some generic features and face similar challenges in their acquisition activities. We consider it worthwhile to identify these features and challenges, and examine how they affected the outcome of the announced overseas acquisitions.

In the acquisition literature, success of acquisition mainly refers to good performance of a post-acquisition entity. In this study, success refers to the fact that an announced acquisition deal is completed, which is in line with some studies on deal completion (Holl and Pickering 1988; Wong and O'Sullivan 2001). According to data from the Thomson Financial Merger & Acquisition database, of 1,324 acquisition attempts by Chinese firms announced between January 1982 and April 2009, only 679 were completed. This success rate of 51.2 per cent is not only lower than that of a developed country like the USA (76.5 per cent), but also lower than the worldwide average (68.7 per cent), as well as that of some emerging countries, such as Brazil (70 per cent), South Africa (72 per cent), India (62.8 per cent), and Russia (59 per cent). Although it is a well-accepted perception that there is a great difference between multinational companies from developed countries and those from China and other emerging economies, no study has been carried out on the pre-acquisition activities of Chinese firms. This paper uses these 1,324 acquisition attempts by Chinese firms to analyze the outcome of Chinese acquisition attempts in general. The research question is: Why could roughly half of these announced deals not be completed?<sup>2</sup>

To answer this question, we need to identify the determinants of deal completion. Despite significant advances in the literature on mergers and acquisitions, the study on acquisitions by firms from emerging

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2 Our study concerns only acquisitions that have reached the stage of public announcement. Deals discussed in private and abandoned before being made public are not included in the analysis.

countries is scarce. A few studies have investigated the motivations of Chinese overseas acquisitions (e.g. Deng 2009; Boateng, Qian, and Yang 2008; Rui and Yip 2008). However, there is lack of research on the rationale behind the completion or termination of cross-border acquisition attempts. There are some empirical studies that investigated the determinants of outcome of acquisition attempts in general (e.g. Hoffmeister and Dyl 1981; Walking 1985; Brown and Raymond 1986; Hirshleifer and Titman 1990; Holl and Pickering 1988; Duggal and Miller 1994; Raad and Ryan 1995; Holl and Kyriazis 1996; Sudarsanam 1995, 1996; Cotter, Shivdasani, and Zenner 1997; Weir 1997; O'Sullivan and Wong 1998a, 1998b, 1999; Henry 2002, 2004; Luo 2005) that identified factors that influence the outcome of acquisition, such as: target management resistance to acquisition bids; managerial ownership; target-company size; toe-hold shareholding levels of bidder companies; the existence of competing bidder parties; and the level of bid premiums offered in takeovers and ownership structure (an excellent review of the empirical evidence regarding the factors influencing outcome of acquisition attempts can be found in Wong and O'Sullivan 2001 and Henry 2004).

Those studies, while providing some useful insights into this issue, focus on acquisitions that occurred in a single advanced country, such as the USA, UK and Australia. The factors investigated are all firm specific, and the sample deals in most studies were listed companies. Given these specific focuses, the ability to reach generalizations from these results is limited. Rather, a broader perspective is needed, especially when studying China's overseas acquisition. For example, a specific issue raised by the consideration of Chinese internationalization concerns the extent to which the pattern of firm internationalization is institutionally embedded rather than reflecting a strategic choice by the leaders of firms (Child and Rodrigues 2005).

In response to these arguments, this paper studies the outcome of China's overseas acquisition attempts from a broader perspective. We combine a) the macro-level factors, such as institutional stability, culture, and trade relations, with b) industry-level factors, such as sensitiveness of target industry, and c) micro-level factors, such as ownership of acquirers and experience, and d) deal-specific factors, such as financial advisors, sought percentage, and industry match into a single framework. This broad framework not only adds value to the literature, but also has practical implications.

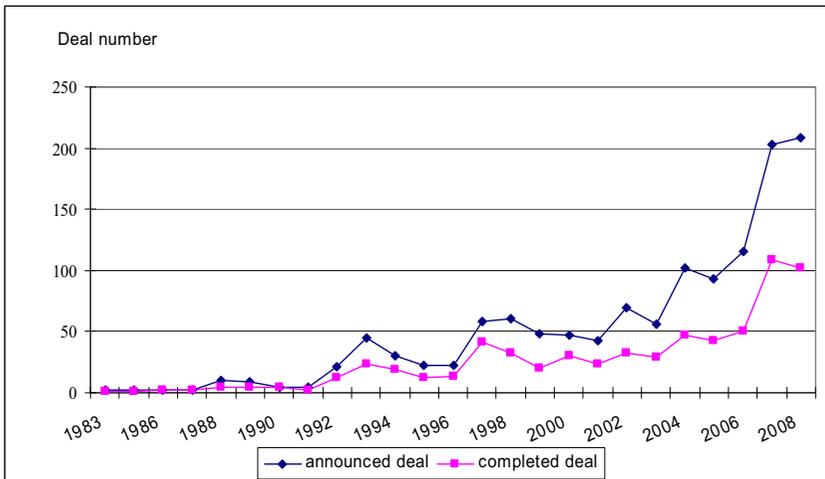
# An Overview of China's Overseas Acquisitions and Their Outcomes

Beginning with a low baseline, China's overseas acquisitions have shown strong growth, and have gradually emerged as the dominant vehicle for Chinese outward investment (OECD 2008). Making use of the Thomson database, we can illustrate China's overseas acquisitions through the following aspects.

