

EUROPEAN CROSS-BORDER MERGERS AND ACQUISITIONS- REALITIES AND PERSPECTIVES

Vancea Mariana

Universiy of Oradea Faculty of Economics

This paper analyses the impact of the economic and financial crisis on merger and acquisition activity in Europe and the latest trends manifested on the cross-border merger and acquisition market involving European companies. Thus, a first objective of this research is to reveal the evolution of the European cross-border merger and acquisition activity in terms of dynamics, volume and structure. Another objective of this research is to reveal the short and medium term perspectives on mergers and acquisitions in Europe. Thus, under the continuous economic recovery of the European countries and the other worldwide economies, the recovery of financial markets and the growth of corporate profits, we shall witness an intensive cross-border merger and acquisition activity in Europe. The expansion engine of these operations seems to be represented by the emerging economies. This research is based on a systematic, logical and comparative analysis of scientific literature and statistical data regarding the cross-border mergers and acquisitions that involve European companies in recent years. This paper is part of the doctoral thesis "Mergers and acquisitions- strategies of growth and development of enterprises. European and national particularities", coordinated by professor Ph.D. Alina Bădulescu from University of Oradea, Faculty of Economics. The doctoral research is supported by The Sectorial Operational Program for Human Resources Development 2007-2013, Contract POSDRU 59/1.5/S/1- "Romanian researchers through modern and efficient doctoral programs".

Keywords: cross-border mergers and acquisitions, firm strategy, external growth, economic and financial crisis, economic recovery

JEL Codes: F23, M10, M16

Introduction

This paper is part of the doctoral thesis "Mergers and acquisitions- strategies of growth and development of enterprises. European and national particularities", coordinated by professor Ph.D. Alina Bădulescu from University of Oradea, Faculty of Economics. The doctoral research is supported by The Sectorial Operational Program for Human Resources Development 2007-2013, Contract POSDRU 59/1.5/S/1- "Romanian researchers through modern and efficient doctoral programs".

In the light of recent events that took place on the global economic scene, this paper intends to analyze the impact of economic and financial crisis on merger and acquisition (M&A) activity in Europe and the recent trends shown on the cross-border activity that involved European companies. Thus, in the first part we revealed some aspects regarding the literature on cross-border M&As. The next part deals with a recent analysis of the European activity evolution on cross-border M&As in terms of dynamics, volume and structure. The fourth part of this paper presents the short and medium term perspectives on M&As in Europe. Finally, there are some conclusions drawn from the research that was conducted.

Research methodology

This research is based on a systematic, logical and comparative analysis of scientific literature and statistical data regarding the cross-border M&As that involve European companies in recent years. Thus, we carried out a quantitative analysis revealing the impact of the economic and

financial crisis on M&A activity in Europe and the latest trends manifested on the cross-border merger and acquisition market involving European companies.

A brief review of the literature on cross-border mergers and acquisitions

In the literature, several studies have examined the field of cross-border M&As. Thus, some researches focused on the macroeconomic determinants of cross-border activity (Neto, Brandão și Cerqueira 2010: 21-57; Manchin 2004: 4; Rossi and Voplin 2004). Martynova and Renneboog (2006: 3-4) or Evenett (2003: 443,445) analysed cross-border M&As since 1990s, period that represented the first truly international merger wave, one of its characteristics being the large the share of cross-border activity in the total volume of M&A. Another research area, in cross-border M&As, is represented by their effects on the corporate performance and on shareholders' value creation (Goergen and Renneboog 2004: 9-45; Gugler, Mueller Yurtoglu and Zulehner 2003: 625-653; Moeller and Schlingemann 2003: 533-564). They discovered that the performance of cross-border deals is lower than in the case of domestic operations.

The impact of economic and financial crisis on European cross-border mergers and acquisitions and recent trends

After a five-year period of continuous growth of merger and acquisition activity, touching the peak in 2007, the European M&As have recorded a downward trend since 2008 due to economic and financial crisis. European economy, as well as other world economies, has been seriously affected by economic recession and financial markets turmoil. Economic and financial crisis has spread rapidly throughout the world, reflecting the interdependence of economies. The year 2008 marked the end of a four-year cycle of steady worldwide growth, in Europe too obviously, which reached climax in 2007 with a value volume of cross-border M&As never seen before. The increase of M&As between 2004 and 2007 was favoured by sustained growth of worldwide economy, liberalization of trade and investment regimes and the adoption of large-scale internationalization strategies by many transnational corporations.

