

Strategic Leap to Multinationality: Study of International Acquisitions by Emerging Multinationals from India

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EXECUTIVE SUMMARY

As emerging multinationals, or rapidly internationalizing firms from developing economies, become a permanent, sizeable and rising feature of the world economy, there is a growing need amongst practitioners, consultants, policy makers and academicians to understand their behaviors better. Due to the fledgling nature of scholarly enquiry, knowledge about such firms' strategic orientation, internal and external forces shaping their strategic behaviors and outcomes of their strategic decisions remains fragmented and shallow till date. In particular, not much is known of their inorganic modes of international expansion and how such expansion strategies impact desired outcomes.

Anchored primarily around the resource-based and institutional theories and deriving support from contextually grounded anecdotal evidence, I attempt to address the following specific research questions in this study,

1. What drives emerging economy firms to acquire firms abroad?
2. What are the antecedents and moderators of cross-border acquisitions by emerging economy firms and how do they shape target-location and acquisition-type decisions?
3. What are the value creation implications of cross-border acquisitions by emerging economy firms to investors and what factors moderate the outcomes?

The theory proposed in this dissertation explicitly recognizes the legacy of a socialistic and planning oriented institutional environment prior to market-reforms which results in outdated routines, practices and capabilities that are no longer viable in the post-reforms market. Thus, firm survival is at stake unless transformational measures are adopted to become competitive. Indigenous firms need to overcome the organizational rigidities and liabilities and have to acquire, replace, reconfigure and redeploy their stock of capabilities and resources. Here it is proposed that cross-border acquisition serves as an effective agent for transformation by not only giving indigenous firms quick access to more disperse and highly desired strategic assets available in foreign markets, but also permitting inter-firm knowledge transfer, which leads to superior complementarities in resource and product markets.

Founded upon the above derived conjecture, a theoretical framework comprising of several models is proposed which outlines the mechanism for such acquisitions and predicts the expected outcomes at different stages of the strategic decision process. Specifically, the proposed models predict the impact of antecedent and moderating factors on the nature of host markets where such investments are made, the extent of ownership sought in the identified target firm and the value implications of such investments to shareholders.

Various hypotheses proposed in the dissertation have been empirically evaluated employing a comprehensive database on cross-border acquisitions by Indian firms over the period 2000 to 2007. The proprietary database on 541 acquisitions is cross-verifiable across several known sources of data such as the Thomson Financial database on M&A, Bombay Stock Exchange announcements, Center for Monitoring of Indian Economy (CMIE) database and Grant Thornton database on M&As. Key factors shaping acquisition decisions are operationalized drawing upon information provided by several distinct sources such as the Company Master Data (Ministry of Corporate Affairs), Prowess database (CMIE), National Accounts Statistics (United Nations), World Economic Outlook (International Monetary Fund), World Competitive Index reports, Heritage Foundation reports, OECD data, company annual reports and media releases. The study employs event study methodology, linear and non-linear regression models apart from t-tests and non-parametric testing techniques to evaluate the hypotheses proposed.

Distribution of data presents several intriguing observations. Contrary to some popular beliefs that Indian cross-border acquisitions are restricted to a few industries and mainly target a few developed economies, this study shows that 195 firms in over 70 different industries acquired targets in 66 countries, of which only 26 can be considered to be advanced economies. Also, media tends to focus more on a few large deals by some well known Indian firms, whereas this study shows that 195 firms and their wholly owned subsidiaries, who range from very young to old, small to large, stand alone to business group affiliated, employ low to high technology and spread across extractive, manufacturing and services sector, contributed to the overall phenomenon. In line with theoretical expectations nearly three-fourth of the target acquired are located in economically and institutionally advanced economies. Nearly half of the acquiring firms in the sample made their first full acquisition directly in foreign markets and the rest accounted for nearly three fourth of cross-border acquisitions. This suggests that not only something compelling is driving many of these firms to undertake such risky investments, also many firms found it beneficial to repeat such actions.

Principle findings from this study are as follows. First, the nature of market where emerging economy firms acquired targets and the extent of ownership sought in the target is a function of firm characteristics (experience and resource-positions), top management's strategic intent driving the acquisitions (need to acquire strategic assets, new markets, new products and aspire to be a global player) and the nature of acquiring firm affiliation (whether belonging to business group or state-owned). Second, international acquisitions by emerging economy firms create value for the acquiring firms. Third, the value created is higher when target firm resources are controlled by acquiring firm and target is located in economically and institutionally advanced economies. Fourth, value created in cross-border acquisitions by emerging economy firms is higher than in within-border or domestic acquisitions by same set of firms. Fifth, top management's aspirations to make the firm globally competitive and previous domestic acquisition experience positively impact value created for investors in such acquisitions. In addition to the main findings, a few other counter intuitive findings merit mention. Younger and smaller Indian firms show greater propensity to acquire firms in economically and institutionally advanced economies compared to the older and larger firms and such acquisitions create greater value for investors. Also, acquisitions of larger and publicly held target firms evoked more positive market response.

As one of the first studies to document acquisitive foreign market entry by emerging economy firms, this study contributes to both mergers and acquisition and international business literature by highlighting the contextual factors shaping such decisions. It is one of the few studies to examine cross-border acquisition as a strategic decision process comprising of key intermediate decisions and emphasize the linkage between intermediate stages and overall decision outcomes. By explicitly modeling the dynamics between external environment compulsions and internal environment attributes this study extends and enriches the literature on firm transformation and adaptation. The study has several important implications for practitioners and policymakers. Foremost, cross-border acquisitions are generally viewed to be high-risk and high-cost investments with low rates of success. In the context of emerging economies, however, evidence suggests that under the compelling circumstances facing indigenous firms, cross-border acquisitions is an effective instrument of transformation. Moreover, by judiciously acquiring targets in more advanced economies, there is a potential to combine complementary resources and products and develop superior resource positions. Such combinations coupled with the intent to be globally competitive facilitate a strategic leap to multinationality for the emerging economy firms.