The Determinants of Chinese Cross-border Mergers and Acquisitions Performance

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ABSTRACT

This thesis focuses on the determinants of Chinese cross-border mergers and acquisitions (M&As) performance. It provides compelling evidence that country-level factors play significant roles in cross-border M&A outcomes in both deal completion and performance.

The thesis examines whether valuation differences influence the performance of Chinese cross-border M&As. It shows that Chinese acquirers enjoy better stock performance around deal announcement when there are larger differences in stock market returns and exchange rate returns between the home and host countries. Regarding the long-term performance of Chinese cross-border mergers, this study finds that there is a negative relationship between stock market return difference and long-term stock performance, while exchange rate return difference is positively related to long-term performance.

The thesis also investigates the role of international trade in Chinese cross-border M&As. It shows that Chinese acquirers are more likely to complete cross-border mergers when there is a higher level of bilateral trade flow between acquirer and target countries. More bilateral trade also leads to higher abnormal returns to acquirer shareholders in both the short- and long-term. Overall, the results indicate that bilateral trade networks and openness help countries build a strong connection, which assists acquirers in cross-border mergers to overcome barriers and generate synergy gains.

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DECLARATION

No part of this thesis has been submitted elsewhere for any other degree or qualification in this or any other university. It is all my own work unless referenced to the contrary in the text.

STATEMENT OF COPYRIGHT

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CHAPTER ONE: INTRODUCTION

1. Introduction

Mergers and acquisitions (M&As) are one of the most important corporate growth strategies. With an ever-changing economic environment, M&As enable companies to grow rapidly through organisational restructuring and thus to survive against fierce industrial competition. Among mergers and acquisitions, cross-border transactions, in particular, are considered by firms to be among the most aggressive strategies to expand and to enter foreign markets (Alba, Park and Wang, 2009). Over the last two decades, capital reallocation via cross-border M&As has experienced a significant increase globally. According to the Institute for Mergers, Acquisitions, and Alliances (IMAA)[1], the number of multinational mergers worldwide increased from 472 in 1985 to 13,606 in 2018. Although there are growing socio-political tensions and economic uncertainties including the China-US trade war, the UK's exit from the EU, and the global economy slowing down, the volume of cross-border M&As has remained high and represents around 30% of the total merger transactions. In terms of resources involved, cross-border M&As were valued over $1.35 trillion in 2018, which is $0.08 trillion higher than valuation in 2017.

Regarding regional cross-border activities, Asia Pacific attracts much attention. In 2018, outward mergers in the Asia Pacific experienced significant growth while inward deals increased more modestly (Mergermarket, 2019). The value of outward acquisitions rose to $160 billion, an increase of 52.4% in comparison with 2017, and was the second-highest on record. China has remained the most targeted country, which could be attributed to an acceleration of mergers approvals by the Chinese government. In terms of

[1]The IMAA is the international academic institution offering professional knowledge and information about mergers and acquisitions.

outbound investment, China's bids in the US fell 94.6% from $55.3 billion in 2016 to $3 billion. Meanwhile, Chinese acquirers taking over EU companies rose by 81.7% from $33.2 billion in 2016 to $60.4 billion.

With the increasing number and importance of M&As, much finance and management research has investigated them from various perspectives. In particular, cross-border M&As are considered a promising field of research because of the international nature of the world economy, which draws attention not only from developed markets but also from developing markets (Bertrand and Betschinger, 2011; Boateng and Wang, 2008; Chen and Young, 2009; Chen and Wang, 2014; Coeurdacier, De Santis, and Aviat, 2009; Dension, Adkins, and Guidroz, 2011; Datta and Puia, 1995; Dos Santos, Errunza, and Miller, 2008; Dutta, Saadi, and Zhu, 2013; Moeller and Schlingemann, 2005; Ryu and Lee, 2009; Shimizu, Hitt, Vaidyanath, and Pisano 2004; Tang, 2015; Tao, Liu, Gao, and Xia 2017; Uddin and Boateng, 2011; and Zhang and van Gorp, 2017). Conceptually, multinational acquisitions are conducted by acquirers for the same reason as domestic deals; two companies merge into one to achieve synergies. However, cross-border deals are related to additional factors that could impede or assist acquisitions. For example, geographic or cultural differences could cost the acquirer more, while regulation-related differences across countries could facilitate cross-border transactions if target shareholders receive better protection following deal completion.

The literature on M&A motivation, performance, and related factors is reviewed in Chapter 2. Research on cross-border mergers and acquisitions mainly focuses on the US and other developed markets and there is little evidence on the Chinese market given that Chinese cross-border M&As have significantly increased in the 21st century. In the

1990s, the number of Chinese cross-border mergers was around 30 per year, which quadrupled to around 117 by the 2000s. In the international M&A market, overseas acquisitions conducted in advanced markets suffered a significant drop following the global financial crisis in 2008, but Chinese acquirers continuously made mergers and acquisitions in the US and European markets; for example, state-owned firms like China Petrochemical and Sinopec and private firms like Geely and Shuanghui.

To gain a better understanding of Chinese cross-border mergers and acquisitions, this thesis investigates the macro-economic determinants of Chinese cross-border deal outcomes. Three factors have been examined: country-level stock price movements, currency movements, and bilateral trade flow of China and the target countries.

Chapter 3 focuses on the role of valuation differences in Chinese cross-border M&A performance. Differences in currency appreciation and stock market valuation between the acquiring and target firm's countries are examined. During the last two decades, the Chinese stock market has significantly expanded. Previous research suggests that there is a positive relationship between the level of domestic stock market activity and the number of cross-border M&As (Sudarsanam, 2003; Di Giovanni, 2005; Neto, Brandao, and Cerqueira, 2010; Wang, 2008). Also, the Renminbi (RMB) has experienced rapid appreciation since its revaluation and reform in 2005. Erel, Liao, and Weisbach (2012) argue that a strong currency can also increase the likelihood of a company seeking to expand internationally.

Although stock market valuation and currency appreciation have played an important role in Chinese firms' decision to conduct outbound acquisitions, little is known about the influences of these two factors on the performance of these cross-border mergers. By

examining 1,174 Chinese cross-border M&As from 1995 to 2016, Chapter 3 seeks to fill this gap by investigating whether any valuation effect generated from the appreciation of the RMB and the misvaluation of the stock market can be transformed into gains for acquirer shareholders in either the short- and long-term.