## Development

China has been a presence in the world merger and acquisition market since the completion of its first overseas acquisition in 1982. However, overseas acquisitions weren't particularly important for the first 20 years; only a couple of acquisitions are recorded each year. From Figure 1 we can see that Chinese firms became active in terms of overseas acquisition only after 1992, when Chinese leader Deng Xiaoping visited South China and called for the opening-up of the Chinese economy to be accelerated.

Figure 1: China's Overseas Acquisition during 1982-2008

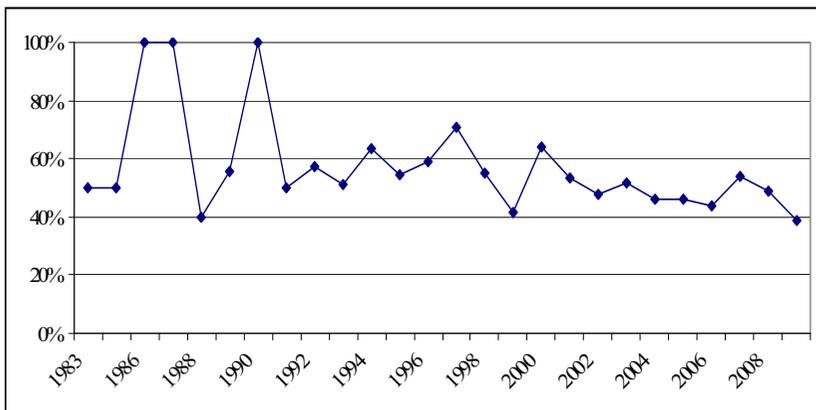


Source: Authors' own calculations based on Thomson data.

But China's overseas acquisitions were hardly noticed until 2004, when a few questionable deals were announced, such as MinMetals' bid for No-

randa. In terms of deal numbers, more than half of the announced deals took place after 2004. In terms of value, the changes are more dramatic. According to UNCTAD, the value of China’s overseas merger and acquisitions increased from 1.1 billion USD in 2004 to 15.5 billion USD in 2007 (UNCTAD 2005, 2008). It grew more than ten times in three years, becoming an important outward FDI entry mode (Global M&A Research Center 2007). This rapid growth reflects to a certain degree the support of the Chinese government. For example, in 2004 National Development and Reform Commission (NDRC) and China Exim Bank jointly issued a notice “concerning the policy on providing credit and loan support for overseas projects encouraged by the State”, which indicated that cross-border merger and acquisitions would be provided with low-rate loans (NDRC 2004). However, an increase in number and value does not correspond with an increased success rate (proportion of acquisitions that are completed out of total announced deals). Figure 2 shows no clear trend in success rate.

Figure 2: Success Rate



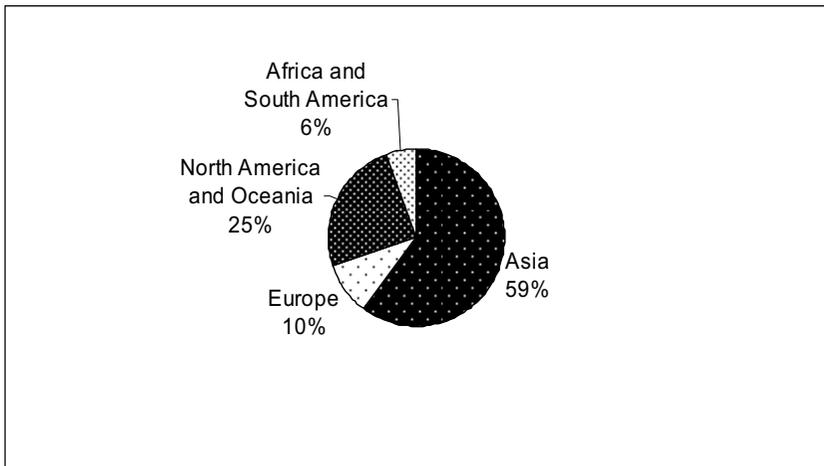
Source: Authors’ own calculations based on Thomson data.

### Locations

According to our data, China has acquisition deals in 81 countries. Figure 3 shows the regional distribution of announced acquisitions engaged by Chinese firms between 1982 and 2009. Fifty-nine per cent of announced acquisitions happened in Asia, followed by North America and Oceania

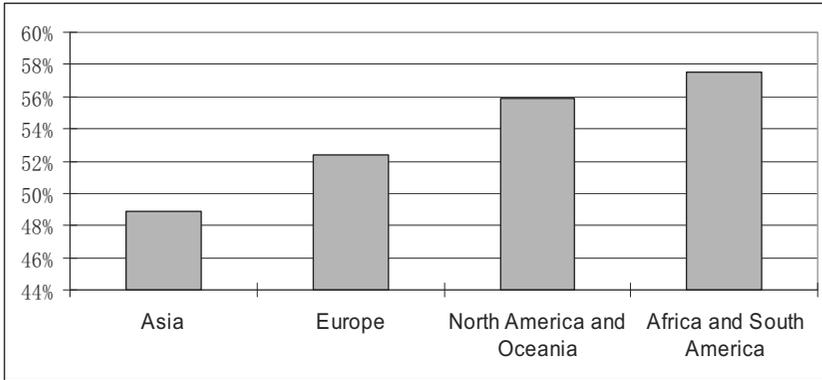
with 25 per cent, Europe with 10 per cent, and Africa and South America with 6 per cent. In terms of success rate, Africa and South America had the highest rate, followed by North America and Europe. Asian targets had the lowest rate (see Figure 4). Table 1 shows targets in which China has at least ten deals announced. The top five targets are Hong Kong, USA, Australia, Singapore, and Canada, which account for 71 per cent of total deals. Success rates differ from country to country. The USA, France, Germany, Indonesia, South Korea and Italy are among those that are important targets with high success rates in the investigating period.

