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What Has Happened with C-B M&A Acceptance? A Follow Up Based on 2005 – 2015 Study

Rasto Ovin and Anita Macek

Abstract

Especially since 1990s when capital flows liberalization took their intensive course, also the literature on foreign direct investment and respectfully cross-border mergers and acquisitions grew. On the other hand, although it was accompanying these processes, foreign divestment attracted much less attention. Speculating about the reasons for such situation, one could stress that following the nature of the balance of payments logic foreign direct divestment was not expected. Nevertheless, these processes were present. This chapter addresses some of the most important impacts of foreign direct investment that had been a subject to inverse processes later. The authors try to confront the drivers of these processes and search for different patterns obviously often deriving outside economic rationale from the position of a developed market economy. Using their expertize the authors connected concrete findings of their study with possible drivers of divestment. According to the finding the common nominator was mixed success with the transition in transition countries.

Keywords: foreign direct investment, foreign direct divestment, cross-border mergers and acquisitions, economic effects, host economy

1. Introduction

There are several studies showing the impact of foreign direct investment (FDI) on domestic economies. Typically, studies find that inward FDI are supporting several areas of basic importance for host economy growth. Different authors put focus on different areas. First there is FDI support of access to modern technology and financial sector development - references [1, 2]. More microeconomic oriented studies found that FDI typically promotes productivity growth of an acquired firm - references [3, 4]. Macroeconomic oriented studies on the other hand bring forth FDI positive effects for the growth potential of the host economy as well as for knowledge transfer, growing engagement of local suppliers in supply chains, additional tax revenues and the better use of local services and infrastructure [5–9].

Bringing in more literature sources will provide results referring to positive effects of FDI for technology development, savings, investments and economic development and growth [10]. Furthermore FDI should promote openness to changes, improve leadership and new advanced technology [11]. According to [12]

FDI is exposed not just as a tool for increasing productivity, but also for fostering human capital development and strengthening corporate institutions.

FDI can also reduce unemployment, increase engagement of local companies in supplier and subcontractor networks, support development strategies of individual sectors, increase development potential of the economy, and develop managerial knowledge skills [13–15].

However, it is also proven that the benefits of FDI are not self-evident and that the economic effect of identical FDI can bring very different results in different countries as well as industries [16–18]. Relevant for the topic of this chapter is that proved that positive effects of FDI are not resulting in an equal effect in all branches and industries, with the same frequency and intensity. As presented by [9] the positive effects of FDI depend on the readiness of the host country to openness, and appear only after a certain period.

It is proved that the benefits from FDI increase in an open investment environment. In countries with macroeconomic stability, democratic investment regime, privatization, active competition policies, and deregulation.

However, with unfavorable conditions negative effects of FDI can occur. Reference [19] proved that FDI caused the reduction of productivity in the host country. Further FDI can reduce employment, increase concentration in the domestic market and even more it can cause the closing of domestic companies.

According to [9] FDI can lead to shrinking of the domestic stock market, anti-competitive reactions of the acquired firms, or even elimination of the domestic competition in the home market. [15] proved that one of the main threat of FDI during the last years is related to the fear of losing the national sovereignty and autonomy of the host country and consequently losing control of strategic industries.

Especially since 1990s when capital flows liberalization took their intensive course, also the literature on FDI and respectfully cross-border mergers and acquisitions (C-B M&A) grew. Although it was accompanying these processes, on the other hand, divestment attracted much less attention. Speculating about the reason for such situation, one could stress that following the nature of balance of payments logic the FDI to take an inverse course was not expected. With the theory arising already in 1980s [16], these processes were present and have been gaining on importance in later decades [17].

As foreign divestment, authors will consider reduction of assets of foreign investor in the receiving country. Authors will not discuss foreign divestment on the basis of management decisions such as changing or concentrating to core business of majority owner, change in the market positions or instability in the host country, poor performance and management, but will focus rather on vague field of general FDI acceptance in a host economy.

Authors will try to find the position of foreign divestment by the help of the data acquired by study on economic effects of C-B M&A carried out by the authors in the period between 2005 and 2015. Having certain information and experience on economies of Western Balkans authors will try to synthesize information of general attitude towards market economy and democratic development.

In this chapter, authors first summarize the results of their studies in the period between 2002 and 2015 proving predominantly positive economic effects of C-B M&A. Second part of the chapter brings the facts discussed in the literature, showing that the important part of FDI had been also subject to inverse processes later. Authors try to confront the drivers of these processes and search for different patterns obviously often deriving outside economic rationale from the position of a developed market economy.