The main findings of Chapter 3 suggest that acquirers could take advantage of misvaluation and enjoy better performance. The results show that the wealth effects for acquirer shareholders significantly increase with the differences in stock market and exchange rate returns of acquirer and target countries. In terms of Chinese acquirers' long-term performance, there is a significant negative relationship between acquirers' long-term performance and the difference in stock market returns in acquirers and target countries, while long-term performance is positively related to exchange rate return difference. This suggests that deals driven by stock overvaluation do not generate synergy gains and this might be because taking less overvalued target results in the reversal of acquirers' valuation. Alternatively, investors may overestimate deal synergies in high valuation stock markets, and the correct stock price gradually as they realise that initial expectations might not be fully achieved. The valuation reversal is not found in the analyses of exchange rate returns, indicating that acquirers taking advantage of highly appreciated currency can create synergies in the long-term.

Chapter 4 focuses on the effects of bilateral trade between home and host countries on the wealth gains of Chinese cross-border mergers. Previous literature suggests that bilateral trade networks and openness build strong connections between countries and reduce trade and investment barriers. China's cross-border acquisitions provide a unique testing

ground because of the high ownership concentration that makes China's multinational deals strongly influenced by the institutional environment and traditional culture.

By examining a data set of 1,130 Chinese cross-border mergers and acquisitions between 2001 and 2016, Chapter 4 provides evidence that Chinese acquirers are more likely to complete a cross-border deal when there is a higher level of bilateral trade between China and the target country, which is consistent with previous literature (Erel, Liao and Weisbach, 2012). Additionally, the results show that acquirers experience significantly higher abnormal returns in both the short- and long-term when China and the target country have more trade exchange, which indicates that the market is more in favour of cross-border deals involving two countries with stronger trade relationships and that these relationships can help acquirers generate synergy gains.

This thesis contributes to the existing literature in several respects. First, to the best of our knowledge, this is the first paper studying the effects of macro-economic factors of both home and host countries on Chinese cross-border M&As. Most studies (Kolstad and Wiig, 2009; Buckley, Clegg, Cross, Liu, Voss, and Zheng, 2010), focus on the effect of a series of host country characteristics on M&As. It can be seen that China's overseas acquisitions have retained an upward trend even when the world's economic condition was in recession, which suggests that the characteristics of the home country also play important roles. This paper offers direct evidence that the booming economy of the home country can benefit outbound M&As.

Second, this thesis makes contributions to the literature on cross-border M&As by providing evidence from China. Extensive research has focused on the effects of macro-economic factors on M&As in the context of advanced economic countries

(Georgopoulos, 2008; Choi and Leon, 2010; Uddin and Boateng, 2011). However, the booming economy of the emerging markets, especially the Chinese market, over the past two decades has contributed to an upward trend of M&A volume and makes emerging market firms more likely to be bidders in cross-border M&As.

Third, to the best of our knowledge, this is the first study to examine the effects of bilateral trade flow on Chinese acquirer performance. Despite the increasing significance of trade relations between China and target countries, only a small number of studies include data on import and export trade volume (Rossi and Volpin, 2004; Chakrabarti, Gupta-Mukherjee, and Jayaraman, 2009) and there is little evidence on the Chinese market.

The thesis is structured as follows. Chapter 2 reviews the existing literature on cross-border M&As and the various determinants of cross-border transaction valuation effect. Chapter 3 investigates the effects of exchange rate and stock market valuation on acquirers' performance in both the short- and long-term. Chapter 4 explores the relationship between the level of bilateral import and export and Chinese cross-border merger outcomes.

CHAPTER TWO: LITERATURE REVIEW

M&As have attracted a large number of studies. These activities are considered to be among the most important investments for companies, industries, and the economy. In particular, there is a huge amount of international investment made via cross-border M&As (Becker & Fuest, 2010; Huizinga & Voget, 2009). Much research has been conducted to examine factors that determine M&A success, ranging from external determinants related to markets and internal determinants related to companies. However, little has been written on cross-border M&As in China. This thesis attempts to fill this gap and contributes to prior studies.

2.1 Definitions

Broadly speaking, the term mergers and acquisitions refers to combining two companies via one or more financial transactions, such as a merger, acquisition, tender offer, takeover, joint venture and purchase of an asset. While some research suggests that employing a broad definition of M&As can be misleading (Nakamura, 2005), mergers and acquisitions are generally considered the same, and the term is employed interchangeably. This section reviews different definitions of mergers and acquisitions given in previous studies.

2.1.1 Merger

The Merriam-Webster dictionary gives the definition of merger transaction as ‘a corporate strategy of combining different companies into a single company to enhance the financial and operational strengths of both organisations’. This is a financial transaction in which a new entity is established through the combination of two or more

companies' assets and liabilities (DePamphilis, 2009; Gaughan, 2011; Jagersma, 2005; Khan, 2011; Sherman and Hart, 2006; Weston, Chung, and Hoag, 1990).

2.1.2 Acquisition

The Merriam-Webster dictionary gives the definition of acquisition transaction as '*a purchase of all or a portion of a corporate asset or target company*'.Unlike mergers which lead to the formation of a new entity, acquisitions are transactions in which bidders take control of targets and the targets no longer exist(Alao, 2010; DePamphilis, 2019; Van Horne and Wachowicz, 2008; Jagersma, 2005; Krishnamurti and Vishwanath, 2008; Scott, 2003).

2.1.3 Takeover

A takeover is defined as a type of acquisition that a target firm is not willing to negotiate with bidders and thus the bidder aims to take over the target through purchasing its stocks directly from target shareholders.

2.1.4Cross-border M&As

Cross-border M&As transactions are defined as the integration of a domestic firm and one or more overseas firms to establish a new entity. The integrated firm holds the assets of both parties (Gaughan, 2010).

2.2 Classification of Mergers and Acquisitions

Depending on the competition between bidder and target, mergers and acquisitions are divided into various types listed in the Statistical Report on Mergers and Acquisitions

(US Federal Trade Commission, 1980). These are vertical, horizontal, market extension, product extension, and conglomerate transactions.

2.2.1 Horizontal M&As

According to Boseman and Phatak (1989), horizontal M&As are transactions of merging two firms with businesses in the same or similar sectors in an attempt to gain market share and cut costs. Becketti (1986) and Sudarsanam (2003) show that horizontal acquisitions were major components of the first M&As after the Great Depression, especially in the oil and steel sectors. Chen and Findlay (2003) argue that there has been a growing number of horizontal acquisitions in recent years due to technological shocks.

