

Assessing the impact of financial crises on cross-border M&A flows in developed and developing economies

Olga Valerjevna Vlasenko¹, Svetlana Nikolaevna Khobotova^{1,2}, Anton Vladimirovich Pyatak²

¹Plekhanov Russian University of Economics Omsk Institute (branch), Str.10 years on October , 195/18, Omsk, 644009, Russian Federation

²Omsk State University. Prospect Mira, 55-A, Omsk, 644077, Russian Federation

Abstract. This article analyzes total value of cross-border mergers and acquisitions (M&A), number of deals and average deal value from 1997 to 2012. Asian crisis in 1997 and World financial crisis in 2008 had a great impact on the world economy during this period and defined its specific features. Therefore this article analyzes key characteristics and direction of M&A flows for developed, developing and transition economies. The research is based on data from different sources, for example: IMF Research Bulletin, UNCTAD, World Investment Report, E&Y reports.

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Introduction

Internationalization became essential stage of development for many companies of different size and this structural shift was accompanied by such economic processes as mergers and acquisitions. Despite the fact that every decision about a deal is very individual and based on company policy as much as on market condition, there are global trends of M&A in world economy that were confirmed by many studies [1], [2]. Exactly these global trends are under consideration in this article.

Structural changes on financial market in 2000s, that caused world financial crisis, gave us an idea to take M&A flows into consideration and analyze how its role and key features have changed in 1997-2012. Moreover, increasing role of BRIC and MIST (Mexico, Indonesia, South Korea and Turkey) countries alters international capital flows and its direction that could be additional factor, which has an impact on M&A [3].

Methods.

Value of M&A flows is one of the key indicators that demonstrates us the state of the world economy. In addition, dynamics of M&A waves was often related to crises [4]. However, some studies say that crisis in 2008 had different impact on M&A flows. Therefore we would test this hypothesis and analyze geographical structure of cross-border mergers and acquisitions after Asian crisis in 1997 and World financial crisis in 2008.

For analysis of geographical structure we used World Investment Report 2013 [5] as the database. Also, there were chosen two classifications

of countries. The first of them is based on level of economic development: developed, developing, transition economies.

The second classification is based on geographical location of region: Europe (EU + other developed countries of Western Europe), North America, Asia, Other developed countries (Australia, Bermuda, Israel, Japan, New Zealand), CIS, Latin America and the Caribbean, Africa.

This approach allows us to make a complete research considering both level of socio-economic development and location. Moreover, there are regions-buyers and regions-sellers to distinguish the direction of M&A flow. We analyze value of cross-border M&A, number of deals and average deal value. Data processing was carried out with help of statistical, regression and correlation analysis. Key dates for the research are: 1997– Asian financial crisis; 1998 – Crisis in Russia, technical default on bonds; 2007 – Mortgage crisis in the USA; 2008 – Crash on stock markets, the beginning of the world financial crisis and global recession; 2010 – The beginning of debt crisis in Europe.

Main part. I. Analysis of value of cross-border M&A

We analyzed condition of cross-border M&A market in 1997-2012 and distinguished 3 periods of rapid growth of activity: 1997-2000, 2004-2007, and 2010-2011.

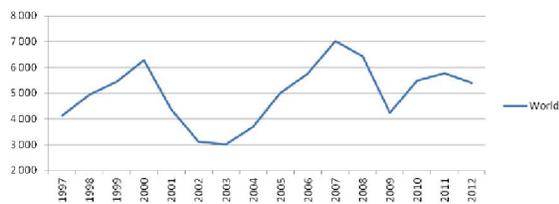


Fig 1. Cross-border M&A market (1990-2012), \$ millions. Calculated on the basis of [5]

The first step of the research was to analyze changes in value of M&A flows for developed, developing and transition economies. Data for analysis is presented in table 1 and 2.

Table 1: Socio-economic structure of world M&A market, sales (1990-2012), share based on value of flows

Sales, %	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Developed economies	77	87	89	94	85	82	84	87	87	84	87	82	81	75	78	84
Developing economies	20	12	11	6	14	17	11	11	14	14	10	15	16	24	16	16
Transition economies	3	0	0	0	1	1	5	2	-1	1	3	3	3	1	6	-1

Source: Author's own calculations based on [5]

Table 2: Socio-economic structure of world M&A market, purchases (1990-2012), share based on value of flows

Purchases, %	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Developed economies	83	86	88	86	84	74	69	73	75	77	78	74	63	68	72	69
Developing economies	10	7	6	8	8	14	14	14	15	15	15	16	18	20	18	19
Transition economies	0	0	0	0	1	1	1	1	1	1	1	2	2	1	1	1

Source: Author's own calculations based on [5]

The year of Asian crisis could be characterized by rapid growth of M&A in developing economies (from 14,18% to 20,12%). Moreover, the crisis caused a new wave of activity on the market of cross-border M&A. This wave existed until 2000. It is worth to mention that except the 1997 growth of M&A flows value occurred mostly because of acquisitions made in developed countries by companies that are originated also from developed countries (about 90% of deals). In addition, share of purchases in developing countries increased from 5,78% in 2000 to 23,95% in 2010). Impact of the crisis on transition economies was not so strong, but, nevertheless, the share of acquisitions made in transition economies in 1997 was one of the highest in history (2,72% of all deals). But it is difficult to assume if the reason for such a growth was Asian crisis or another round of privatization.