2. Why it happened?

Basing on the theoretical paradigm of liberal concept of the balance of payments it seemed plausible that the study measuring economic effect of this form of FDI would prove the positive acceptance and sentiments of stakeholders in receiving countries. The result of authors' studies carried out in the period between 2005 and 2015 show that C-B M&A, despite some reservations in the literature [18–21], support the receiving country technological improvement and exports.

Nevertheless, at the same time also processes of divestment were taking place. According to [22] multinational enterprises divested one of every five foreign-owned affiliates over this period of time.

In the following text authors will discuss the possible reasons for divestment and will try to locate the factors that were not taken into account with authors' study that have proved drivers of divestment sentiment.

In the last quarter of 2020 new developments in the EU saw Poland and Hungary opposing the present EU Commission threat that due to issues with (un)democratic processes in these countries (with Slovenia under present government also checking for feasibility of such course) they could be expelled from a massive economic help from the EU. This simply showed that the countries that would be beneficiaries of processes of widening of western-type democracy might have changed their view after being accepted in this noble community for which they longed for decades. No one could conclude that with pledging for acceptance in the EU the politicians as well as opinion creators were rather thinking on higher wages, access to western goods and free movement (until it suits them). Their perspective seemed to be biased towards higher standard of living without endeavor to catch up with their missing or interrupted path to a modern democratic society. The same is actually valid for the process of liberalization of capital imports. Rather than doing their homework with institutional setting and economic environment (financial markets, meritocracy, public finance transparency and accountability) which could assure FDI best contribution to the incoming countries economy, they seemingly expected (were allegedly promised) manna from heaven and are now claiming that it was rather Dans' fake gifts.

If we turn the side of the medal, we could probably conclude that there is another factor preventing host countries to be more effective with adjustment of their economic environment to the reality of liberal capital flows. The conditions in which they are supposed to open and develop their economies differ very much from the conditions that today's leading economic powers had in the time of their positioning as such. It is not difficult to conclude that the present domination of western economic model and technology was actually achieved through all kinds of their interventionism in favor of domestic economies. These were the times following first industrial revolution. Only when established as leading economies they became promoters of trade and capital flows liberalization. They are actually doing their best to impose liberal order to those, which would surely benefit from certain interventionism. The problem is that due to arrears in their (democratic and institutional) development they are not in position to carry out such policies against foreign competition without the risk of being expelled from the international trade community facing the negative consequences for their economic development and growth.

Foreign divestment must therefore be seen as a sign that with international integration and globalization also process of international economic disintegration is taking course. Opposing the dissolvent of their culture and tradition, the follower countries (countries not in first line of systemic leaders of global technology

progress) no doubt have support of domestic electoral body. The solution is surely not to be found in the present economic and international co-operation model.

It needs no special proof, that “Asian tigers” have taken a different path in response to liberal capitalism. According to [23] the list of countries with highest average intelligence quotient is topped by Singapore, China, Hong Kong, South Korea and Taiwan. Being on the top by the (unpopular) criteria of intelligence quotient these societies under democratic or less democratic environments obviously succeeded with adjusting of their cultural model to the mainstream dictated by western industrial countries. Up to now, nothing else could be said apart from that, that they supply a clear proof that in favorable conditions FDI supports host country economic growth, employment, technology improvement and international competitiveness.

3. The facts deriving from author’s studies

As stressed above authors base the findings on the results of their study in the period between 2005 and 2015, researching European economies that were divided in developed and transition countries and separately the ones of Slovenia and Serbia.

In the research of European economies in total 53 answers from developed countries and 38 from transition countries were analyzed. As developed countries old EU members before 2004 EU enlargement, Island, Norway and Switzerland were considered. Although there are considerable differences among them, these countries have been experiencing western type of democracy, private ownership and market economy. They are: Austria, Belgium, Cyprus, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Island, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, and UK. On the other side as transition countries considered were European countries, who after World War II shared state ownership, mono-party system and central planning. Authors presupposed that these heritages should define a different need for privatization, to replace obsolete capacities in manufacturing and to develop markets and hierarchies typical for a market economy – all being normal consequences of inward C-B M&As. The countries representing this group were: Belarus, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Russia, Slovakia, Slovenia, and Serbia and Montenegro.

The results pointing to possible sentiments for foreign divestment on the side of receiving countries are stressed below.

We start with receiving countries motivation for attracting C-B M&A.

