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The emergence and performance of the Chinese merger market and the impact of partner location

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ABSTRACT

Chinese acquirers spent \$38 million on mergers and acquisitions in 1990, and \$666.1 billion on mergers and acquisitions in 2016. As the Chinese merger market has grown, so too has the literature on its performance. Little is known, however, about with whom Chinese firms can best do business. We aim to fill this gap. We suggest that because the liabilities of distance, foreignness, and outsideness complicate acquisition performance, targets in countries and regions which add fewer of these liabilities will outperform those that add more. We plot the overseas expansion of Chinese acquirers, and compare the performance of Chinese acquisitions, within the Greater China region, within the Confucian cultural sphere, and between Asian and the West. In each case, we predict that increasing cultural distance decreases performance. Then, because the Continental European governance system is institutionally more familiar to the Chinese system than it is to the Anglo-Saxon system, we consider the Chinese experience in each of these two systems. Our results largely support our hypotheses built on the partner location performance hierarchy argument, but we also point to the limits of the generalizability of existing literature in understanding the Chinese market.

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Mergers and acquisitions; performance; China; culture; institutions; corporate governance; confucian system; Anglo-Saxon system; Continental European system

Introduction

The Chinese market for mergers and acquisitions is booming¹; in 1990, Chinese acquirers spent \$38 million on mergers and acquisitions, and in 2016 they spent \$661.3 billion.

As the Chinese merger market has grown, so too has the literature on the performance of Chinese mergers and acquisitions (e.g. Peng, Luo, and Sun 1999; Cooke 2006; Peng 2006; Xia, Tan, and Tan 2008; Yang et al. 2011). A number of scholars have looked at the performance of Chinese overseas acquisitions (e.g. Boateng, Qian, and Tianle 2008; Chen and Young 2010) but none, to the best of our knowledge, have considered how the location of the target impacts performance. In other words, little is known if Chinese acquirers can work better with American, European or Asian targets. The purpose of this paper is to address this gap.

We propose a hierarchy of targets in terms of location and performance expectation. Based on the suggestion that international deals are more costly than domestic deals

– because of the liabilities of ‘distance’ (Boeh and Beamish 2012), ‘foreignness’ (Zaheer 1995) and ‘outsideness’ (Johanson and Vahlne 2002) – and the observation that cultural and institutional differences vary, we propose the following ordering of international targets.

First, we suggest that Chinese acquisitions, outside of mainland China, but within the *Greater China Region* – that is, Hong Kong, Macau, and Taiwan – will outperform those outside the region, because acquisitions within the region will present fewer geographic and cultural challenges, and the same institutional challenges that Chinese acquirers will face anywhere outside of China. Second, we suggest that Chinese acquisitions outside of the *Greater China Region*, but within the *Confucian world* – that is, Japan, Korea and Vietnam – will outperform those outside because all the countries in this region share a common Confucian foundation (Miles and Goo 2008), and a social systems that emphasise ‘harmony’ (Alston 1989) and ‘reciprocity’ (Lovett, Simmons, and Kali 1999; Chung and Hamilton 2001). Outside of the Greater China region, in other words, Confucian targets are the next most familiar. Third, we suggest that Chinese acquisitions outside the *Confucian world*, but still within Asia will outperform those in the West, because Asian cultures are more similar to each other – in terms of their collectivist and long-term orientation – than they are to Western cultures – which tend to be short-term focused and individualistic (Hofstede 1984, 2001, 2007). Asian target, in other words, will be more familiar to Chinese acquirers and, therefore, perform better. Finally, we suggest that, in the West, ‘Continental European’ targets will outperform ‘Anglo-Saxon targets’, because while the cultural and geographic distances are high in the case of all Western targets, the governance literature (Weimer and Pape 1999; Cernat 2004; Mueller 2006) suggests that the Chinese corporate governance system is more similar to the Continental European system – employed throughout continental Europe – than it is to the Anglo-Saxon – employed in the English-speaking world (Miles and Goo 2008). Continental targets we suggest will be relatively more familiar, institutionally, to Chinese acquirers.

We test this hierarchy of targets using a sample of 19,766 large (>\$10 m) Chinese acquisitions, announced in the period Jan 1990 - August 2017, and a sub-sample of all 1,542 acquisitions by stock-listed acquirers, for which we could measure performance.

We show that the average Chinese deal adds 3.23% to the market value of the acquiring firm, and that almost 60% of Chinese acquisitions in the sample created value. This is surprising, given that studies using Western samples usually report that 65–85% of mergers and acquisitions fail (McCarthy and Dolfsma 2012). We show that most Chinese acquisitions are domestic, and with good reason: the average domestic deal adds 2.6% to the market value of the acquiring firm. Looking at the international deals we find little evidence to suggest that deals within the *Greater China* region create value, but find that those with the *Confusion Region*, and the wider Asian continent, add value in the way that we would expect. Amongst the Western targets, we report that Chinese acquirers prefer Anglo-Saxon targets to Continental targets, but show that the Chinese do better deals with Continental targets than they do with Anglo-Saxon targets; we report that the Chinese neither create nor destroy value with Continental acquisitions, but destroy value with their Anglo-Saxon acquisitions. We finish our discussion by reflecting on why some parts of the performance hierarchy are supported, while other parts are not, and point to potential future research questions. We make a number of contributions. Firstly, and because we study the impact of target location on acquirer performance, we add to the theory of mergers and acquisitions. Next, and because we study Chinese acquisitions, we contribute to the discussion which has been dominated by ‘case studies and descriptive

statistics' (Lin et al. 2009, 1114), and to a literature which has 'focused ... on the USA and UK' (Moschieri and Campa 2009, 72).