Figure 3: Target Region of China's Overseas Acquisition (Announced Deal)



Source: Authors' own calculations based on Thomson data.

Figure 4: Success Rate by Regions 1982-2009



Source: Authors' own calculations based on Thomson data.

Table 1: Target Nations with at Least Ten Announced Deals

Target Nation	Number of Announced Deals	Share in Total Announced Deals (%)	Number of Completed Deals	Share in Total Completed Deals (%)	Success Rate (%)
Hong Kong	536	40.51	270	39.71	50.4
United States of America	141	10.66	89	13.09	63.1
Australia	120	9.07	57	8.38	47.5
Singapore	86	6.5	41	6.03	47.7
Canada	55	4.16	30	4.41	54.5
United Kingdom	30	2.27	13	1.91	43.3
Japan	27	2.04	12	1.76	44.4
Germany	23	1.74	14	2.06	60.9
Malaysia	19	1.44	10	1.47	52.6
Taiwan	17	1.28	5	0.74	29.4
South Korea	15	1.13	9	1.32	60.0
Indonesia	14	1.06	10	1.47	71.4
France	14	1.06	9	1.32	64.3

Target Nation	Number of Announced Deals	Share in Total Announced Deals (%)	Number of Completed Deals	Share in Total Completed Deals (%)	Success Rate (%)
Thailand	14	1.06	5	0.74	35.7
Italy	12	0.91	7	1.03	58.3
Kazakhstan	10	0.76	4	0.59	40.0
Russian Fed	10	0.76	2	0.29	20.0

Source: Authors' own calculations based on Thomson data.

## Industries

The targets of China's overseas acquisitions are spread across many industries. According to our data, China's overseas acquisitions address 295 of 444 industries at the SIC 4-digit level. Table 2 shows the industrial distribution at an aggregated level.

Table 2: Industrial Distribution of China's Overseas Acquisitions

Target Industry	An- nounced Deals	Per Cent	Com- pleted Deal	Percent- age	Success Rate (%)
Financials	249	18.79	123	18.09	49.4
Materials	225	16.98	109	16.03	48.4
Industrials	206	15.55	108	15.88	52.4
Consumer Products and Services	150	11.32	80	11.77	53.3
High Technology	142	10.72	72	10.59	50.7
Energy and Power	128	9.66	65	9.56	50.8
Media and Enter- tainment	70	5.28	37	5.44	52.9
Telecommunications	55	4.15	29	4.26	52.7
Real Estate	43	3.25	25	3.68	58.1
Healthcare	34	2.57	18	2.65	52.9
Retail	23	1.74	14	2.06	60.9

Source: Authors' own calculations based on Thomson data.

Eighty-three per cent of announced deals occurred in financials, materials, industrials, consumer products and service, high technology, and

energy and power. Regarding the outcome of acquisitions, some industries show relatively lower success, such as materials, energy and power, financials, high technology.<sup>3</sup>

## Ownership

Table 3 shows the ownership of Chinese acquirers. The most active group are private enterprises, which account for 30 per cent of announced deals and 31 per cent of completed deals. The second group are public companies, followed by SOEs and subsidiaries. However, the most active group is not the most successful one. The subsidiary group has the highest success rate (60 per cent), followed by private (52 per cent), public (48 per cent) and SOE (41 per cent).

Table 3: Ownership and Success Rate

	Announced Deal		Completed Deal		Success Rate (%)
	Number	Share in Total Announced Deals (%)	Number	Share in Total Completed Deals (%)	
SOE	256	19	121	18	47
Private	401	30	209	31	52
Subsidiary*	230	17	139	20	60
Public	353	27	169	25	48
Others	84	6	42	6	50

Note: \* The term “subsidiary” in this paper refers to an entity with a parent with 50 per cent or more ownership, that is not publicly traded on a stock exchange nor a government entity.

Source: Authors' own calculations based on Thomson data.

## Determinants of Outcome of Acquisitions

As previously stated, some studies investigated the outcome determinants of acquisition attempts, but most research was carried out from a financial perspective, and focused only on micro-level factors. Dikova, Rao Sahib, and van Witteloostuijn (2009) made the first effort to investi-