2.2.2 Vertical M&As

According to Gaughan (2011), vertical M&As are transactions of merging two firms with businesses in similar sectors but involving different stages of the supply chain, such as purchasing, distribution, and retail of raw materials. For instance, an upstream company (a supplier of a service or product) might be combined with a downstream company (a customer in the output market) in a vertical acquisition, which could lead to higher economic efficiency and lower product cost through the economies of scope(Besanko,Dranove,Shanley, and Schaefer,2009; Salop and Culley, 2014).

2.2.3 Product-Extension M&As

Product-extension M&As are transactions of merging two firms in the sample market which provide relevant products or services. According to Aaker and Keller (1990), Boush and Loken (1991), DelVecchio and Smith (2005) and Park, Milberg, and

Lawson(1991), product-extension is aimed at achieving a larger customer base through increasing the diversity of similar products.

2.2.4 Market-Extension M&As

Market-extension M&As are transactions of merging two firms in different markets but offering the same products or services. Unlike horizontal M&As, acquirers and targets in market-extension M&As are not competing with each other. Previous studies suggest that market-extension mergers are made to gain a larger customer base by expanding the geographic reach of the company. Cross-border M&As are market-extension deals, accounting for a large percentage of the whole M&A market (Ernst & Young, 2017).

2.2.5 Conglomerate M&As

Conglomerate M&As are transactions of merging two firms with different businesses and operations in different markets. Church (2004) and Weston, Chung, and Siu(2004) suggest that there is no horizontal, vertical, or complementary relationship between bidders and targets in conglomerate transactions. According to Amihud and Lev (1981) and Matsusaka (1993), conglomerate deals are conducted to generate synergies and reduce risk by diversifying into new markets and sectors.

2.3 Motivations for Mergers and Acquisitions

The driving force of M&As [2] has been much examined in previous literature. Nevertheless, further studies are still required due to address the unsolved question of acquirers' performance following transactions, i.e. bidders are likely to suffer negative to

[2] 'Mergers', 'acquisitions' and 'takeovers' are interchangeable terms in this study.

zero abnormal stock returns(Andrade,Mitchell, and Stafford 2001; Bruner, 2002; Datta,Pinches, and Narayanan, 1992; Jensen and Ruback, 1983; Loughran and Vijh, 1997; Mulherin and Boone, 2000).

To better understand merger success, it is important to examine the motivation behind a firm's takeover decision (Seth, Song, and Pettit, 2002). Previous literature has proposed several explanations, for example, efficiency theory, valuation theory, managerial hubris theory, empire-building theory and managerial timing theory(Doukas and Petmezas, 2007; Hodgkinson and Partington, 2008; Roll, 1986; Seth *et al.*, 2002; Shleifer and Vishny, 2003).However, the whole picture of M&As cannot be explained by only one theory.

2.3.1 Efficiency Theory

According to the efficiency theory, M&As are implemented to create synergies (Porter, 1985). Synergies can be obtained through redeploying the assets of acquirers and target firms and the combination of acquirer's and target's physical practices (Bradley, Desai, and Kim, 1988; Capron, Dussauge, and Mitchell, 1998).Synergy is defined by Merriam-Webster dictionary and other literature, e.g. Jensen and Ruback (1983) and Bradley,Desai, and Kim(1988) as the value resulted from combining two or more entities is greater than the sum of their separate value. The literature on mergers and acquisitions suggests that there are mainly four categories of synergy: financial synergies via the improvement of capital efficiency (Seth, 1990), operational synergies from economies of scale and scope (Seth, 1990), management synergies through the application of complementary competencies (Sudarsanam, Holl and Salami, 1996), and collusive synergies through the market and purchasing power (Chatterjee, 1986).

2.3.1.1 Operational Synergy

The success of M&As is usually measured by operational synergy, which could be achieved via economies of scale and scope, and reducing recurring expenses related to production, marketing, and compensation(Devos,Kadapakkam, and Krishnamurthy, 2009; Lubatkin, 1983). Therefore, acquirers conducting horizontal or vertical deals tend to achieve operational synergies (Mooney and Shim, 2015). Increasing the operational efficiency of productive assets could result in higher cash flow and thus increase the value of the company.

Previous literature provides mixed evidence on the existence of operational synergy. Ghosh (2001) and Ravenscraft and Scherer (1987) examine the acquirers' accounting performance following deal completion and suggest that there is little improvement in operating efficiency. In contrast, Healy, Palepu, and Ruback (1992) and Heron and Lie (2002)measure operating performance with asset turnover ratio and confirm that acquirers enjoy operational synergies.Houston, James, and Ryngaert (2001)focus on the banking sector and report that synergies are generated from cost savings rather than revenue increases. Devos, Kadapakkam, and Krishnamurthy (2009)use the methodology of value line forecast and suggest that 8.38% of the value created by M&As for acquirers is from operating synergies, which is higher than that from financial synergies (1.64%).

2.3.1.2 Financial Synergy

Trautwein (1990) reports that acquirers can gain financial synergies with decreased costs of capital and diversified risks. This could be realised by several methods. According to Lewellen (1971), combined firms with more financial assets have more debt capacity and

thus can access cheaper capital. Lewellen (1971) also argues that acquirers could have a lower unsystematic risk by taking over a firm in an unrelated business and therefore the two firms' cash flows can be protected. More recently, Hoberg and Phillips (2010) report supportive evidence on financial synergies and suggest that it can be achieved through product differentiation.

2.3.1.3 Managerial Synergy

Managerial synergies can be generated in M&As with two firms having different levels of management efficiency. According to Trautwein (1990), merger transactions with an experienced acquiring firm and inexperienced target are likely to create managerial synergies. Lang, Walkling, and Stulz (1989) examine managerial synergies with Tobin's Q theory. Acquirers tend to benefit from managerial synergies when they have a higher Tobin's Q ratio than target firms, suggesting that the target's managerial efficiency can be improved with the acquirer's help. This is also confirmed by Servaes (1991) who found that better acquisition performance can be achieved by the difference of the Q ratio between the acquiring and the target firm. Therefore, firms with poor performance tend to be taken over (Martin and McConnell, 1991a; Palepu, 1986). However, Agrawal and Jaffe (2003) find little evidence of managerial synergy and conclude that merger performance is insignificantly related to the operating performance of targets.