Background

Mergers and acquisitions

An extensive literature documents why mergers might occur (see e.g. Trautwein 1990; Mueller 1985; Weitzel and McCarthy 2011). In one of the earliest classifications, Chatterjee (1986) suggests that mergers and acquisitions are used to create 'operative', 'financial' and/or 'collusive' synergies. Operative synergies are the gains that come from 'increased production and/or administrative efficiencies', financial synergies are the gains that come from 'reductions in the cost of capital', and collusive synergies are the gains that come from 'increased market power' (Chatterjee 1986, 121). Subsequent researchers have refined this basic model (see e.g. Krishnan, Hitt, and Park 2007; Devos, Kadapakkam, and Krishnamurthy 2008); Houston, James, and Ryngaert (2001), for example, splits operative synergies into 'expansionary' synergies, which are the gains that come from an expansion into a new product or regions, and 'cost-cutting' synergies, which are the gains that come from acquisitions which reduce the acquirers (average) costs. And to this model, resource-based scholars have added the gains that come with controlling 'strategic assets' – such as natural, technological, financial and human resources (e.g. Chen 2008) – and international business scholars have made use of Dunning's (1980, 1988, 1993) OLI paradigm, to suggest that foreign acquisitions may also be motivated by 'market seeking' gains – which come with access to foreign markets, and the potential that they offer for the export of domestic products and for an increase in sales (e.g. Buckley et al. 2007).²

The dangers of mergers and acquisitions

Mergers & Acquisitions are thus believed to mostly have benefits. The empirical reality of mergers and acquisitions is, however, somewhat different. After 100 years of research on 'the M&A markets of the USA and UK' (Moschieri and Campa 2009, 72), the impact of a merger on the performance of the acquiring firm is said to be, at best, 'inconclusive' (Haspeslagh and Jemison 1991, 59), and is thought, at worst, to be 'systematic[ally] detrimental' (Dickerson, Gibson, and Tsakalotos 1997, 359). Many mergers are described as failures: Puranam and Singh (1999) suggest that between 65 and 85% of all mergers and acquisitions fail, and that as many as 50–65% are divested within 5 years. Houston, James, and Ryngaert (2001) estimate that only about 60% of predicted cost-cutting synergies, and only about 7% of predicted of revenue-expanding synergies are ever realised. Huge sums of money are lost in the process, and huge amounts of shareholder value destroyed. Moeller, Schlingemann, and Stulz (2005), for example, estimates that shareholders lost '\$216 billion' in the 1990s on mergers and acquisitions (758), and concludes that shareholder would 'have been better off if management had simply burned the cash used to pay for the acquisition' (765).

A large literature suggests that cross-border deals are a particularly troublesome subset of mergers and acquisitions (e.g. Chatterjee and Aw 2000; Eckbo and Thorburn 2000; Rossi and Volpin 2004; Moeller and Schlingemann 2005; Levine and Schmukler 2006; Gozzi, Levine, and Schmukler 2008; Sarkissian and Schill 2017). This literature argues that while any merger

might be subject to ‘unforeseen and insurmountable challenges’ (Child, Faulkner, and Pitkethly 2001), international deal-makers add the liabilities of ‘distance’ (Boeh and Beamish 2012), ‘foreignness’ (Zaheer 1995) and ‘outsideness’ (Johanson and Vahlne 2002) to the performance equation.

Broadly speaking, the ‘liability of distance’ is the costs associated with doing business ‘far away’: distance increases transportation (Capron, Dussuage, and Mitchell 1998) and monitoring costs (Böckermann and Lehto 2003), obstructs the flow of information and increases information asymmetries (Coval and Moskowitz 1999). Distance it reduces market power (Levy and Reitzes 1992) and access to soft information (Hauptman and Hirji 1999). Distance is present, to a varying degree, in most mergers and acquisitions. The liabilities of ‘foreignness’ (Zaheer 1995) and ‘outsideness’ (Johanson and Vahlne 2002), however, are two specific sets of costs associated with cross-border deals. These are the liabilities that come with doing business ‘abroad’: the former can be thought of as the costs of learning a new set of rules – both in a cultural and institutional sense – and the latter can be thought of as the cost of associated with a developing a new network position in a foreign market (Zaheer 2002; Bell, Filatotchev, and Rasheed 2012; Qian, Li, and Rugman 2013). Both liabilities increase transaction costs, complicate communication (Chevrier 2003), reduce the quality of the information transferred (Jaffe, Trajtenberg, and Henderson 1993), create uncertainty (Reus and Lamont 2009), and may lead to situations of ‘them and us’ (Huntington 1993) which, in turn, increases employee turnover (Krug and Hegarty 1997). Both liabilities have been linked to sub-par cross-border performance.