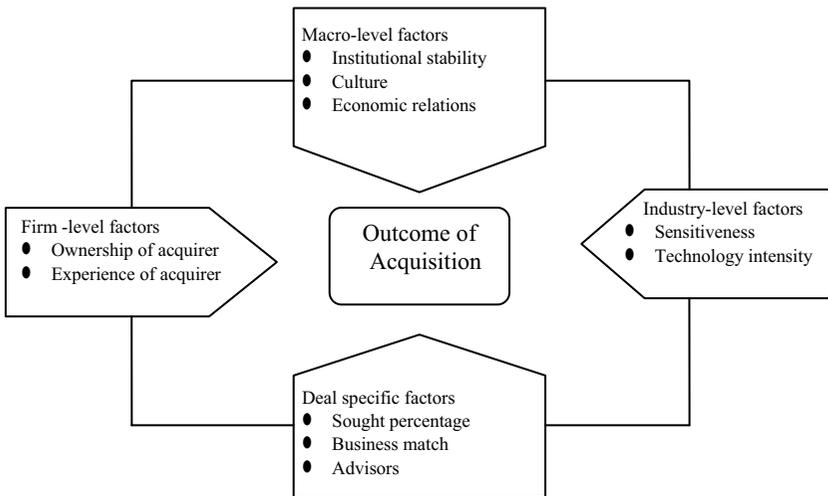
<sup>3</sup> Changes in overseas acquisitions in terms of location and industries over time are not presented due to length limitations. This information is available upon request.

gate the effect of institution on the likelihood that an announced cross-border acquisition deal would be completed. Their study offers a good example of incorporating national factors into acquisition study. However, the study only focuses on one specific industry, and the acquirer and target nations are overwhelmingly in the developed world. Research with greater variation is needed to better generalize its result. Given that China is a developing country and has only a short experience in the world mergers and acquisitions market, a broader framework is also needed to understand China's overseas acquisitions. We believe that different levels of factors decide the outcome of an acquisition deal, and therefore we need a comprehensive framework to analyze deal completion.

Although a specific theory explaining cross-border deal completion is not yet available, several relevant theoretical arguments help us build an empirical framework. Dunning's eclectic paradigm (Dunning 1993), a framework widely used in international business research, explains why, where and how FDI is chosen over other internationalization modes. The theoretical construction provides a three-tiered framework for a company to follow when determining if the pursuit of direct foreign investment is beneficial. According the framework, whether or not an FDI is beneficial essentially depends on a firm-specific factor, location-specific factors, and internalization advantages. Peng and colleagues (Peng 2002; Peng, Wang, and Jiang 2008; Peng et al. 2009) proposed a strategy tripod perspective to explain the strategy and performance of MNCs from both developed and developing countries. The strategy tripod consists of three legs: a resource-based view, an industry-based view, and an institution-based view. The resource-based view focuses on the origins of a firm's competitive advantage, and addresses why some firms in the same industry vary systematically in performance over time (Barney 1991; Teece, Pisano, and Shuen 1997). The industry-based view emphasizes the key principle of competitive strategy formulation in a firm's relationship to its environment, as represented by the industry in which it competes (Porter 1980). The institution-based view underlines the manner in which institutions exhibit significant legitimacy pressures for firms, which consequently affect a firm's strategic choices and performance (Peng, Wang, and Jiang 2008). These two theories have often been applied to the strategy and performance of MNCs. Therefore we apply the same framework in our study. Although they are different frameworks, the essential similarity is that they both adopt a multi-level

and multi-perspective approach, which provides a foundation upon which we have built a conceptional framework for our empirical study (see Figure 5). This framework indicates that determinants come from four categories: national-level factors, firm-level factors, industry-level factors, and deal-specific factors. For the sake of brevity, we have chosen to discuss the factors without extensive review.

Figure 5: A Conception Framework for Outcome of Acquisition Determinants



Source: Authors' own compilation.

## Macro-level Factors

### Stability of Institution

As North stated, “We would readily observe that institutions differ if we try to make the same transactions in different countries” (North 1990: 4). This statement implies that transactions are carried out differently in different institutional environments (the impact of institution on economic exchanges can be found in many studies, e.g. Williamson 1985; North 1990, 1991; Brunetti and Weder 1998; Buckley et al. 2007; Dikova, Rao Sahib, and van Witteloostuijn 2009). In a country without stable institutions, transaction uncertainty and complexity can be very high. When it comes to acquisition, if the host-country institution is

unstable, situational complexities may obstruct deal completion. Stability of an institution can be measured in different ways. This study focuses on the quality of bureaucracy. In general, bureaucracy is the means through which administrative execution and the enforcement of legal rules are organized. A country with a high-quality bureaucracy has the strength and expertise to govern without drastic changes in policy or interruptions to governmental services. This type of bureaucracy tends to be relatively autonomous of political pressures, and has an established mechanism for recruitment and training. In a country with low-quality bureaucracy, a change in government tends to be traumatic in terms of policy formulation and day-to-day administrative functions (Political Risk Services Group 2007). One can expect that the uncertainty of consummating an acquisition deal is higher in a country with a low-quality bureaucracy, than in a country with a high-quality bureaucracy. In line with this expectation, we propose:

### *Hypothesis 1*

The likelihood that an overseas acquisition deal led by China is completed is positively related to the quality level of a host country's bureaucracy.

## **Culture**

Cross-culture differences are widely discussed in international business studies. Regarding acquisition, there is a greater need for cultural sensitivity in resolving incompatibilities (Weber, Shenkar, and Raveh 1996). One common problem with pre-acquisition is need to collect reliable information about the target in a short time (Very and Schweiger 2001; Jemison and Sitkin 1987). These can be even more challenging in a culturally different environment, which may cause the acquirer to abandon a deal when the situation is too difficult to handle (Jemison and Sitkin 1987). In addition, conflicts between the acquisition deal parties frequently stem from differences in business ideology. This can trigger disputes between parties as they seek to finalize a deal. Cultural differences are likely to increase the likelihood of such tensions, which may cause deal abandonment. Following this logic, we propose:

## *Hypothesis 2*

An overseas acquisition deal is less likely to be completed in an alien culture environment than in a familiar culture environment.