2.3.1.4The Source of Synergy in Cross-border Mergers and Acquisitions

Given the presence of international barriers in cross-border mergers, the source of synergy in cross-border mergers and acquisitions is from internalization and reverse internalization (Seth, Song and Pettit, 2002). For example, acquirers tend to reduce

international transaction costs by acquiring a foreign target. Additionally, by conducting cross-border mergers, acquirers could take advantage of target firms' expertise and resources at the home market to create more investment opportunities. Dunning and Lundan (2008) apply the eclectic paradigm to three synergies for international expansion: efficiency-seeking, asset-seeking and foreign market-seeking. In terms of efficiency-seeking, cross-border mergers are driven by synergies from combining operations which could reduce operating costs. As for asset-seeking, acquirers of cross-border mergers, especially from an emerging market, are motivated by greater access to those capabilities and resources that are imperfectly mobile across countries due to information asymmetry (Anand and Delios, 2002; Wernerfelt, 1984). Last, regarding foreign market-seeking, firms are motivated by pursuing a larger market size in both domestic and foreign markets. Scaperlanda and Mauer (1969) develop a market-size hypothesis and suggest that the size of the host country market plays an important role in determining a firm's FDI decision, which is also confirmed byChakrabarti(2001).

2.3.2 Monopoly Theory

Jensen and Ruback (1983) suggest that M&As are motivated by expanding the market and gaining market power. With cross-subsidising products, acquirers can realise synergies from reduced market competition (Trautwein, 1990). Such deals include Bayer-Monsanto and Syngenta-ChemChina.

2.3.3 Agency Theory

Some literature suggests that M&As can be explained by agency theory, the conflicts of interest between managers and stockholders which arise because the company's

ownership and control are separated (Jensen and Meckling, 1976). M&As could be conducted to generate higher compensation for managers instead of more shareholder value. Murphy (1985), Yim (2013), and Anderson, Becher, and Campbell (2004) find a positive relationship between the compensation of acquirer executives and M&As. Harford and Li (2007) report that, following a merger, acquirer executives' compensation increases with merger performance. This is also confirmed by Guest (2009) and Bliss and Rosen (2001) who investigated UK and US M&As respectively in the banking industry.

In addition to compensation, acquirer executives are likely to conduct M&As when firms have a higher level of free cash flow (Jensen, 1986). With excess cash flow, managers tend to invest in projects rather than paying shareholders due to the conflict of interest. Empire-building incentives could also drive M&As. By increasing firm size, CEOs can enjoy personal benefits such as social prominence, power within the company, salary, and bonuses (Avery, Chevalier, and Schaefer,1998;Jensen, 1989; Reich, 1983).

2.3.4 Hubris Hypothesis

Roll (1986) explains the motivation of M&As with the hubris hypothesis, i.e. acquirers conduct mergers due to overconfidence in their ability to generate gains for companies and shareholders. Unlike agency theory where the acquirer executives conduct mergers to pursue their personal interest at the cost of stockholders, hubris theory argues that managers conduct deals to increase shareholder value but they overestimate gains and underestimate risks. Three factors can contribute to overconfidence: the self-importance of managers, praise of managers in the media, and recent good performance of companies (Hayward and Hambrick, 1997).

Following Roll (1986), studies have largely tested the hubris hypothesis and provide consistent findings. Hayward and Hambrick (1997) document that mergers involving an overconfident acquirer CEO are more likely to have a higher premium but worse performance. Malmendier and Tate (2005) find that firms with an overconfident manager tend to invest in more projects when there are more internal funds. Further, Malmendier and Tate (2009) provide consistent evidence that acquirers with an overconfident experience lower abnormal returns. Moeller, Schlingemann, and Stulz(2005) argue that mergers and acquisitions with huge value destruction are due to CEO overconfidence.Theliterature also explains the underperformance of serial acquirers with the hubris hypothesis (Doukas and Petmezas, 2007; Billett and Qian, 2008; Conn, Cosh, Guest, and Hughes,2005; Ismail, 2008; Kolasinski and Li, 2013).

2.3.5 Market-Timing Hypothesis

Unlike the hubris hypothesis suggesting that managers are irrational while the market is efficient, the market-timing hypothesis suggests that managers are rational and take advantage of misevaluation in the inefficient market (Shleifer and Vishny, 2003). As managers are assumed to be rational, deviations in a company's share price from its true value can be identified in the short-term. According to the theory, acquirers are more likely to conduct M&As with stock payment when (a) the market valuation is higher; (b) the acquirer's stock price significantly deviates from its true value; and (c) acquirers have experienced recent higher returns. The theory also suggests that acquirers paying with stock are more likely to suffer worse performance than those paying with cash.

Much evidence has been found that is consistent with the market-timing hypothesis. Rhodes-Kropf, Robinson, and Viswanathan (2005) split market-to-book ratio into three sectors – time-series sector error, firm-specific error and long-term pricing to book – and find that: (a) acquirers tend to have higher valuations than target; (b) acquirers with less overvalued stock tend to pay with cash; and (c) acquirers having greater firm-specific errors tend to pay with stock. Dong, Hirshleifer, Richardson, and Teoh (2006) find that market valuation is more likely to be a driving factor of M&As in markets with higher valuations. They report that mergers before 1990 can be explained with the Q hypothesis while evidence on mergers after 1990 is more consistent with market-timing theory. Ang and Cheng (2006) also find that mergers paid for with stock are positively related to market overvaluation. Savor and Lu (2009) investigate the market-timing hypothesis and suggest that acquirers with stock payment enjoy significantly higher returns in the long-term, which is in line with Shleifer and Vishny (2003).

In addition to academic supportive evidence of market-timing theory, there is anecdotal evidence as well. Taking the deal of America Online and Time Warner as an example, America Online's stock price was at the highest in history during the month prior to the deal announcement and then dropped approximately 80% over the following four years.

However, some literature also finds inconsistent results and explains M&As with other theories. Harford (2005) suggests that M&As are driven by economic shock, institutional regulation, and technology development. Gugler, Mueller, and Weichselbaumer (2012) and Fu et al. (2013) find that acquirers with overvalued stock do not have better performance than other overvalued firms not conducting mergers, indicating that acquirers cannot take advantage of stock overvaluation to protect firms from falling share

prices in the long-term. Eckbo et al. (2018) develop hypotheses according to information asymmetry and argue that mergers are driven by the acquirer's concern about adverse selection of a target firm and that the percentage of stock provided by acquirers significantly increases when there is more information on the valuation of the acquirer's stock.