The Chinese merger market

It is well known that Chinese merger market has grown rapidly in recent years. It is also well-known that as it grew the Chinese merger market quickly internationalised (see e.g. UNCTAD 2005; MOC 2006, 2007; Athreye and Kapur 2009; Nicholson and Salaber 2013). Rui and Yip (2008), for example, report that Chinese acquirers spent a total of \$30 billion on foreign acquisitions between 1978 and 2002, but spent \$57.2 billion in 2005, alone, and a further \$73 billion alone in 2006. McCarthy and Dolfsma (2012) also report that the number Chinese outbound acquisitions increased by a factor of 47 between 2000 and 2011.

It is perhaps surprising, therefore, to note that most of the literature on Chinese mergers and acquisitions only ‘us[es] case studies and descriptive statistics’ (Lin et al. 2009, 1114), and that empirical research on the Chinese merger market only started in the late 1990s (see e.g. Peng, Luo, and Sun 1999). Writing in 2011, Yang et al. (2011) counts

a total of six previous papers [that] deal with M&As in China (Peng, Luo, and Sun 1999; Cooke 2006; Peng 2006; Xia, Tan, and Tan 2008; Lin et al. 2009; Chen and Young 2010), [only] three of which use rigorous quantitative methods (Xia, Tan, and Tan 2008; Lin et al. 2009; Chen and Young 2010). (241)

Because of this, there are significant gaps in our understanding of the way in which the Chinese merger market operates, and there is a need for comparative studies (Earley 1989; Peng and Heath 1996; Li and Peng 2008), ‘in order to test or generalise Western findings’ (Yang et al. (2011), 241). Unfortunately, however, such attempted still remain relatively rare (Lu, Tsang, and Peng 2008; Nicholson and Salaber 2013).

The partner location performance hierarchy

This paper addresses to this gap in our understanding, by considering, effectively, the applicability of the literature on cross-border mergers and acquisitions to Chinese acquirers. We reason that differences in language, regulation, currencies, culture and legal systems complicate the performance of an international acquisition, and predict superior performance for domestic deals. International deals which alter fewer of these variables will outperform those that alter more variables. This reasoning leads us to predict a performance ordering of the overseas targets of Chinese acquirers, which we refer to as the partner location performance hierarchy. Table 1 presents an overview of this hierarchy. The intuition is explained below.

Hypotheses

A rich literature suggests that domestic deals should outperform international deals. Theoretically, international deal makers incur the liabilities of ‘distance’ (Boeh and Beamish 2012), ‘foreignness’ (Zaheer 1995) and ‘outsideness’ (Johanson and Vahlne 2002). Empirically a large literature suggests that cross-border deals underperform (e.g. Chatterjee and Aw 2000; Eckbo and Thorburn 2000; Rossi and Volpin 2004; Moeller and Schlingemann 2005; Levine and Schmukler 2006; Gozzi, Levine, and Schmukler 2008; Sarkissian and Schill 2017). Because we have no reason to suggest that Chinese acquirers are any more astute at dealing with these liabilities, we suggest that the existing literature applies. Thus:

H1 – Domestic Chinese M&A deals will outperform international Chinese deals.

While domestic deals are to be preferred to international deals, clearly, not all international deals are equally as complicated. If the liabilities of distance, foreignness and outsideness complicate cross-border mergers and acquisitions (Kogut and Singh 1988), then clearly deals which incur fewer of these liabilities will outperform those that incur more. This reasoning leads to a hierarchy of international destinations. Firstly, we suggest that Chinese acquisitions outside of China, but within the *Greater China Region* – that is, Hong Kong, Macau, and Taiwan – will outperform those outside of the region. Acquisitions within the region, we argue, present Chinese acquirers with fewer geographic and cultural challenges, and the same level of institutional challenges than they will face anywhere outside of Mainland China. Thus:

H2 – M&A deals by Chinese acquirers in the Greater China region will outperform deals outside the region.

Table 1. The partner location performance hierarchy.

Liability	Domestic	International				
		Asian		Western		
		Greater China	Confucian	Asian	Continental	Anglo Saxon
Distance (Geographic costs)	0	0	1	1	2	2
Foreignness (Cultural and Institutional)	0	1	1	2	2	3
Outsidedness (Developing a position)	0	1	1	1	1	1
Total additional liabilities*	0	2	3	4	5	6

*These numbers are, in themselves, meaningless, and arbitrary, and are intended merely to provide a rank indication.

Further, we suggest that Chinese acquisitions outside the *Greater China Region*, but within the so-called *Confucian cultural sphere* – that is, Japan, Korea and Vietnam – will outperform those outside that sphere. Acquisitions within that world, we suggest, will present fewer cultural challenges, because all the countries in the Confucian world are built upon a ‘Confucian’ foundation (Miles and Goo 2008), and share a social systems that emphasise ‘harmony’ – epitomized for instance by the Japanese concept of *wa* (和) – at the group-level (Alston 1989), and ‘relationships’ – epitomised for instance by the Chinese concept of *guanxi* (关系) – at the individual level (Lovett, Simmons, and Kali 1999; Chung and Hamilton 2001; Hitt, Lee, and Yucel 2002). Outside of the Greater China region, in other words, Confucian targets are the next most familiar. Thus:

H3 – M&A deals by Chinese acquirers in the Confucian Region will outperform non-Confucian deals.