## **Economic Relation between Host and Home Countries**

Although no study has addressed this issue yet, we would like to argue that economic relation between host and home countries may influence deal completion. The rationale behind this is that the better two countries integrate, and the better the firms from one country understand the business environment in another country, then the better the chance that a deal is completed. Economic relation is a broad concept, which is difficult to measure. In this study we focus on trade relation. Trade relation includes export- and import linkages. We expect that both linkages are related to acquisition activities. According to the investment development path:

as indigenous firms start to generate their own ownership (O)-specific advantages they tend to exploit these firstly by exports, and then, as their foreign markets expand and/or the costs of home-based production rise, by outward investment. At this stage, in order to become global players, industrializing country firms also begin to seek out foreign technology, management skills and organizational expertise, by means of mergers and acquisitions (M&As) (Dunning, Kim, and Lin 2001: 146).

The path reveals the ordering sequence between export and acquisition. From this sequence, we expect that export experience benefits investment performance, including pre-acquisition performance. On the other hand, China's imports might also be related to acquisition activity. If China imports intensively from one country, China would understand that country well in terms of its business environment and culture. This would help reduce uncertainty in an acquisition process. The trade relation in this study is measured by trade intensity. This is defined as the ratio of China's import and export share in relation to the total imports and exports of a host on one hand, and the percentage China represents of total imports and exports in world trade on the other hand. High trade intensity suggests a high level of penetration and recognition of Chinese companies in the host country. The same is true for foreign companies in China. Furthermore, this bilateral relationship may posi-

tively influence the likelihood that acquisition deals are completed. Therefore we suggest:

### *Hypothesis 3*

An overseas acquisition is more likely to be completed in a host country that has high trade intensity with China, than in a host country that has low trade intensity with China.

## Industry-level Factors

### Sensitiveness of Target Industry

After an acquisition attempt is announced, it has to face an important hurdle, which is compliance with the host country's (and international) regulations. Acquisitions are usually subject to a regulatory scrutiny, as required by different national competition laws. This practice applies to about 90 countries across the world (Singh 2002). Therefore, the success of an acquisition deal does not rely purely on economic or financial rationales. Political concerns and perceived national security threats can lead to national review agencies to quash deals in the name of national security or to protect local "champion" companies from competitive disadvantage (Toth 2008). The targeting of some companies may face political pressure, particularly those whose operations have national security or national interest implications involving energy and other scarce natural resources (sensitive resources), military production, and crucial infrastructure. Given that countries have different definitions for what constitutes a sensitive industry, this study focuses on energy and sensitive-resource sectors. Hereafter, we refer to these sectors as sensitive industries. We expect:

### *Hypothesis 4*

An overseas acquisition in energy and sensitive-resource industries is less likely to be completed than one in other industries.

### *Technology Intensity of a Target*

As a developing country, one important motivation behind China's foreign acquisitions is the desire to obtain advanced technology (Deng 2009).<sup>4</sup> However, the technology gap between the target and acquirer may also hamper the completion of a deal. Upon the signing of a preliminary acquisition contract and the making an initial public announcement, communications between both parties go into greater detail and address issues such as how integration will work. During this stage, the acquirer may abandon the deal when they realize it is too difficult to integrate due to a big technology gap with the target. We see similar problems in the energy and power industries. Some high-tech industries can also be sensitive because they involve a certain group's interests and/or a country's security. Therefore, we propose:

#### *Hypothesis 5*

An overseas acquisition with a high-tech target is less likely to be completed than a deal with a low-tech target.

## Firm-level Factors

### Ownership of Acquirers

Ownership of acquirers is also sensitive to deal completion. Like other developing and transitional economies, China's is characterized by active government involvement in business, through ownership and regulation (Peng 2000; Child and Rodrigues 2005). It is a widely shared perception that Chinese companies' cross-border acquisitions have benefited from the government's financial support. This support may enhance an acquirer's competitiveness in the bid. However, we must also consider the reaction from host countries. According to Luo (2005), the market reaction to a merger and acquisition announcement predicts whether the companies later complete the deal. Subsidization by home government is often seen as an unfair business practice by the host's bidders. Involvement by home government may also increase political sensitivities. The host country's government is likely to turn down the acquisition attempt

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4 Acquisition motives may also influence the result of acquisitions. However, we do not have the data to test the differences between motives.

for the sake of local industry protection and national security. SOE acquirers are most likely to be attacked by protectionism. MinMetals' bid is an example. In 2004, China's MinMetals made a formal bid for Noranda, the largest Canadian mining company. But the announcement set off protests from both the political left and right in Canada. The main concern is that China's MinMetals is government-owned. Following this practice, we propose:

### *Hypothesis 6*

An acquisition deal with a SOE acquirer is less likely to be completed than other forms of enterprises.