World financial crisis in 2008 was the reason for rapid drop in M&A market activity for 2 post-crisis years (75% decline for 2 years). After 2008 share of flows from developed economies dramatically decreased from 80,4% to 64,38%. In

contrary, part of M&A made by corporation from developing countries skyrocketed from 15% to 29,62%. Value of M&A flows in the world finally increased only in 2010, namely with 2 years lag after the crisis. Starting from the 2011 share of purchases by companies from developed countries greatly increased together with value of M&A flows in the world. Growth of M&A in developed countries coincides with growth of M&A flows from developed countries in 2011. Similar connection could be observed in 2007 after mortgage crisis in the USA. It means that corporations from developed countries prefer buying companies from the same group during crisis. It is confirmed also by trends in 1998-2000. We could also notice that share of deals in developing countries grow during the crisis years both in 1997 and 2008-2010, but growing share of mergers and acquisitions by companies from developing countries did not result in growing market. Moreover, cross-border M&A market returned to the pre-crisis level only after the share of acquisitions made by corporations from developed countries had begun to grow.

Statistics of 2012 demonstrates great decrease on cross-border M&A market again. It could be observed together with growing share of sellers from developed countries and buyers from developing economies. It is a bad sign about condition of world economy because can indicate that opportunity for growth after the crisis is over. That means we could scarcely expect strong growth on this market soon. Research of E&Y [6] explain this trend by the fact that buyer and seller agreement on deal valuation has become increasingly difficult to bridge in 2012 due to the volatility of commodity prices and growing divergence between equities and commodity prices. Sellers have been unwilling to accept lower valuations based on their depleted share prices in 2012. Furthermore, cost overruns at upcoming capital projects, running into billions in some cases, have become commonplace. As a consequence, companies shifted gear from "growth for growth's sake" to "capital optimization" during 2012. Low cost, long life assets became the priority and M&A activity slowed.

Next step was to analyze geographical structure of deals and the role of different regions at cross-border M&A market.

The biggest share of cross-border M&A flows comes to Europe. The second place takes North America. This ranking always existed during 1997-2012. However, shares of deals in these regions have explicit reverse trend. Asian sellers became active players on cross-border M&A market in 1997 and had solid third place in 2000s. Cross-border M&A flows from Asia have reverse trend with Other

developed countries similar to pattern of Europe and North America. Other regions did not follow any visible pattern and their shares were very unstable. Structure of buyers relating to Europe and North America is quite similar to structure of sellers. Share of cross-border M&A flows from Europe always was higher than from North America except 2003.

During the Asian crisis value of acquisitions in Asia increased almost twice to share of 8,75%. Within 3 years after the crisis absolute value of M&A in Asian region was remaining the same, but its share decreased because of increasing part of deals in Europe (from 37,78% to 56,95%). Share of buyers located in Europe reached 74, 20% in 2000. Although buyers from North America increased its value of M&A flows, the share of acquisitions from this region dropped almost twice in 3 years. This means that after the crisis the main driver of market growth was in Europe.

In 2008 and 2010 share of acquisitions in North America grew rapidly when share of acquired European companies, on the contrary, was decreasing. Situation in 2009 was opposite with growing part of acquisition in Europe. Share of deals in other regions were stable except 2010. While the value of M&A flows in the world was dramatically dropping, share of buyers from Asian, other developed and CIS countries was growing. For example, share of acquisitions from Asia in 2009 increased to 26,95%. Activity growth in 2010 occurred mostly because of buyers from the USA and Canada. In 2011 European companies joined this list, while Asian companies started losing their share but value of deals made by companies from this region didn't change. Thus, we can make an inference, that during World financial crisis Asian regional M&A market was active at the initial stage of crisis both at purchases and sales when European and North American corporations was dormant. Since 2010 Asian companies began to lose their share and this decline continued until today.

II. Assessing the number of cross-border M&A flows and average value of deals

First two steps of research were based on analysis of M&A flows value. However, this approach is not always acceptable to describe the activity on M&A market because a couple of big deals could change statistics very much and make it impossible to analyze. Therefore, at the third step we used number of deals for analysis.

The only big distinction from value of deals analysis is in that Asian crisis didn't cause so rapid growth of acquisition number as it was with M&A flows value. On the other hand, World financial crisis

caused exactly the same changes in number of deals as in its value.

The fourth step of research was to analyze average value of M&A deals from 1997 to 2012. This research lets us understand how typical M&A deal looked like after Asian crisis and World financial crisis in different parts of the world.

Average deal value clearly characterizes trends, which was caused by this crisis. Asian crisis caused an immediate increase in deals value, which continued for 3 years. The first two years of world financial crisis were marked with drop of this indicator, but 2 years after the crisis trends became similar to situation after crisis in 1997.