Next, we suggest that Chinese acquisitions outside of the *Confucian cultural sphere*, but within Asia, will outperform those outside of Asia. Asian targets, we reason, will present fewer cultural challenges to Chinese acquirers, because Asian cultures are more similar to each other – in their tendencies towards collectivist and in a society fostering a more long-term orientated – than they are to Western cultures – which are more short-term focused and individualistic (Hofstede 1984, 2001, 2007). M&A deals targets, we suggest, therefore, will be more familiar to Chinese acquirers and will be more likely, therefore, to perform better than Western targets. Thus:

H4 – Asian M&A deals by Chinese acquirers will outperform non-Asian deals.

Finally, with respect to Western targets, we suggest that M&A deals by Chinese acquirers involving ‘Continental’ targets will outperform ‘Anglo-Saxon targets’. While the cultural and geographic distances are high in the case of all Western targets, the governance literature (e.g. Weimer and Pape 1999; Cernat 2004; Mueller 2006) suggests that the Chinese corporate governance system is more similar to the Continental European than it is to the Anglo-Saxon (Miles and Goo 2008). In the Anglo-Saxon system – in use throughout the English-speaking world – the firm is conceived as an instrument for creating shareholder value (Weimer and Pape 1999). Ownership is dispersed and shareholders are atomistic, but all shareholders are equally protected (La Porta, de Linanes, and Shleifer 1998). This, and the fact that the stock market is the stick by which performance is gauged, and the stick by which managers are compensated, makes shareholder the most significant stakeholders in the Anglo-Saxon system. By contrast, in the Continental system – in use throughout continental Europe – the firm is considered to be a coalition of various participants, all of whom strive for the continuity of the firm as a whole (Moerland 1995). Ownership is concentrated, for instance in a single family, and employees and debt providers are given a significant say in the ways in which the firm is run. This means that shareholders are important in the Continental systems, but not more important than any of the other stakeholders. Because of this, Continentals firms tend to be focused on stability and continuity, while Anglo-Saxon firms tend to be focused on the creation of short terms gains, and on the distribution of those gains to shareholders (Gelauff and Den Broeder 1996). For Chinese acquirers the latter system – the Continental system – is likely to be more familiar. In the Chinese system the purpose of the firm is to create an inheritance (Miles and Goo 2008). Ownership tends to be concentrated (Claessens, Djankov, and Lang 2000; Carney et al. 2011), often in the hands of a single family, and there

is a high degree of overlap between ownership and management in most Chinese firms (Heugens, van Essen, and van Oosterhout 2009; Zhang and Ma 2009; Ahlstrom, Chen, and Yeh 2010; Peng and Jiang 2010; Schulze and Gedajlovic 2010). The similarity between Chinese and Continental firms on one hand, and the lack of familiarity of Chinese acquirers with the stock market, on the other (Boisot and Child 1996; Keister 1998, 2009; Yiu, Lau, and Bruton 2007; Rui and Yip 2008), which is all important in the Anglo-Saxon world, leads us to suggest that Continental targets will present Chinese acquirers with fewer challenges than Anglo-Saxon targets. Thus:

H5 – M&A deals by Chinese acquirers of Continental targets will outperform deals involving Anglo-Saxon targets.

Methods

Sample

We test these hypotheses underpinning the partner location performance hierarchy using a data from the *Thomson Reuters SDC*. We refine it to include all deals: (1) announced between Jan 01, 1990 and July 31, 2017; (2) with transaction values above US\$10 million. We only include deals: (3) for 100% of the target firm's shares; and (4) deals which do not involve recapitalisation, a repurchase of own shares, or a spin-off to existing shareholders. Doing so, we create an initial sample of 19,766 acquisitions.

Target location

Using the location of the firms involved, we obtain a number of indicator variables.

First, and to test the first hypothesis – which suggests that domestic Chinese acquisitions will outperform international Chinese acquisition – we create: (1) a *China* indicator that identifies Chinese acquirers (*A_China*) and Chinese targets (*T_China*); (2) an *International* indicator that differentiates between domestic Chinese deals and international Chinese deals.