In contrast to SOEs, a private enterprise is more likely to pursue profitability and efficiency following market rules, and is less likely to encounter the unfavourable reactions. The same principle is applicable to subsidiaries, which are less sensitive in political terms than SOEs. Furthermore, acquisition activities of a subsidiary can be supported by a parent company that may have more cross-border experience. This experience will positively affect the acquisition process. Reactions towards other ownership forms, such as public firm and joint venture, lie somewhere between SOE and private. Therefore we have:

### *Hypothesis 7*

An acquisition deal with a) a private acquirer or b) subsidiary acquirer is more likely to be completed than with other sorts of acquirers.

## **Experience**

Experience is important in international business, and this applies to cross-border acquisitions as well. Previous experience with acquisition processes in multiple countries may facilitate deal completion in a new location. With more acquisition experience, firms can develop routines in terms of adherence to diverse competition laws, consistent messaging to all stakeholders, development of effective communication strategies, and the planning the integration and transformation of the merging firms into one new entity (Dikova, Rao Sahib, and van Witteloostuijn 2009). Therefore, the accumulation of experience in addressing various critical issues that firms face after the initial deal announcement may increase the likelihood of success. Hence, we suggest:

### *Hypothesis 8*

An acquirer that has successful experience with overseas acquisition is more likely to complete a deal than one without experience.

## Deal-specific Factors

### Advisor

Professional advisors are familiar with nation-specific legal and tax systems, local accounting practices, and local management style. When it comes to overseas acquisitions, it is logical to assume that it is important to hire an international advisor, especially for Chinese firms without much experience in international mergers and acquisitions. We expect that a deal with an international advisor is easier to be completed than those without.

### Sought Percentage

Is the percentage sought by an acquirer of a target's ownership stake. The higher this percentage, the more there is at stake for the acquirer's and target's shareholders. We expect that a deal with high sought percentage is difficult to be completed, because the higher the percentage, the more influential the deal will be and the more attention and reactions that it will evoke, which in turn, creates more complexity for deal completion.

### Industry Match

When acquisitions take place across unrelated businesses, the announced acquisition attempt may induce negative reactions from investors and the market. This is because investors often believe that unrelated acquisitions tend to hurt the stockholders of acquiring firms, and the market may believe that the acquiring firm paid too much for the target firm, or that the combination will result in diseconomies for the combined firms (Flanagan 1996). Following these assumptions, we propose:

### *Hypothesis 9*

An overseas acquisition is more likely to be completed if a) the acquirer hires an advisor, b) sought percentage is low, and c) the acquirer and target are in the same industry.

## Data and Methodology

### Data

The sample of this study is the population of 1,324 cross-border acquisitions engaged by Chinese firms that occurred between January 1982 and March 2009, accessed from the Thomson Financial Merger & Acquisition database (henceforth Thomson). Thomson collects data on M&As worldwide from many sources – English and foreign language news media, filings at the Securities and Exchange Commission (SEC) and its international counterparts, and trade publications. The M&A data cover corporate transactions involving any value, and where the value of the transaction was undisclosed. Both public and private transactions are included. This database offers information on deal status, dates of transaction announcement and completion, and some features about targets and acquirers, such as ownership, industry, experience, sought percentage, and advisor. To ensure the accuracy of the information, we double-checked it using Lexis-Nexis Academic Universe database. Regarding country-level data, quality of bureaucracy and government stability are from the PRS Group's Institutional Country Risk Guide assessments (<http://www.prsgroup.com>); culture data are from GLOBE project. Export and import data are from IMF Direction of Trade database (Table 4).

### Methodology

Our dependent variable is acquisition completion, which is a dummy variable that takes the value of 1 if the announced acquisition attempt is completed and 0 if it is not.<sup>5</sup>

Table 4 gives an overview of all explanatory variables, including their expected sign, related hypothesis, measures, and data sources.<sup>6</sup> All

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5 Here we only consider if a deal is completed or not. We do not distinguish if a deal was completed in the year in which it was announced or in the following years.

the macro-level explanatory variables are in line with the acquisition deals in terms of period. For example, if an acquisition was announced in 2007, levels of bureaucracy quality and trade intensity also refer to 2007 for the countries concerned.

Because the dependent variable is dichotomous, we use logistic regression to analyze the determinants of outcome of acquisition attempts. The logit model is represented as follows:

$$P(i) = 1/[1 + e^{-\beta X(i)}]$$

where  $P(i)$  is the probability of acquisition  $i$  being completed;  $e$  is the exponential function;  $X(i)$  is the vector of independent variables, including the key explanatory variables and control variables listed above; and  $\beta$  is the regression coefficients for the vector of independent variables  $X(i)$ . The explanatory power of the logit model is determined using the likelihood ratio test.

Table 4: Overview of Hypothesis, Variables, Estimations and Measures

	Hy-pothesis	Variables and Ex-pected Sigh	Measures	Source
Macro-level factors	H1	Bureaucracy quality (+)	A score ranging from 0 to 4. High points are given to countries that have high bureaucracy quality, the details can be found at Political Risk Services Group, 2007	Political Risk Services Group
	H2	Culture (+)	Dummy variable with the value of 1 if a target is an Asian country that influenced by Confucianism and Hinduism, and 0 if it is not*	GLOBE project (House et al. 2004)
	H3	Trade intensity (+)	$TI_{ch} = \frac{(x_{ch} + m_{ch}) / (x_h + m_h)}{(x_c + m_c) / (x_w + m_w)}$ x and m denote export and import, c, h and w denote China, host country and the world	IMF DOT

6 Bilateral investment treaties could be an institutional factor that influences the cross border acquisition. However, in our 1,324 samples, only 93 acquisition deals were announced before the bilateral treaty was signed. In addition, an empirical test results an insignificant coefficient. Therefore we do not include this variable in our study.