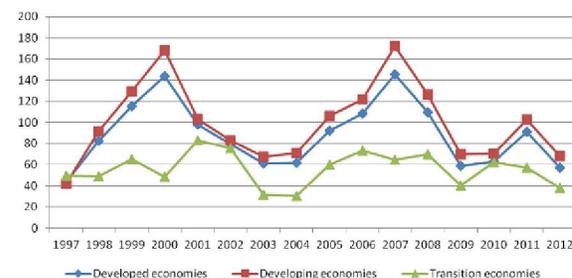


Fig 2. Average value of M&A deals, socio-economic structure (1990-2012).

Calculated on the basis of [5]

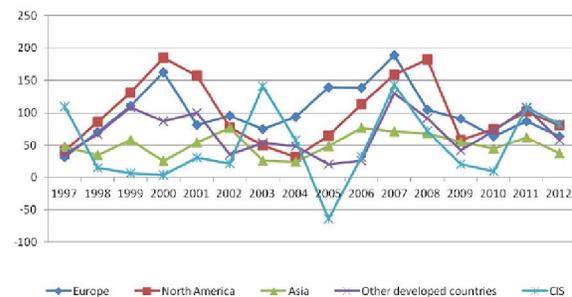


Fig 3. Average value of M&A deals, geographical structure (1990-2012).

Calculated on the basis [5]

Now we are trying to make inferences about changes on cross-border M&A market, which were caused by crisis in 1997 and 2008, and sum up result of previous 4 steps.

Conclusion.

Within 1997-2012 the major part of cross-border M&A flows was in developed economies and its minimal share was 75% in 2010. Share of mergers and acquisitions in developing economies was growing within all the 2000s until 2010. Share of buyers from developed countries greatly increased in

1997-1999 and in 2010-2011. Between these two periods we can observe increasing share of acquisitions made by corporations from developing economies.

Structure of buyers and sellers stays stable during all period. Despite the fact that Asian companies begin to play more important role on M&A market they still don't have enough financial strength to make a big impact on the market or create new waves of M&A.

Crises in world economy cause growth of activity on M&A market and Asian crisis caused growth of value and number of cross-border M&A almost immediately. However, after world financial crisis the same effect appeared only with two-year interval. We can try to explain this paradigm by looking at the core of both crises. Asian crisis resulted in heavy economic damage to Asian, CIS and Latin America countries, while crisis in 2008 struck all over the world. Asian crisis was the reason of activity growth on M&A market for 3 years because typical buyers (corporations from Europe and the USA) were not stroked by the crisis. Research of Lingnan University [7] agrees with this conclusion and holds that the financial crisis causing a series of M&A activities. Some companies aim to enjoyed synergy gain or others aim at saving their subsidiaries that were trapped in the financial crisis.

Situation in 2007 was much more difficult because recession and liquidity crisis restricted ability of corporations to make M&A deals all over the world. Typical acquirers didn't have enough money to stimulate new wave of activity on M&A market. This conclusion may seem obvious but nearly everyone in 1997 thought there would be more M&A volume - more strategic transactions and initial public offerings. And, despite the Asia crisis and Russian default, global meltdowns weren't in anyone's calculations [8]. Influence of crisis could be confirmed by research of [9] which states that macroeconomics factors are statistically more significant in crisis period for cross-border M&A market compared to the pre-crisis period.

This state of market changed in 2010. This year could be characterized as the beginning of growing value and number of cross-border M&A deals. We think that basic reason for that was the state of world economy at this moment. Firstly, corporations from developed countries have almost recovered from crisis. Secondly, bear trend was still observed on the stock market. Thirdly, because of crisis credit rates were at very low level and made LBO (leveraged buyouts) possible. This assumption is confirmed by computing of Pearson correlation coefficient between credit rates in Germany, the USA and Great Britain and value of cross-border M&A

flows from these countries. Results of analysis are presented in table 3.

Research of Baker & McKenzie [10] states that with cheaper financing options and more robust market conditions, executives are increasingly confident and thinking more creatively about their growth strategies. These conclusions are confirmed by average value of M&A deals. Although during the crisis most of companies become cheaper, average price of M&A deals increases. This way companies can get bigger discount in compare with period of economic growth. Rapid growth of average value of M&A deals is observed exactly in 1997 and 2010.

Table 3: Correlation between credit rates and value of cross-border M&A (1990-2012)

	Germany	The United States of America	Great Britain
Pearson correlation coefficient	-0,064	-0,031	-0,055
Source: Author's own calculations based on [5]			

Ultimately, the World financial crisis is a complex problem with a long-term effect which may be partly hidden during next few years. The Economist Intelligence Unit survey of senior executives confirms that business sentiment on M&A is still far from confident. Over one-half (54%) of respondents say that it will take another decade for the M&A market to recover fully from the impact of the global financial crisis and rebound to 2007 levels is unthinkable for now. However, there is reason to believe the worst may be over [11].

Corresponding Author:

Dr. Vlasenko, Plekhanov Russian University of Economics Omsk Institute (branch), Str.10 years on October, 195/18, Omsk, 644009, Russian Federation.

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