The recession that began in 2008 has forced many potential acquirers to change their expansion plans by means of acquisition. Acquirers wishing to continue the taking-over process were to find out that the access to finance was severely affected. Many bidders who have signed agreements with target companies have sought to renegotiate the transaction or waive it. Thus, many transactions were void. However, as often happens in times of recession, companies with large capital provisions have taken advantage of the opportunities arising on the merger and acquisition market. The year of 2009 recorded the lowest level of merger and acquisition activity, both in terms of their value and number. Europe was severely affected by this recession, and within it, the European Union whose companies were major acquirers, but also main targets on the global market of M&A. The EU registered a pronounced decrease related to this activity. This reflects the strong economic relations that exist, on the one hand, between the European Union and the rest of the world, and on the other hand, between the Member States of the Union. The longest and deepest economic recession in the history of the European Union economy, as it is characterized by the European Commission in the economic forecast of 2009 (European Commission 2009:7), resulted in a notable decline of trade and investment flows between the EU and the world, but also among the Member States.

Diminishing the profits of companies and the stock market drop had severely decreased the value and number of cross-border M&As. At the same time, the decrease of demand for goods and services has prompted companies to restrict their investment plans abroad, both through M&As and Greenfield investments, although the latter declined since 2009. The decrease in cross-border M&As has contributed most significantly to the decline of foreign investment flows in 2009, which decreased by 34% worldwide (65% in value), compared to a 15% decrease in the number

of greenfield investment (UNCTAD 2010a:9). The global crisis reduced the funding available for FDIs and merger and acquisition operations.

According to UNCTAD statistics, the global cross-border M&As in 2008 declined by 30.9% to \$706.5 billion compared to the record level registered in 2007 of \$1,022.7. The decline was more pronounced in 2009, therefore the amount of worldwide cross-border M&As had declined by 64.6% compared to the previous year, reaching only \$249.7. The crisis impact on cross-border M&As is obvious, as seen by different regions and economies. Among developed economies, Europe, and especially the **EU-27** economy (which weighs significantly in the total of merger and acquisition activity across Europe) was seriously affected. Thus, net sales in developed Europe cross-border activity declined by 51% both in 2008 compared to 2007 and 2009 compared to 2008 and they reached 133,871 billions \$ in 2009. EU economy faced a 52,3% decline in net sales in 2008 compared to the peak year 2007, respectively 53,7% in 2009 compared to 2008 and reached 116,226 billions dollars, which reflected an emphasis of the recession this year. In 2008 the collapse of M&As that had as target EU companies was more pronounced compared to the one recorded worldwide (30.9%) and by the group of developed countries (34.8%). In 2009, all worldwide regions and economies were badly affected and the downward trend generalised even in countries that had not been affected in the previous year (e.g. in U.S. mergers and acquisitions of companies have continued to grow in 2008 by 37.8% compared to 2007, but in 2009 they have decreased by 82.3%).

Regarding the purchases performed by developed Europe's corporations, these dropped by 36,9% in 2008 compared to 2007, the decline being more pronounced in 2009 when purchases declined by 71,3% compared to 2008, summing up only 102,709 billions dollars. Net purchases realised by EU companies, initially dropped by 42,9%, the decline being more pronounced in this case than for the group of developed countries whose acquisitions have decreased by 32,5% or for Japan whose purchases increased by 85,7%, but less pronounced than in the case of the U.S. whose acquisitions have decreased by 60,9%. In 2009 net purchases realised by UE corporations fall out by 70,7% compared to the previous year at 89,694 billions dollars and the decrease in was even more pronounced than in USA (-66,1%) or Japan (-69%).

Transition economies in South-Eastern Europe were also severely affected, although the amount of their value was much lower than that of developed countries. Practically, on the international merger and acquisition market, the companies located in these countries have played a predominant role of targets of these operations. In terms of cross-border merger and acquisition value in South-Eastern Europe and CIS, in 2008, decreased by 33% compared to the previous year, so that from \$20,337 billion it reached \$7,125 billion. In 2009, the decline was more pronounced, summing up 65%, so that net sales reached only 896 millions dollars. This severely decrease was due to the decline in acquisitions made by the EU-15 companies, which were the main acquirers in the area. Actually, in the last years, firms from UE-15 concentrated their attention on the new member states UE-12 and on the other emerging countries of Europe.