2.3.6 Motivations for Cross-border M&As

M&As can be motivated by three factors (Angwin, 2007): economic growth realisation, strategic consideration, and behavioural incentive. An extensive body of research explains cross-border mergers with neoclassical theory. It suggests that cross-border deals are conducted as an efficiency-improving strategy to allocate resources in a larger market and thus increase market power and operating efficiency. For example, Mitchell and Mulherin (1996) argue that acquirers take over overseas targets to deal with industry shocks due to deregulation, trade liberalisation, or other institutional changes. Taking the deregulation of the European Union as an example, a large number of acquirers from other markets are attracted to it and have taken over target firms in sectors such as energy and banking. In terms of the deregulation in home countries, Chinese acquirers have significantly increased cross-border M&As since the 2000s as China has started to relax capital control and remove barriers to overseas investment. Kang and Johansson (2000) report that cross-border M&As in several industries (petroleum, finance, and the motor industry) are driven by international competitiveness. Barkema and Vermeulen (1998) suggest that cross-border M&As are conducted as international expansion strategies to enter foreign markets. However, the literature on corporate finance argues that cross-

border M&As are investment strategies and thus are conducted to generate gains for shareholders.

Hijzen, Gorg, and Manchin (2005) review the literature and classify the motivation of cross-border M&As into three groups: firm-, industry- and macro-level driving forces. Evenett (2003) argues that multinational M&As result from globalisation. For bidders from developed markets, they conduct cross-border deals to increase scale and reduce costs. For bidders from emerging markets, overseas deals are made to gain access to resources and advanced intangible assets, such as natural resources, brands, more skilled talent and technology (Eun, Kolodny and Scheraga, 1996). For example, firms in countries with less advanced technology are more likely to conduct cross-border acquisitions to acquire more advanced technology (Bertrand and Zuniga, 2006). The number of cross-border deals with acquirers from developing countries has increased since the early 2000s, and especially since the global financial crisis in 2008 (Godement, Parello-plesner, and Richard 2011; Sun, Peng, Ren, and Yan,2012).

For Chinese cross-border M&As, there are several additional driving factors. The main one is to acquire technology and resources. Shimizu et al. (2004) point out that firms from developing countries such as China might conduct cross-border M&As in developed countries to acquire intangible assets such as patented technologies. Second, overseas M&As are motivated by increasing market share and entering new markets. It is quicker and cheaper than establishing an international branch with foreign debt when there are organisational constraints and cultural and business practice differences (Datta and Puia, 1995; Barkema and Vermeulen, 1998). Taking Lenovo and IBM as an example, Lenovo conducted a cross-border acquisition to expand its PC market share in overseas

markets and avoid trade barriers. Third, cross-border M&As are motivated by diversification, which offers opportunities to reduce risks and costs of entering new markets. According to Boateng and Glaister (2003), risks can be decreased with assets, services, and products allocating in various markets, which could also help firms achieve synergies (Friedman and Gibson, 1988 and Trautwein, 1990). Table 2.1 reviews literature on cross-border mergers and acquisitions conducted by companies in emerging markets.

The previous literature has investigated determinants of cross-border M&As and the determinants can be categorised in three groups: firm-, industry- and country-level factors (Boateng, Naraidoo, & Uddin, 2011; Collins, Holcomb, Certo, Hitt, & Lester, 2009; Shimizu, Hitt, Vaidyanath, and Pisano,2004).

2.3.6.1 Firm-level factors

Firm-level factors including firm size, multinational experience, development strategy have an effect on cross-border mergers. Forssback and Oxelheim (2008) find that overseas investment is driven by financial characteristics including financial performance and cash flow. They later (2011) report that firms with higher equity valuations and firms listed on large stock exchanges tend to participate in cross-border acquisitions. Similarly, Pablo (2009) suggests that companies acquiring targets in Latin America are more likely to hold higher market-to-book and cash and equivalents to total assets ratios than those acquiring firms in local mergers. Raff et al. (2012) investigate direct international investment by Japanese companies in 21 developed countries between 1985 and 2000. Their results show that companies having higher levels of productivity may employ greenfield investment strategies instead of international acquisition. Chen et al. (2009)

find that companies in the East Asia region are less likely to conduct cross-border transactions due to financing constraints. Investigating 173 US companies between 1990 and 1999, Paul and Wooster (2008) find that companies featuring greater advertising intensity and higher sales growth tend to conduct cross-border acquisition to increase market share and seek market advantages. Zhu et al. (2011) examine a sample of 537 cross-border and 1,171 domestic acquisitions in emerging markets between 1990 and 2007 and find that acquirers in multinational deals tend to have a larger firm size and better financial performance than those in domestic deals. Additionally, overseas acquirers are more likely to take over target firms in less competitive industries in hosting countries.

A huge amount of organisational learning literature suggests that companies' internationalisation strategies are influenced by experience (Barkema and Vermeulen, 1998; Theodorakopoulos and Figueira, 2012). Very and Schweiger (2001) examine cross-border M&As in the US, Germany, France, and Italy and find that acquirers with previous knowledge or experience in the host country are positively related to subsequent foreign market entry strategies in the same country. Collins et al. (2009) also report consistent results. Nadolska and Barkema (2007) examined 1,038 cross-border mergers in the Netherlands over three decades and find that firms conducting overseas transactions have significant international experience. Francis et al. (2014) investigate 317 multinational mergers made by US acquirers in developing countries between 1993 and 2010 and show a positive relationship between deal completion and previous merger experience.

2.3.6.2 Industry-level factors

In addition, earlier literature on industrial organisation and economics also examines industry-level factors that drive cross-border acquisitions (Ovtchinnikov, 2013; Zou & Simpson, 2008; Kang & Johansson, 2000). It argues that not only can the strong capital and management expertise of acquirers affect M&As, but so can technology shocks and industry booms. Taking the telecommunications industry as an example, it has been one of the emergent sectors offering a huge number of opportunities because of economic reforms and technological innovations. Hitt, Franklin, and Zhu (2006) also suggest that sectors with high technology intensity tend to see firms entering other growth markets to increase market share and hedge risks. Kang and Johansson (2000) find that cross-border mergers are particularly influenced by market competition and structure. Zou and Simpson (2008) investigate Chinese cross-border M&As with industry-level samples between 1991 and 2005. Their evidence suggests that overseas deals are likely to be related to industry characteristics, such as technology intensity, industry profitability and economic reforms. Ovtchinnikov (2013) examines cross-border acquisition with a large sample of 41,853 deals between 1960 and 2008 and reports that deregulation exerts an influence on overseas mergers.