Then, to test the partner location performance hierarchy of international deals, we use a number of indicators. Firstly, a *Greater China Target* dummy variable identifies Chinese acquisitions in Hong Kong and Macau, and Taiwan with a 1, and other international acquisitions with a 0. Secondly, a *Confucian Target* dummy variable identifies all international targets outside the *Greater China Region*, but within the Confucian cultural sphere – that is, in Japan, South Korea, and Vietnam – with a 1, and other international acquisitions with a 0. Thirdly, an *Asian Target* dummy variable identifies targets within Asia, but outside the *Greater China and Confucian Regions* – that is, Brunei, Cambodia, East Timor, Indonesia, Laos, Malaysia, Mongolia, Myanmar, the Philippines, Singapore, Thailand – with a 1, and other international acquisitions with a 0. Finally, an *Anglo-Saxon* dummy variable identifies all acquisitions in Australia, Canada, Ireland, New Zealand, the United Kingdom and the United States, as well as their dependencies (such as the Falkland and Guam) with a 1, and all other acquisitions outside of *Asia* with a 0, and a *Continental* dummy variable identifies all acquisitions in Continental Europe, minus Ireland and the UK, and their dependences (such as Gibraltar and the Isle of Man) with a 1, and other acquisitions outside of *Asia* with a 0.

Deal performance

Following the majority of merger performance studies (see Zollo and Meier 2008 for an excellent review), we calculate performance using an event study methodology. In an event study, a pre-event 'estimation window' is defined, and historical data is used to forecast the firms' normal' stock price at a future date; this is an expectation of how the firm's stock should have been priced, had the event not occurred. Comparing this 'forecast' with 'actual' data on the firm's stock price, after the event, provides an indicator of the firms' abnormal' return; this is the change in the firm's value, above or below the firm's expected value, which is attributable to the event. Summing the abnormal returns over a period of time, known as an 'event window', leads to an expression as 'cumulative abnormal returns'. Algebraically, the abnormal return is calculated by identifying the difference between the actual returns and normal returns of the acquiring firms. Abnormal return of a security i :

$$AR_{i,t} = R_{i,t} - E[R_{i,t}] \quad (1)$$

Here, $R_{i,t}$ is the actual return and $E[R_{i,t}]$ is the estimated or normal return to the acquiring firm. Equation (2) displays how the normal return is calculated;

$$E[R_{i,t}] = \alpha_i + \beta_i R_{m,t} + \varepsilon_{i,t} \quad (2)$$

where α_i is the intercept coefficient, β_i is the slope, $R_{m,t}$ the formation of the used benchmarks, and $\varepsilon_{i,t}$ is expected to be equal to 0. Summing the abnormal returns to the firm, within a predefined event window, produces *cumulative abnormal returns* (CAR):

$$CAR_i[t_1, t_2] = \sum_{t=t_1}^{t_2} AR_{i,t} \quad (3)$$

We calculate CAR to the acquiring firm using the standard 250 day estimation window – measured from 295 days before each event to 45 days before it $[-295, -45]$ – and the standard one $[-1, +1]$ and five day event window $[-5, +1]$. We follow the precedence of measuring CARs before the announcement to include pre-bid run-ups (Schwert 1996) and afterwards to observe the effect of the event. If a merger was announced on a non-trading day, we code the subsequent trading day as the official announcement day.

We retrieve the stock-market data necessary to complete an event study using *Datastream*. Data availability, at this point, reduces the sample of available deals to 1542 deals.

Performance controls variables

A number of factors are known to impact deal performance (see King et al., for a review). We thus control for: (1) the per cent of the deal financed by cash (*Per cent Cash*) and stock (*Per cent Stock*) because Heron and Lie (2002) shows that cash-financed deals outperform stock-financed deals; (2) *Acquirer Size*, measured in thousands of employees, because Moeller, Schlingemann, and Stulz (2004) show that larger acquirers make worse deals; (3) the *Deal Size*, because Moeller, Schlingemann, and Stulz (2004) show that larger deals perform poorly. All the necessary data is collected from *DataStream*, and / or the SDC. We test each of the control variables for normality, and employ logs of all variables that fail the test. Table 2 provides a descriptive overview of the data that we use in this study. All variables are winsorized, between 0.01 and 99.99%, to minimise the effect of possibly spurious outliers.³

Table 2. Pairwise correlations and descriptive statistics.

	Mean	S.D.	Min	Max	1	2	3	4	5	6	7	8	9	10	11	12
1 CARs	0.05	0.11	-0.28	0.37	1.00											
2 Domestic Target	0.93	0.26	0	1	0.08 [0.00]	1.00										
3 Greater China Target	0.02	0.12	0	1	-0.07 [0.00]	-0.44 [0.00]	1.00									
4 Confucian Target	0	0.05	0	1	0.03 [0.19]	-0.17 [0.00]	-0.01 [0.80]	1.00								
5 Asian Target	0.01	0.08	0	1	0.01 [0.56]	-0.27 [0.00]	-0.01 [0.69]	0.00 [0.88]	1.00							
6 Anglo Saxon Target	0.03	0.16	0	1	-0.06 [0.03]	-0.60 [0.00]	-0.02 [0.38]	-0.01 [0.74]	-0.01 [0.60]	1.00						
7 Continental Target	0.01	0.12	0	1	-0.03 [0.21]	-0.42 [0.00]	-0.01 [0.54]	-0.01 [0.81]	-0.01 [0.71]	-0.02 [0.41]	1.00					
8 Per cent Cash	3.55	0.75	-4.2	4.61	-0.09 [0.00]	-0.14 [0.00]	0.04 [0.09]	0.02 [0.48]	0.05 [0.05]	0.10 [0.00]	0.04 [0.06]	1.00				
9 Per cent Stock	4.4	0.25	1.59	4.61	0.06 [0.03]	0.07 [0.00]	-0.08 [0.00]	0.00 [1.00]	-0.11 [0.00]	-0.02 [0.36]	0.00 [0.89]	-0.15 [0.00]	1.00			
10 Acquirer Size	7.35	1.45	0	13.14	-0.04 [0.11]	-0.10 [0.00]	-0.04 [0.08]	0.01 [0.74]	0.06 [0.02]	0.12 [0.00]	0.01 [0.59]	0.10 [0.00]	0.00 [0.87]	1.00		
11 Deal Size	4.71	1.41	2.3	9.8	0.11 [0.00]	0.05 [0.03]	-0.07 [0.00]	-0.01 [0.73]	-0.01 [0.64]	0.03 [0.25]	-0.06 [0.01]	-0.18 [0.00]	0.13 [0.00]	0.16 [0.00]	1.00	
12 Year	2012.79	3.48	1995	2017	0.02 [0.54]	0.05 [0.05]	-0.10 [0.00]	-0.05 [0.03]	-0.06 [0.01]	0.03 [0.24]	0.05 [0.02]	-0.13 [0.00]	-0.05 [0.02]	-0.04 [0.09]	0.10 [0.00]	1.00