As shown in the **Table 1** the most important motives for attracting C-B M&A were the access to new markets, followed by the transition process, know-how transfer and technology improvements. External pressure on domestic policies as well as C-B M&A as a support for a better strategy of industry development did not attract much attention in relation to the motives of C-B M&A.

The attitude of expanding national economies, compared to transitional economies, where capital imports have the function of repairing domestic structural disproportions is shown with giving the higher importance to access to new markets in developed countries compared with the ranking in transition countries.

National competitiveness and the importance of development local management skills, have been considered more important motive for attracting C-B M&A in transition countries than in developed countries because the situation of catching up in this field is logically more present in transition countries.

Motivation factor	Developed countries	Transition countries
External pressure on domestic politics	5,82%	7,84%
Development of local management skills	4,58%	7,84%
Lack of strategy for certain industries development	6,87%	7,84%
Part of transition process	17,46%	15,69%
Access to new market	23,50%	16,67%
Technology improvement	13,74%	12,75%
Increase of national competitiveness	12,00%	12,00%
Know-how	16,03%	14,71%
Source: [24].		

Table 1.
Grounds for countries’ motivation when attracting C-B M&A.

Answers also show that technology improvement is important motive for attracting C-B M&A in all countries. While in transition countries technology improvement closes the gap towards developed countries, in developed countries it is basically there for consolidation of strategic industries.

Being less motivated for entrance of foreign markets transition countries typically demonstrate themselves as closed economies in the period before the start of 1990s. Lagging behind developed countries transition countries surprisingly demonstrate that they are not as they should be convinced that the C-B M&A are also about the transition from closed economy into an open market economy.

One would also expect that meeting the western standards through C-B M&A would represent higher priority to execute external pressure on domestic politics to accomplish transition processes in transition countries.

Authors also analyzed possible threats of C-B M&A for domestic economies. Results are presented in the **Table 2**.

As it can be seen from the **Table 2** shrinking of domestic stock market was assessed as the lowest threat of C-B M&A in all receiving countries, while crowding-out of domestic industries was the highest threat for C-B M&A receiving countries.

The **Table 2** also shows that apart from ‘crowding-out of domestic companies’ where there was a relatively small difference between both groups of countries, other answers show quite different perspectives when assessing C-B M&A threats.

The risk of reduction in employment and decrease of competition in the home market were considered essentially larger threats in developed countries than in transition countries. Such sentiments could derive from conviction, which may be the ground for the real policy of preventing takeover bids in European developed countries: takeovers of ‘national champions’ may cause destabilization of labour markets. The problem of unemployment reduction because of C-B M&A is present in transition countries too but in a smaller extent, probably because C-B M&A have established themselves as one of the tools of privatization and economic restructuring, which must take place anyway.

However, in transition countries more focus is given on low pricing of sold assets and undermining of the domestic economic development strategy. These two threats received more attention in transition countries because of the huge restructuring that C-B M&A cause in this environment endangers the last positive illusions of the domestic economic development model and ‘national champions’ that survived the transitional process. And there is no doubt, that when they are

Threat	Developed countries	TRansition countries
Shrinking of domestic stock market	3,09%	5,88%
Crowding-out of domestic industries	25,77%	28,24%
Undermining of domestic economic development strategy	5,15%	12,94%
Low pricing of sold assets	7,22%	16,47%
Decrease of competition in the home market	20,62%	14,12%
Reduction of employment	38,14%	22,35%
Source: [24].		

Table 2.
Threats of C-B M&A.

sufficiently scarce and unique, domestic assets signify a special incentive for foreign investors, which is then expected to be offset correspondingly in their selling price.

Threats of crowding-out and undermining competition through inward C-B M&A were subject to a more detailed analysis with the help of additional questions requiring detailed information on the matter. It was of special interest to us that through these questions a possible difference between expectations (threats) and experience (the cases that the respondents have registered) would arise. We have chosen the two items mentioned above, as it was expected that they would be ranked high with threats of inward C-B M&A.

In the **Table 2** above the case could be supported through the fear that C-B M&A could undermine domestic economic strategy. It should be clear that importing foreign capital should be a part of national strategy, while functioning of these investments by themselves should be treated as a step in the right direction. Without entering the reasons for such sentiment this conviction becomes relevant as soon these threats enter the domestic policy discussion with domestic critics of transition itself and trade unions. In this way, it influences politics' sentiment towards C-B M&A making it harder to the foreign investors to pursue their initial business goals and could thus pave the way for divestment.

As it can be seen in the **Table 3** the market structures in developed countries as being far more developed than those in transition countries, are obviously offering less chance to foreign affiliates to act in an anticompetitive way.