2.3.6.3 Country-level factors

Country-level factors including exchange rates, cultural and physical distance, market growth and institutional laws both at home and in the host countries, are also determinants in conducting overseas deals. The factors are grouped into the following

areas: economic and financial factors, cultural factors, regulatory factors, geographical factors and political factors.

Regarding economic and financial factors, Yang and Yi (2008) report a relationship between a country's financial development and economic growth. The rationale behind it is that financial systems and development play significant roles in the capital market and regulatory framework and will influence economic growth; for example, international trade and a country's inward and outward investments. Kang and Johansson (2000) find that during the currency crisis in 1997, outward investments made by Asian countries such as international M&As decreased. Moskalev (2010) suggests that the openness of the host country that is subject to the global economy is considered when bidders conduct overseas acquisitions. Fedderke and Romm (2006) report that the determinants of foreign direct investment (FDI), including political and economic stability, infrastructure, regulation and market size, are important factors in multinational mergers. Uddin and Boateng (2011) find that there is a negative relationship between inflation rate and inward M&A investment and a positive relationship between inflation rate and outward merger transactions.

For cross-border M&As, the previous literature mostly focuses on the UK and US markets because of the availability of data (Vasconcellos, Madura and Kish, 1990; Vasconcellos and Kish, 1996; Akhigbe, Martin and Newman, 2003; Hijzen et al., 2008; Coeurdacier et al., 2009). More recently, there has been increasing interest in cross-border mergers in emerging markets (Ang, 2008; Chen et al. 2009; Fedderke and Romm, 2006; Pablo, 2009; Wang, 2013). Vasconcellos, Madura and Kish (1990) looked at a US sample and show that the acquirer's and target's exchange rates, economic conditions and

product diversification are positively related to overseas acquisitions, while information asymmetry, monopolistic power and institutional laws have the opposite effect. Vasconcellos and Kish (1996) investigate multinational mergers in the US and Canada between 1982 and 1990 and show that lower debt yields in Canada drive Canadian companies to take over US targets. Vasconcellos and Kish (1998) further examine cross-border mergers between US and European countries from 1982 to 1994. Their evidence suggests that overseas mergers are motivated by country-level factors including exchange rates, government policy, regulation, financial markets and economic conditions. The results show that cross-border M&As tend to be conducted when the home country has higher bond yields than the host country.

Di Giovanni (2005) investigates cross-border mergers between 1990 and 1999 with a gravity methodology and shows that both inward and outward capital flows are clearly influenced by institutional and financial market conditions, and financial market size plays an important role when a company conducts overseas mergers. Bilateral agreements on service and capital tax are also key determinants for inward merger investments, whereas high tax rates and bilateral distance are less favoured. The evidence also suggests that every 1% increase in the stock market to GDP ratio is related to a 0.955% increase in the probability of cross-border M&As. Hijzen et al. (2008) examine overseas mergers in OECD countries between 1990 and 2001 and show that trade barriers such as overseas transaction costs are negatively related to outward merger investments.

Coeurdacier et al. (2009) investigate cross-border acquisitions in the European market. Their results show that every 10% drop in corporate income tax is associated with a 68% increase in outward merger investment in service and manufacturing sectors, suggesting

that profitability plays an important role. Consistent with other literature, they also find that trade barriers and trade protection are less favoured by cross-border M&As. With 210 large merger transactions in the US, Kiymaz (2009) finds that the acquirer's country risk ratings have a significant effect on multinational mergers.

Forssbæck and Oxelheim (2011) examine 1,400 European acquirers conducting cross-border M&As between 1996 and 2000. Their findings suggest that acquirers in more mature markets in terms of economy and politics are more likely to conduct cross-border transactions to achieve synergies. Uddin and Boateng (2011) examine UK samples from 1987 to 2006 and show that outbound acquisitions are driven by real GDP and interest rates, while inbound acquisitions are motivated by fiscal policy, real GDP and stock market value. For example, increased interest rates and higher stock market valuation result in more outbound acquisitions.

Pablo (2009) investigates 868 cross-border M&As in emerging markets from 1998 to 2004. The evidence shows a positive relationship between the level of economic freedom and the business environment of the target country and the number of merger transactions. Acquirers conducting multinational mergers also tend to have a better economic condition than those conducting local mergers. Inward merger investment is also motivated by the target country's infrastructure development, trade openness, lower corporate tax rate, financial deregulation policy and level of government intervention. Regarding Asian markets, Ang (2008) examines a sample in Malaysia and finds that the target country's real GDP is one of the determinants of inward investment; every 1% increase in real GDP is related to a 0.95% increase in foreign investment. Chen et al. (2009) investigate overseas mergers in East Asian countries between 1998 and 2005 and

find that cross-border acquisitions are driven by better corporate governance and well-developed financial market development. In addition, family- and state-owned companies tend to conduct acquisitions in local markets, while firms in high-tech industries are more likely to conduct multinational acquisitions.

Fedderke and Romm (2006) examine overseas investment in African markets between 1960 and 2002. Their findings suggest that factors favoured by cross-border investors are higher GDP growth rate and economic openness, while factors less favoured are political uncertainty and foreign investment restrictions. More recently, Agbloyor, et al. (2013) have reported similar results with a large data set of 42 countries from 1970 to 2007. They show that advanced financial systems, better infrastructure facilities and economic openness lead to more FDI.

Among country-level factors, institutional and regulatory factors are regarded as one of the most important in determining cross-border M&As. Shimizu et al. (2004) report that to protect local firms and generate more revenue, governments tend to impose restrictions on foreign ownership and levy higher taxes on foreign companies. This is also mentioned by Bittlingmayer and Hazlett (2000) who find that bureaucratic interest and local market protection are linked to a country's regulation system. Consequently, firm development strategies to enter a foreign market, such as joint ventures and M&As, are likely to be influenced by a country's regulatory framework. Rossi and Volpin (2004) find that countries with better investor protection and higher accounting standards experience higher growth in cross-border M&As.