Estimation

We consider the impact of partner location using OLS techniques. In all estimations we cluster, at both the targets and acquiring industry, according to Froot (1989) and Wooldridge (2002), using both firms *Standard Industrial Classification* (SIC) codes, to allow for industry effects. We also include year dummies, to account for year specific effects. We also adjust all standard errors for heteroskedasticity, using the Huber (1967) and White (1980) sandwich estimator of variance. Finally, and before interpreting the results, we confirm that multi-collinearity is not an issue, using a variance inflation factor (VIF) test (Hair et al. 1992).

Results

The Chinese merger market

Figures 1, 2 and Table 3 report the growth and shape of the Chinese merger market. Figure 1 illustrates the near exponential nature of the growth in the Chinese merger market; from 2 deals in 1990, worth \$38 million, to 3261 deals in 2016, worth \$661.3 billion. Figure 2 provides a breakdown in the composition of the Chinese merger market. It reports that, despite the huge growth in the market, the willingness of the Chinese to internationalise remains low; in total, 91.4% of Chinese deals are domestic. Table 3 looks at the location of Chinese acquisitions that cross borders. It reports that 2.7% of Chinese deals ($n = 528$) or 30% of Chinese international deals, involve targets in the Greater China region. Confucian targets ($n = 613$) account for 35% of Chinese overseas acquisitions, and Asian targets ($n = 740$) account for 42% of Chinese overseas acquisitions. Outside of Asia, Anglo-Saxon targets ($n = 566$) account for the lions-share of the overseas acquisition (32%), with the United States ($n = 241$) and Australia ($n = 167$) standing out as popular non-Asian destinations, while Continental Europe ($n = 253$) accounts for 14% of Chinese overseas acquisition, with Italy

Figure 1. The emergence of the Chinese merger market.

Figure 2. A break down of the Chinese merger market.

($n = 44$), Germany ($n = 42$), and the Netherlands ($n = 22$) as the most favoured destinations.

Partner types and performance

Models 1–6, in Table 4, reports on how the choice of partner impacts performance. We report results using the $[-5, +1]$ event window; the results using the $[-1, +1]$ window are consistent and available from the authors upon request.

Models 1–4 consider the specifics of Chinese acquisitions within Asia. *Model 1*, for example, tests the hypothesis that Chinese domestic deals outperform international deals. A positive and significant coefficient for the *Domestic Target* indicator provides support for hypothesis 1; domestic deals perform 2.6% better than international deals. *Model 2* adds the *Greater China Target* indicator to test the hypothesis that deals within the *Greater China Region* will outperform deals outside of the region, for reasons of cultural closeness. A negative and significant coefficient on the *Greater China* dummy forces us to reject hypothesis 2. *Model 3* adds the *Confusion Target* indicator to the equation, to test hypothesis 3 that Chinese acquisitions within the Confusion world outperform those outside the region. A positive and significant coefficient provides supports for that hypothesis. Lastly, *Model 4* adds the *Asian Target* indicator, to test the hypothesis that Asian targets outperform non-Asian targets; a positive and significant coefficient allows us to support hypothesis 4.

Next, *Models 5–7* consider the specifics of Chinese acquisitions in the West, to test hypothesis 5 that Chinese acquirers will be able to create more value with targets based in Continental European governance systems, than targets in the Anglo-Saxon system. *Model 5* shows that Chinese Anglo-Saxon acquisitions destroy value, and *Model 6* shows that Chinese Continental European acquisitions do not create value. *Model 7* confirms these effects, when both indicators are included, and thus supports the suggestion that Chinese acquirers can do better deals in the Continental governance system than the Anglo-Saxon system.

Table 3. The global distribution of Chinese targets.