	Hy- pothesis	Variables and Ex- pected Sigh	Measures	Source
Industry level factors	H4	Sensitive resource (-)	Dummy variable with the value of 1 if an acquisition deal is in energy and other sensitive industries and 0 if it is not	Thomson
	H5	High-tech target (-)	Dummy variable with the value of 1 if a target is in AeA's 45 SIC codes list (AeA.net), and 0 if it is not	Thomson and American Electronics Association
Firm level factors	H6	SOE acquirer (-)	Dummy variable with the value of 1 if an acquirer is state owned enterprise and 0 if it is not	Thomson
	H7a	Private acquirer (+)	Dummy variable with the value of 1 if an acquirer is a private enterprise and 0 if it is not	Thomson
	H7b	Subsidiary acquirer (+)	Dummy variable with the value of 1 if an acquirer is a subsidiary and 0 if it is not	Thomson
	H8	Experience (+)	Dummy variable with the value of 1 if an acquirer has successful experience in overseas acquisition, 0 if it is not	Thomson
Dear specific factors	H9a	Advisor (+)	Dummy variable with the value of 1 if an acquirer hires an international advisor, and 0 if it is not	Thomson
	H9b	Sought percentage (-)	The percentage of the ownership stake sought by an acquirer	Thomson
	H9c	Industry match (+)	Dummy variable with the value of 1 if the acquirer and target in a transaction are in the same industry, and, and 0 if they are not	Thomson

Notes: \* There are two reasons to choose this measure. 1) China's culture is, by and large, shaped by Confucianism and Hinduism; 2) Many similarities exist between Confucianism and Hinduism. We admit that there is a limit to using the dummy variable, because it cannot distinguish the differences of non-Asia countries. We leave this for future study with a focus on culture perspective.

Source: Authors' own compilation.

We calculated the correlation between all explanatory variables. All correlations are below the commonly used cut-off threshold of 0.7 (see Appendix), which reveals no multicollinearity problems.

## Result

Table 5 presents the results of logistic regression models. Model 1 gives the results with SOE acquirer included. Model 2 gives the results with private acquirer included. Model 3 gives the results with subsidiary acquirer included.

Table 5: Estimation Results

	Model 1		Model 2		Model 3	
	Coefficient	Std. Error	Coefficient	Std. Error	Coefficient	Std. Error
Bureaucracy quality	0.070	0.085	0.083	0.085	0.073	0.085
Culture	-0.462**	0.168	-0.421**	0.166	-0.472**	0.168
Trade intensity	0.051**	0.024	0.048**	0.024	0.046**	0.024
Sensitive resource	-0.290**	0.147	-0.314**	0.146	-0.307**	0.146
High-tech target	-0.156	0.164	-0.141	0.163	-0.101	0.164
SOE Acquirer	-0.259*	0.147				
Private acquirer			0.057	0.123		
Subsidiary acquirer					0.511***	0.153
Experience	0.406***	0.126	0.392***	0.126	0.439***	0.127
Advisor	0.417**	0.177	0.411**	0.179	0.395**	0.177
Sought	0.001	0.002	0.001	0.002	0.001	0.002
Industry match	0.018	0.114	0.029	0.114	-0.007	0.114
Constant	-0.177	0.373	-0.307	0.366	-0.320	0.367
Log likelihood	-896.22		-891.56		-896.92	
LR chi2	31.84		28.99		40.14	
Prob > chi2	0.0004		0.001		0.0000	
Number of observation	1324		1324		1324	

Notes: \* p < 0.10; \*\* p < 0.05; \*\*\* p < 0.01.

Source: Authors' own compilation.

The reason that we include the three ownership variables into the model separately is that we intend to compare each of them with the rest of the firms. For each model, we report the coefficients, standard error, value of the likelihood function at convergence and the likelihood-ratio chi-square. The chi-square statistic is significant at the 1 per cent level in all models, which suggests our models fit the data well.

From Table 5 we see that the coefficients of Trade intensity, Nature resource, SOE acquirer, subsidiary acquirer, Experience and Advisor are all significant and with expected signs, which support to Hypothesis 3, 4, 6, 7b, 8 and 9a. The rest of the variables are either insignificant or in a wrong sign, leaving Hypothesis 1, 2, 5, 7a, 9b and 9c not accepted.

## Conclusion

The findings above give rise to the following observations worth discussion. First, although institutions of home and host countries may inspire China's overseas acquisition activities, they are not always in favour of the outcome of the acquisitions. The home country's institutions can stimulate overseas acquisition activities in both a direct and an indirect way. Directly, with government's support, many firms (especially SOEs) are able to conduct acquisitions abroad; indirectly, institutional restrictions or constraints, such as restrictions on domestic acquisition, or regional protectionism, may act as a push factor for overseas acquisitions. A relatively friendlier institutional framework in developed host countries may act as a pull factor for China's overseas acquisition. These institutional factors may increase the number of overseas acquisitions, but they do not always have a positive impact on deal success. According to our analysis, home country's institution, such as government's ownership, has a negative effect on the outcome of acquisition; host country's institution, such as bureaucracy quality does not have a significant effect on deal completion.