2.3.6.4 The effects of macro-economic factors on cross-border M&As

Prior literature has studied the effects of macro-economic factors on M&As in both home and host countries. Buckley et al. (2007) and Kolstad and Wiig (2009) study the macro-economic effects of host country characteristics on M&As. Buckley et al. (2007) find that high exports and imports, and high GDP, high inflation rate and culture proximity to China increase with Chinese FDI, suggesting that a close trade partnership tends to boost M&A volume. Kolstad and Wiig (2009) examine the joint effect of institutional and natural resources on M&As. Chinese firms are likely to invest in overseas targets of the weaker institutional environment and with abundant natural resources. Cheung and Qian (2008) find a similar result using the ratio of fuel, ore and metal exports to total merchandise exports as a proxy for natural resources.

Unlike these studies, Tolentino (2010) focused on the macro-economic factors of the home country. His study shows the openness to the emerging country's economy to trade, interest rates and the exchange rate has a significant influence on FDI outflow. Others study macro-economic factors on M&As from the perspective of developed markets. Uddin and Boateng (2011), studying cross-border M&As involving UK firms between 1987 and 2006, find that GDP, exchange rate, interest rate and share prices have pronounced influence on the level of UK outbound M&As, while GDP, money supply and share price have significant effects on inbound M&As. Choi and Jeon (2010) study the effect of macro-economic factors in the US market and find that macro-economic factors can explain the trend of US M&As and stock market conditions are one of the important macro-economic factors in determining M&A volume. Using bilateral Canadian-US data, Georgopoulos (2008) finds that the deprecation of the Canadian dollar

against the US dollar attracts more US firms to Canadian firms. This result is similar to the European M&As of Canadian firms.

2.3.6.4.1 Exchange Rates

Froot and Stein (1991) first put forward the effect of a depreciated currency on FDI inflows, showing that lower exchange rates offer foreigners more incentives to acquire productive corporate assets at low cost. Similarly, Blonigen (1997) proposes a similar 'asset acquisition' theory, with the assumption of market segmentation. Erel et al. (2012) provide empirical evidence that countries whose currencies have appreciated are more likely to be acquiring firms, and vice versa. After controlling for overall time trends econometrically, they show that short-term movements between two countries' currencies increase the propensities of firms in the country with the appreciating currency to purchase firms in the country with the depreciating currency. In line with this, Georgopoulos (2008), using bilateral Canadian-US data on M&As, finds the depreciation of the Canadian dollar against the US dollar increases the probability of Canadian firms being acquired by US firms, but this finding is limited to the sample of high R&D industries. Practical verification of such a relationship was that when the Japanese Yen appreciated relative to other major currencies in the summer of 2010, a substantial number of Japanese firms intended to expand overseas (Economist, 2010).

Kindleberger (1969) suggests that when domestic firms produce goods for sale overseas or compete in their domestic market with overseas competitors, it is likely that domestic firms' profits will increase following permanent currency appreciation, making them attractive to foreign acquirers. There are many ways through which even permanent valuation differences affecting merger propensities and performances through lowering

the cost of capital for acquiring firms under foreign control and allowing potential foreign acquirers to bid more aggressively than the domestic rival bidders.

Black et al. (2012), to the best of our knowledge, have produced the only study looking at the effect of RMB appreciation on bidder wealth creation. They expected that RMB appreciation would benefit acquiring firms' wealth creation by providing cheaper funding, but their paper finds no evidence to support this hypothesis. Their results could be limited by the relatively small sample of 43 cross-border M&As, as the research was concentrated on merger activity before 2010.

2.3.6.4.2 Bilateral trade volume

Using 56,978 cross-border M&As between 1990 and 2007, Erel et al. (2012) find that M&A volume tends to increase with economic relationship and geographic proximity. In particular, their study shows that bilateral trade increases the likelihood of mergers between the two countries and firms with higher economic development tend to be bidders, while firms from a weaker economy country tend to be targeted. Their study provides support for the theory that bilateral trade would benefit M&As between the two countries. In addition, their research leaves an open question on which macro-economic factor has a most significant impact on the acquiring firms' likelihood of purchasing the other firm.

Consistent with the view of Erel et al. (2012), Ferreira et al. (2010) show the important role of the bilateral trade in explaining the volume of cross-border M&As. In their study, bilateral trade is used as a proxy for economic integration and well economically integrated countries tend to have a high volume of cross-border M&As. Their country-

pairs analysis shows that cross-border M&A activity is more frequent between countries with larger bilateral trade volume.

2.3.6.4.3 Stock valuations

Another important factor in determining bidder shareholder returns on acquisitions is the difference between the stock market returns of the acquirer and target country. Shleifer and Vishny (2003) propose a market-timing model in which an overvalued bidder tends to buy a less overvalued or undervalued target with stock payments. Their model assumes that the market is less than fully rational while the bidder manager is rational and target managers voluntarily accept the overvalued stock. Such misvaluation-driven M&As tend to create arbitrary opportunities.

However, it is argued that a long-term stock return reversal should be predicted as the merger is driven by fundamentals. Additionally, the key component to arbitrage in such deals is that the source of valuation difference is private information held by managers; a firm's managers should have superior information on stock movements than other participants (Rhodes-Kropf and Viswanathan, 2004; 2005). Although it is rather implausible that managers have superior information about the valuation of the overall stock market or even any particular currency as proposed above, Baker et al. (2009) suggest that managers of the target company would be willing to accept payment in a temporarily overvalued stock due to irrational expectations. Nevertheless, such acquisitions can only be accompanied by limited arbitrage. If the valuation differences are permanent, the attractions of acquisitions and the wealth gains for acquirers, especially those involve targets with cash flows in the local currency, could be unaffected by the changes in valuation.

2.3.6.5 Special Factors for Chinese Cross-border Mergers and Acquisitions

There has been a significant increase in the number of Chinese cross-border mergers and acquisitions during the latest two decades. The literature on Chinese cross-border deals is not attracted only by the rapidly growing number, but also by the Chinese unique institutional environment. First, Hellman and Schankerman (2000) point out that there is a high degree of government intervention in a company's business decision, such as financial decisions, strategic decisions and operational decisions. Previous research investigates the role of government playing in Chinese cross-border acquisitions and finds mixed evidence. On one hand, capital outflows are likely to be constrained in developing countries by governments' regulatory restrictions (Morck, Yeung, and Zhao,2008). On the other hand, firms in emerging markets tend to get support from the government, especially in areas related to a country's development strategy. Klimek (2016) examines Chiese state-owned enterprises involved in cross-border mergers between 2013 and 2015 and documents that Chinese cross-border mergers and acquisitions are motivated by achieving wider political and socialobjectives of the government and acquiring strategic assets to improve the global status of the Chinese economy, which could be explained with the weaknesses of competitive advantages (Zheng, Wei, Zhang and Yang, 2016).