	Number of deals	Per cent	Cumulative
China Domestic	18,015	91.4	
<i>Greater China Region</i>	528	2.7	94.1
Hong Kong	495		
Taiwan	28		
Macau	5		
<i>Confucian Region</i>	85	0.43	94.5
Japan	29		
South Korea	41		
Mongolia	9		
Vietnam	6		
<i>Asian Continent</i>	127	0.64	95.1
Indonesia	13		
India	8		
Laos	1		
Malaysia	16		
Pakistan	7		
Philippines	5		
Singapore	75		
Sri Lanka	2		
<i>Anglo-Saxon</i>	566	2.86	98
Australia	167		
Canada	80		
New Zealand	14		
United Kingdom	64		
United States	241		
<i>Continental</i>	253	1.28	99.28
Austria	3		
Belgium	9		
Cyprus	1		
Czech Republic	3		
Denmark	4		
Finland	5		
France	36		
Germany	42		
Greece	3		
Hungary	3		
Ireland-Rep	3		
Italy	44		
Luxembourg	7		
Malta	1		
Netherlands	22		
Norway	10		
Poland	1		
Portugal	3		
Russian Fed	14		
Serbia	4		
Spain	16		
Sweden	8		
Switzerland	10		
Other	200		100
Total	19,766		100

Discussion

Main findings

A number of the findings presented above fit with our expectations / predictions, but some findings require additional consideration. Our results suggest:

- (1) The Chinese merger market is booming and creating value

Table 4. Results.

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Domestic target	0.026*** (0.007)	0.017* (0.009)	0.021*** (0.008)	0.022** (0.009)			
Greater China target		-0.044** (0.022)	-0.040* (0.021)	-0.039* (0.021)			
Confucian target			0.098** (0.066)	0.099** (0.066)			
Asian target				0.013* (0.034)			
Anglo-Saxon target					-0.031** (0.014)		-0.031** (0.014)
Continental target						-0.020 (0.022)	-0.021 (0.022)
Per cent stock finance (log)	0.014 (0.013)	0.013 (0.013)	0.013 (0.013)	0.013 (0.014)	0.015 (0.013)	0.015 (0.013)	0.015 (0.013)
Per cent cash finance	-0.009** (0.004)	-0.009** (0.004)	-0.009** (0.004)	-0.009** (0.004)	-0.009** (0.004)	-0.010*** (0.004)	-0.009** (0.004)
Acquirer size	-0.003 (0.002)	-0.004* (0.002)	-0.004* (0.002)	-0.004* (0.002)	-0.003* (0.002)	-0.004* (0.002)	-0.003* (0.002)
Deal size	0.008*** (0.003)	0.008*** (0.003)	0.008*** (0.003)	0.008*** (0.003)	0.009*** (0.003)	0.008*** (0.003)	0.008*** (0.003)
Acquirer industry Clusters	Included	Included	Included	Included	Included	Included	Included
Target industry Clusters	Included	Included	Included	Included	Included	Included	Included
Year dummies	Included	Included	Included	Included	Included	Included	Included
Constant	-0.022 (0.062)	-0.004 (0.062)	-0.008 (0.062)	-0.012 (0.064)	-0.001 (0.062)	0.003 (0.063)	-0.001 (0.062)
Observations	1,542	1,542	1,542	1,542	1,542	1,542	1,542
R ²	0.025	0.027	0.029	0.029	0.023	0.022	0.024

Notes: Standard errors in parentheses.

*** $p < 0.01$; ** $p < 0.05$; * $p < 0.1$

The Chinese made 19,766 large (>\$10 m) acquisition between Jan 1990 and August 2017, and the growth has been near exponential. In 1990, Chinese acquirers made two large mergers and acquisitions; in 2016, they made 3261 large acquisitions. Looking at the sub-sample for which we could calculate performance, we find that the Chinese are, on average, creating value with their acquisitions. The average Chinese acquisition in the sample added 3.23% to the market value of the acquiring firm, and that almost 60% of Chinese acquisitions in the sample created value; Western samples usually report that 65–85% of acquisitions fail (McCarthy and Dolfsma 2012).

(2) There is mixed support for the proposed partner location performance hierarchy

A number of our expectations regarding the proposed performance hierarchy were confirmed, but a number of the results were quite unexpected. We found:

(a) Domestic deals outperform international deals

We expected and found that domestic deals outperformed international deals. The majority of Chinese acquisitions (91%) are domestic, and the evidence shows that domestic acquisitions create value; on average, domestic acquirers add +2.6% to the market value of the firm. This finding fits with the wider literature, which shows that domestic deals perform better (Chatterjee and Aw 2000; Eckbo and Thorburn 2000; Moeller and Schlingemann 2005).

(b) Acquisitions in the Greater China Region destroy value

We expected that acquisitions in the Greater China region would be the next best thing to a domestic acquisition, but we find that these acquisitions actually destroy value. While understanding why this is true requires additional research, it might be that targets within the Greater China region are not sufficiently different to those on Mainland China to generate the anticipated benefits that justify incurring the costs that come with the liability of distance, foreignness and outsideness.