The extent of the decline in cross-border activity was more pronounced in the old member states than in the new ones. The main European bidders came from UE-15 (Great Britain, France, Germany, Italy, Spain), but the global recession produced dramatic changes in the major investors hierarchy. Thus, Great Britain had to cede the leader position in cross-border purchases to France. On the other hand, UE-15 countries represented main targets in european cross-border activity, and the top five countries by net sales value includes Great Britain, Netherlands, Spain, Germany and France. Still, these countries were most affected by the recession, but still Great Britain kept his leader position.

Two thirds of cross-border M&As have involved developed countries, but the share of developing and transition savings, as targets of such transactions, had increased from 26% in 2007 to 31% in 2009 and 34.4% in 2010. European companies were the targets in about 42% of cross-border M&As in the peak year 2007, their share decreasing thereafter up to 35% in 2010.

As purchasers, in 2007 the share of European bidders was 44,4% in the total cross-border volume and it fell to 34,6% in 2010 (UNCTAD 2010:4).

If we look at the EU share in the global cross-border sales, we can observe that the share declined from 52% in 2007 to 47% in 2010 (we mention that the data for 2010 covers only the first five months) and the share of purchases declined from 53% in 2007 to 15% in 2010. USA improved its position both in terms of sales and purchases in the global cross-border activity and Japan improved its position especially regarding purchases. However, UE as entity maintained its global leader position in terms of sales and purchases and is still occupying a place at the forefront globally.

Table no 1. The evolution of UE share in the total volume of cross-border mergers and acquisitions, compared to USA and Japan (in billions of dollars and %)

Region/Economy	Net sales				Net purchases			
	2007	2008	2009	2010	2007	2008	2009	2010
World	1022,7	706,5	249,7	125,2	1022,7	706,5	249,7	125,2
EU								
Value	527,7	251,1	116,2	58,8	537,8	306,7	89,6	18,6
Share of total	52	36	47	47	53	43	36	15
USA								
Value	164,9	227,4	40,0	29,1	179,8	70,1	23,7	50,8
Share of total	16	32	16	23	18	10	10	41
Japan								
Value	16,5	9,2	-5,7	2,5	30,3	56,3	17,4	11,2
Share of total	2	1	...	2	3	8	7	9

Source: UNCTAD Statistics and own calculations:

http://www.unctad.org/sections/dite_dir/docs/wir2010_anxtab_9.pdf;

http://www.unctad.org/sections/dite_dir/docs/wir2010_anxtab_10.pdf;

Regarding sectorial distribution of European cross-border activity, the impact of the crisis across sectors resulted in a shift in their relative weight in the total value of M&As. The manufacturing industry was the most affected, but the decline was felt also by the primary sector and services (financial services or business services, have recorded a sharper decline) (UNCTAD 2010a: 11). Despite these adverse evolutions in 2008 and 2009, in the first half of 2010, on the cross-border merger and acquisitions market that involved European companies was outlined a revival of operations and a restart of an upward trend. Thus, the value of cross-border M&As increased by 36% in first five months of 2010 (UNCTAD statistics provide data only until May 2010), compared to the same period of the last year. This reflects the upward trend following the economic growth in the countries of target and acquirer companies, corporate profitability growth and share price growth.

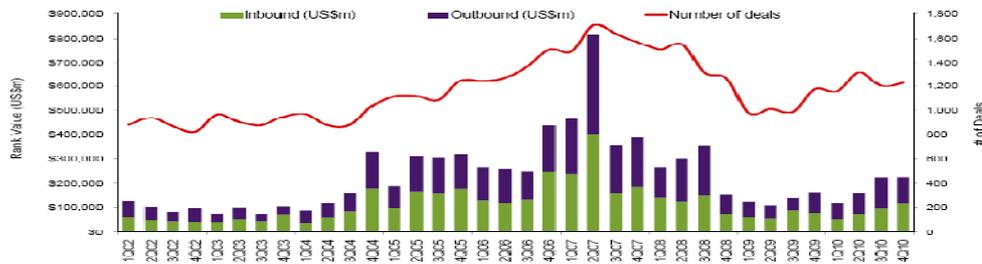


Figure no 1. Evolution of European cross-border mergers and acquisitions

Source: Thomson Reuters, *Mergers and Acquisitions Review, Financial Advisors, 2010: 9*, https://online.thomsonreuters.com/DealsIntelligence/Content/Files/Global_MA_%20Financial_Review.pdf

If UNCTAD statistics provide for the moment data on M&A only for the first half of 2010 (from which general trends can be inferred), the Thomson Reuters company has published a report on merger and acquisition activity for the year 2010. Thus, according to the report drafted by Thomson Reuters company (2010: 9) the year 2010 marked an increase in merger and acquisition activity so that cross-border M&As involving European companies summed up \$716.1 billion, which represented a growth by 35.8% compared to 2009. After a slight decrease in the value of cross-border mergers and acquisitions during the first quarter of 2010, starting with the second quarter and particularly in the second half of 2010, the value of cross-border transactions began to significantly increase. This was due mainly to European corporations, whose acquisitions had increased compared to 2009 by 57.2% to \$388.1 billion.