Similarly, to above risk of creating hostile environment for C-B M&A poses also the sentiment of anticompetitive behavior that was already experienced. It is surely difficult to judge when harsh competition for domestic companies was caused by the practice, normal in the West or when real anticompetitive practice was at work. This sentiment has otherwise to do with lagging institutional reforms – here in the field of competition policy.

Authors also examined professionals' assessment of media attitude towards inward C-B M&A. Results are presented in the **Table 4**.

Probable the strongest case for also existing sentiments, which may also curb divestment makes pretty inverse treatment of C-B M&A in media when considering two groups of host countries. In the **Table 4** above it is shown that C-B M&A were treated more favorably in developed countries, because inward C-B M&A in developed countries obviously face a highly developed social and economic environment with more consistent markets and financial structures and are therefore accepted more friendly in media. Further, in developed countries it is expected that they could neutralize their possible negative effects of C-B M&A more than transition countries and this can also lead to less public skepticism.

Anticompetitive behavior by foreign affiliates	Developed countries	Transition countries
It has happened in several cases	11,32%	23,68%
There have been some cases when it happened	41,51%	60,53%
There have not been such behavior	47,17%	15,79%

Source: [24].

Table 3.
Anticompetitive behavior by foreign affiliates.

General treatment of C-B M&A in media	Developed countries	Transition countries
Favorable	1,89%	0%
Showing acceptance	32,08%	13,16%
Neutral	43,40%	44,74%
Not to friendly	22,64%	36,84%
Unfavorable	0%	5,26%

Source: [24].

Table 4.
General treatment of C-B M&A in the media.

The authors performed similar research by comparison of sentiments towards C-B M&A of local communities in Slovenia and in Serbia [25]. Authors were interested in the comparison between local communities in Slovenia and Serbia and they wanted to analyze the consequences of different approach with accepting change and especially international opening.

When analyzing C-B M&A threats also here results relevant for this chapter appeared. First interestingly with some threats Slovenian critical sentiments towards C-B M&A were exposed surprisingly stronger than in Serbia, regarding the fact that Slovenia is often considered as one of the champions of transition. They refer to possible reduction of employment and environmental damage, the last being nevertheless a sign of higher development level.

In the same article the explanation for such outcome is explained with the fact that at the beginning of the transition processes in Eastern Europe Slovenia was according to Economic development clear leader. This perception, however, often harmed political will to change causing arrears especially in institutional transition and was also off set in lower acceptance of foreign capital [25].

Otherwise, as expected the differences pointing at possible sentiments to support divestment are in favor of Slovenian local municipalities. So, in Serbia typically the public seems to be convinced that Serbian companies have been acquired for too low price and that foreigners could exercise unwanted influence on the local level.

To a certain extend these results coincide with the results of already mentioned study by [22]. As possible drivers of divestment sentiments here among others through statistical significance unit labour costs, trade openness, level of control of corruption labour market efficiency and environmental policy stringency was proved.

4. Conclusion

This chapter shows the summary of the results of the research [24, 25] done in European countries and separately in Serbia and Slovenia. Main positive effects as

well as some threats of C-B M&A are presented. Special attention is given also to the media treatment of C-B M&A in European countries and as an important part of the FDI had been a subject to inverse processes later authors tried to connect the results of their research done in the past to these processes.

Using their expertise the authors connected concrete findings of their study with possible drivers of divestment – those coming from the policy and public sentiment in host countries were considered here. According to the findings the common nominator was mixed success with the transition process in transition countries. It proved that it would be a gap in institutional transition that prevented connection with interests of foreign investors and host country.

The results of comparison of economic effects in developed and transition countries actually enabled the insight into possible drivers of divestment. It is plausible to conclude that economic effects were focused to the beginning of transactions, while the era of investment operation dissonances could later lead to climate favorable to divestment.

For this chapter highly relevant are also findings in the source [26] that in respect to institutional distance the chances for foreign divestment are subject to an inverse U curve. This would mean that parting from lower institutional distance these chances grow, reach their peak on the border outskirts of certain institutional setting arrangements and lower when the institutional distance is bigger. Applied geographically this would be the case, which could be expected for an investor from European industrial economy. Here lower chances for foreign divestment would refer to neighboring economies and would reach their peak on the bordering belt economies – here meaning the economies of Western Balkans. Going further the Asian economies which we use as example of Asian Tigers have quite different institutional setting and thus institutional distance to the investor's country. Due to other factors mainly explainable with their flexibility the chances of foreign divestment should be reduced.

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