(c) Confucian and Asian Targets add value

We expected and found that both Confucian and Asian targets would add value to Chinese acquirers. Our results suggest that the average Confucian target adds 9.8% to the value of the market value of the acquiring Chinese firm. This seems to suggest that Chinese acquirers which step outside of the Greater China region, but remain within the Confucian world, add the most value. By contrast, Chinese acquisitions outside of the Confucian world, but within Asia, add value, but only add 1.3% to the acquirer, on average. Confucian targets, in other words, seem to be sufficiently different to justify internationalisation, but sufficiently similar to be easily integrated.

(d) Anglo-Saxon targets perform badly, and Continental targets are unspectacular

Lastly, we expected that when cultural and geographic distances were equally high, Western targets with lower institutional hurdles would not only be preferred, but would demonstrate superior performance. We somewhat support this suggestion. Chinese acquisitions of Anglo-Saxon targets destroy value; the average Anglo-Saxon acquisition reduces the value of the acquiring firm by 3.1%. Chinese Continental European acquisitions perform better, but they neither create nor destroy value. We thus support the hypothesis, but find that while the Chinese do the worst with Anglo-Saxon targets, they don't do much better with Continental European targets.

Together, these findings provide support for only part of the proposed performance hierarchy. Our failure to support the entire hierarchy supports the suggestion that China is 'different' (Lin et al. 2009), and that Chinese mergers and acquisitions are significantly different (Peng and Heath 1996), insofar as the expectations derived from the literature, typically based upon the study of US acquirers (e.g. Hitt et al. 2001; Moschieri and Campa 2009), is not fully generalizable to Chinese firms. We strongly support the calls, therefore, for additional comparative research (e.g. Lin et al. 2009; Yang et al. 2011; Nicholson and Salaber 2013) to further test or to generalise Western findings, and to develop theories for emerging economies (Earley 1989; Tsui 2007).

Limitations

Our findings are subject to a number of important limitations. Firstly, we only consider large acquisitions, which we define to mean greater than \$10 million. Such a restriction is put in place because smaller deals are known to perform differently (see e.g. Weitzel and McCarthy 2011), and because the convention in the merger literature is to implement a minimum restriction. In doing so, however, the generalizability of our results becomes unclear. Secondly, we do not consider the underlying motives behind the merger, which others have suggested are critical to understanding merger performance (Shrivastava 1986; Bower 2001; Javidan et al. 2004; Schweizer 2005). It may be, however, that Asian targets outperform Western targets, not because of cultural similarities and differences, but because there are more

cost-cutting acquisition in Asian, and more revenue-expanding acquisition in the West. Additional research is required, we suggest, to investigate this possibility.

Conclusions

The purpose of this paper was to document the emergence of the Chinese merger market, and to consider how the choice of partner – in terms of physical location – impacts performance.

Building upon a theoretical literature which suggest that international deals are more costly – in terms of the liabilities of ‘distance’ (Boeh and Beamish 2012), ‘foreignness’ (Zaheer 1995) and ‘outsideness’ (Johanson and Vahlne 2002) – we argued, firstly, that domestic Chinese acquisitions will outperform international deals and, secondly, that those international deals which incurred more of these liabilities would underperform those that incurred less. Effectively, therefore, the aim of this paper was to answer the calls of scholars looking to test the generalizability of the existing literature to emerging market firms (e.g. Earley 1989; Tsui 2007; Lin et al. 2009; Yang et al. 2011; Nicholson and Salaber 2013).

Our results demonstrate that: (1) unlike Western firms, Chinese acquirers are creating value through mergers and acquisitions; (2) the literature only imperfectly applies to Chinese acquirers. We find that in most cases the performance of Chinese overseas acquisitions support the proposed performance hierarchy, but certainly not in all cases. Our failure to support the entire hierarchy supports the suggestion that China is ‘different’ (Peng and Heath 1996; Lin et al. 2009), and that the existing literature is not fully generalizable. In doing so, we create a number of rich research opportunities for scholars looking to dig deeper into the largely unexplored field of linking Western literature to Chinese mergers and acquisitions.

Notes

1. See McCarthy, Dolfsma, and Weitzel (2016). While technically and legally different, terms like ‘merger’, ‘acquisition’, and ‘takeover’ are used interchangeably. Following the convention, we describe merger and acquisition waves as merger waves. We define the Chinese mergers market, furthermore, as the set of deals that involve Chinese firms.
2. Rich literatures consider which of these factors contribute the most to merger performance (e.g. Houston, James, and Ryngaert 2001; Devos, Kadapakkam, and Krishnamurthy 2008) and if these factors apply to emerging market firms (e.g. Li 2007; Dunning and Lundan 2008; Rui and Yip 2008; Athreye and Kapur 2009; Gubbi et al. 2010; Sun et al. 2012).
3. Winsorizing is a technique for dealing with the effects of possibly spurious outliers. By winsorizing between 0.01 and 99.99%, we set all data below the 0.01th percentile equal to the 0.01th percentile, and all data above the 99.99th percentile equal to the 99.99th percentile. The estimators that this creates are more robust to outliers, and by winsorizing the data, we can make use of the full set.

Disclosure statement

No potential conflict of interest was reported by the authors.

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