Short and medium term prospects of cross-border merger and acquisition activity

After the worldwide economy has experienced a deep recession, since 2010 the economic recovery (reflected by the increased production and foreign trade) included most economies, while the EU along with other major economies of the world acted to restore the worldwide financial stability and economic growth. In this context, the prospects for merger and acquisition activity on short and medium term are optimistic, being reinforced by the favourable development recorded in 2010. UNCTAD estimates, in *World Investments Prospects Survey 2010-2012* (2010b: 4), indicate a medium-term optimism related to the business field. Restructuring in the field of industry and privatizing companies (it is expected a new round of privatization within the European countries with large public debt) that were saved during the worldwide turmoil will generate further opportunities in terms of cross-border mergers and acquisitions for corporations.

According to the latest forecast made by the International Monetary Fund, the recovery from recession in Europe continues to make headway but is still modest. However, if the developed countries in Europe record a smaller growth, for 2011 and 2012 being projected increases by 1.7% respectively 1.9%, the emerging states in Europe present a more accelerated growth by 3.7% in 2011 and 4% in 2012 (IMF 2011: 67). Taking into account this scenario, we believe that 2011 will reflect a more dynamic evolution of merger and acquisition activity in Europe and, thus, a continuation of the upward trend started in 2010. This will be encouraged by the fact that the financial situation of corporations has a tendency to improve (corporate profits began to grow), the stock market has increased compared to 2009 and corporate and industrial restructuring is creating new opportunities for acquisitions, especially for the corporations in the emerging countries. By the year 2009, if companies were facing great difficulty in financing M&As, since 2010, the demand for loans to finance external growth operations has increased, fueled by an attenuation of credit standards. The investigation conducted by the European Central Bank in January this year reflects the fact that financing M&As still had a positive impact on the

corporate loan demand, which reflects the desire of companies to resume expansion projects (ECB 2011:7).

In Europe is expected a growth of the operations performed by corporations located in developing countries that are increasingly eager to expand on developed markets. Within the European Union, although the economic recovery is still fragile and unevenly distributed among the Member States, yet this will encourage the corporations in developed countries to expand, in order to enhance the competitive position and access to new markets. Although the developed economies of Europe remain the place where most transactions related to M&As are carried out, there is an increase in the share of these transactions within the European transition economies. We notice a decrease in interest for developed countries concerning M&As and an increase in interest for companies located in transition economies. According to UNCTAD (2010b:12) the top destination regions for investments such as M&As are South-East Asia, the EU-15, North America, Latin America and the Caribbean region, the new EU-12 Member States, South-Eastern Europe and CIS.

Conclusions

The strong decline of cross-border M&A activity in Europe in 2008 and the highlight of the downward trend in 2009 were caused by the reduction of opportunities for companies to invest, as a consequence of restricting the access to financial resources internally (as a result of corporate profits decrease) and externally (due to the reduction of the available liquidity and the increase of funding cost). On the other hand, the market deterioration due to economic recession which practically affected all economies and the unfavourable economic prospects had adversely influenced the companies' predilection to invest. As a result of the global economic slowdown and the recession that affected most economies, the more difficult credit conditions, the sharp reduction of corporate profits and the stock market decline, many companies were forced to abandon their expansion plans and hence the merger or acquisition projects. However, due to the worldwide economic growth that was recorded, the recovery of financial markets, the corporate profit growth, the investment appetite for expansion, national and international development increased significantly since 2010, which was reflected in an increase European cross-border activity. In conclusion, under the continuous economic recovery of the European countries and the other worldwide economies, the recovery of financial markets and the growth of corporate profits, we shall witness an intensive cross-border M&A activity in Europe. The expansion engine of these operations seems to be represented by the emerging economies, whose companies will represent not only attractive targets but also acquirers eager to expand on developed markets.

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