Second, acquirer's ownership influences the outcome of acquisition attempts.

- The analysis result shows, *ceteris paribus*, the deals with SOE acquirers are less likely to be completed. This finding indicates that, although the support from government encourages initiation of the acquisition attempts, it incurs negative reaction on the deal completion.

- In line with our expectations, the deals with subsidiary acquirers are more likely to be completed than other deals. This finding confirms that a subsidiary has stronger capability in deal completion due to the support of a parent company.
- We observe that the coefficient of private acquirer is positive but insignificant in our analysis. This indicates that, although a private acquirer may not incur any negative reaction on its acquisition attempt from host institution, economic and financial rules also play a role. In general, Chinese private enterprises are not yet well developed, especially in global markets. They are small in scale, weak in liquidity, and short of international business talents, which make them less competitive in the merger and acquisition market. The probability of success is low when a stronger competitor appears. Given that private enterprises are the most active players in overseas acquisition, the weaknesses of private enterprises reduce the success rate of deal completion. Therefore, the low competitiveness of main players provides one explanation for the low success rate of China's overseas acquisitions.

Third, experience is an important success factor. However, internationalization of Chinese firms remains at a very primary stage. According to our statistics, 766 out of 1,324 announced deals (58 per cent) took place after 2004, and 931 out of 1,324 announced deals (70 per cent) without any successful experience abroad. In terms of acquirers, only 12 per cent of them had successful experience according to our data. A distinctive domestic social environment and lack of global experience hampers Chinese acquisition deals. This result provides another explanation as to why half of China's acquisition deals could not be successful.

Fourth, China's distinctive institutions endow some specific attributes for the nation's overseas acquisitions. These attributes, together with the institutions of home countries, induce some specific and negative reactions towards China's overseas acquisitions attempts. From our empirical study, we found that when other conditions are equal, a deal in a sensitive industry with a SOE acquirer is less likely to be completed. Since 1982, 1,324 overseas acquisition attempts by China have been recorded in the Thomson database. Among these deals, 354 deals were in sensitive industries, and 256 deals were with SOE acquirers. These deals are more likely to receive a negative reaction toward deal completion after announcement. This result gives an additional explanation as to why half of China's acquisition deals could not be successful.

Fifth, trade intensity between China and the host countries is a significant factor influencing the outcome of acquisition deals. This implies that experience and recognition accumulated from international trade plays a role. This result implies that Chinese firms should be cautious when they conduct an acquisition in a country in which China has weak economic ties.

Sixth, the results suggest that advisors play a positive role in the pre-acquisition activities, which implies that the hiring an international advisor is recommended.

In summary, by using 1,324 deals and a logit model, we examined potential factors that may influence the success of announced acquisitions by Chinese firms. The results confirm that factors from macro level, firm level and deal level all simultaneously influence the outcome of announced acquisitions. Based on the findings, we conclude that the distinctive domestic social and economic environment of acquirers, sensitiveness of the industry, ownership and low competitiveness of acquirers, and a lack of global experience all hamper Chinese acquisition deals.

Although this study helps to understand the outcome of China's overseas acquisitions, it is not without limitation. In order to set up a comprehensive empirical framework to figure out the reasons behind the low success rate of China's overseas acquisitions, we were not able to make an in-depth analysis of all the determinants. Future efforts are required to do in-depth researches on each of the determinants, such as institution, culture, and characteristics of industry and firm.

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# Appendix

## Descriptive Statistics of Independent Variables

	Mean	Std. Dev.	Bureaucracy Quality	Culture	Trade Intensity	Sensitive Resource	High-tech Target
Bureaucracy Quality	3.271	0.719	1				
Culture	0.581	0.494	-0.306	1			
Trade Intensity	3.746	3.369	-0.303	0.697	1		
Sensitive Resource	0.267	0.442	-0.045	-0.384	-0.296	1	
High-tech Target	0.144	0.351	-0.006	0.105	0.060	-0.233	1
SOE Acquirer	0.193	0.394	-0.087	-0.140	-0.035	0.199	-0.097
Private Acquirer	0.303	0.460	0.085	-0.016	-0.019	-0.041	-0.018
Subsidiary Acquirer	0.174	0.379	-0.001	0.143	0.115	-0.083	-0.041
Experience	0.297	0.457	-0.048	-0.058	-0.045	0.139	-0.088
Advisor	0.122	0.328	0.048	-0.066	-0.077	0.145	-0.042
Sought	60.014	37.843	0.043	-0.109	-0.165	-0.048	0.004
Industry Match	0.484	0.500	-0.064	0.011	-0.042	-0.078	0.114
	Mean	Std. Dev.	Bureaucracy Quality	Culture	Trade Intensity	Sensitive Resource	High-tech Target
Bureaucracy Quality							
Culture							
Trade Intensity							
Sensitive Resource							
High-tech Target							
SOE Acquirer	1						
Private Acquirer	-0.322	1					
Subsidiary Acquirer	-0.224	-0.302	1				
Experience	0.098	0.007	-0.110	1			
Advisor	0.075	-0.146	-0.007	0.151	1		
Sought	-0.092	0.005	-0.020	-0.068	0.026	1	
Industry Match	-0.063	-0.060	0.082	-0.051	0.040	0.075	1

Source: Authors' own compilation.

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