Chen and Young (2010) and Wu and Xie (2010) examine the relationship between government ownership and the performance of Chinese cross-border mergers and find negative effects of government ownership on acquirer's performance in both short- and long-run. However, Du and Boateng (2015) find inconsistent evidence, andNicholson and Salaber (2013) fail to document any significant effects.

One of the significant topics attracting attention is that takeover premium in Chinese cross-border mergers and acquisitions is remarkably higher than European acquirers, which could be explained with government support (Urbšienė, Nemunaitytė and Zatulinas, 2015). It is argued that higher than average premiums are likely to harm shareholders' wealth. However, this effect could be offset by government support of financing and creating a favourable business environment and (Du and Boateng, 2015). Zhou, Gou, Hua and Doukas (2015) find consistent evidence on this view that state-owned enterprises experience significantly better stock and operating performance in cross-border mergers and acquisitions. Boateng and Bi (2014) examineses Chinese domestic mergers and document that state-owned enterprises tend to make payments to target firms with more cash as they can get more access to government funds. Another explanation is that cash payment is likely to diminish dilution of government ownership and therefore facilitate post-acquisition integration process. However, by investigating 6,000 outward acquisitions by Chinese state-owned enterprises, Gu and Reed (2016) fail to find supportive evidence.

2.4 M&A Process

The M&A process plays a critical role in deal outcomes (Cartwright and Schoenberg, 2006; Haspeslagh and Jemison, 1991; Lasserre, 2003). This section reviews the related literature to give a better understanding of the success of mergers.

Prior studies have identified three major stages of M&A activity: pre-acquisition, negotiation and post-acquisition. Boland (1970) divides the merger process into pre- and post-merger. Graves (1981) describes the merger process as having four stages: planning,

anxiety, acquisition and evaluation. Marks (1982) identifies three phases: pre-merger, legal combination and post-merger. Buono and Bowditch (1989) suggest that there are seven: pre-merger, planning, announcement, initial combination, legal combination, post-merger and psychological combination. Galpin and Herndon (2000) identify five stages: formulate, locate, investigate, negotiate and integrate. Parenteau and Weston (2003) group the whole merger process into four: planning, target screening, due diligence and implementation, and deal integration.

2.4.1 Pre-Acquisition Planning Process

Previous literature describes the pre-merger planning process as consisting of synergy generation, target selection and due diligence (Jemison and Sitkin, 1986; Haspeslagh and Jemison, 1991; Galpin and Herndon, 2000 and Lasserre, 2003).

Jemison and Sitkin (1986) suggest that evaluating acquirer and target firms' fit in terms of strategy and organisation plays an important role in acquisition and synergy creation. Strategic fit is related to a company's growth strategy and a company can conduct horizontal, vertical or conglomerate mergers (Howell, 1970; Salter and Weinhold, 1981; Shelton, 1988; Haspeslagh and Jemison, 1991). In terms of organisational fit, the literature suggests that the administrative and cultural relationship between acquirer and target firm is important for post-merger performance (Buono and Bowditch, 1989; Callahan, 1986; Datta, 1991; Ferracone, 1987; Hayes, 1979; Jemison and Sitkin, 1986; Leighton and Tod, 1969; Magnet, 1984; Sales and Mirvis, 1984; Seed, 1974).

Regarding target selection, it is suggested that the right target is chosen with consideration of the firm's strengths and weaknesses (Angwin, 2001; Kitching, 1967;

Schweiger et al., 1994). Target selection is closely related to merger decisions such as takeover premium, payment methods and merger performance. Barney (1991) provides insights on target selection with the resource-based view (RBV) and argues that it would be significantly more valuable if a firm could have access to different resources. The RBV identifies three levels. To achieve synergies, acquirers need initially to identify resources. Grant (1991) suggests that there are two types of resources: intangible resources, such as copyrights and patents and tangible resources, such as inventory and machinery. Capron et al. (1998) suggest five resources: marketing, financial resources, research and development, managerial and manufacturing. In addition, the acquirer is required to identify the similarity and relationship between its own resources and those of the target firm (Rumelt, 1984). Last, the information on the pros and cons of the target's resources should be gathered and evaluated for the purpose of merging two organisation's resources successfully. Denrell et al. (2003) suggest a risk arising from the uncertainty of target resources' value due to asymmetric information, which could be reduced by acquiring a firm in the same country (Capron and Shen, 2007; Seth et al., 2000).

Due diligence is another important analysis at the pre-acquisition planning process, which includes research and evaluation of the target firm's legal and financial aspects, such as ownership, structure, integration costs and assets assessment (Angwin, 2001; Harvey and Lusch, 1995; Knecht and Calenbuhr, 2007). The analysis is motivated by gathering sufficient information on the target firm and laying a solid foundation for merger negotiation and final decisions like takeover premium (Angwin, 2001; Haspeslagh and Jemison, 1991; Lasserre, 2003; Sacek, 2015). Capron and Pistre (2002) also argue that

complete due diligence before the merger is negatively correlated to the integration time after the merger because it can shorten a firm's post-merger learning curve.

2.4.2 Negotiation

With a potential target, acquirers conduct negotiation during a courtship period that enables the two firms to develop a mutual understanding prior to deal agreement (Colombo et al., 2007; Jemison and Sitkin, 1986; Kitching, 1967). Sebenius (1998; 2002) regards a successful negotiation as a process of accurate and efficient information exchange between two parties, which could result in the mitigation of conflicts of interest. Previous literature suggests that cooperation on projects, joint ventures and accurate communication can facilitate negotiation (Angwin, 2000; Gomes et al., 2013; Hubbard and Purcell, 2001). By conducting an efficient negotiation, there would be less information asymmetry between the acquirer and target firms, therefore increasing the probability of success (Jemison and Sitkin, 1986).

2.4.3 Post-Merger Integration Process

Previous literature suggests that the post-merger process includes various activities. For example, Cording et al. (2008) regard integration as the process of combining two companies, while Pablo (1994) suggests that the integration process enables acquirers and targets to function as one entity by changing organisational structures. However, Heimeriks et al. (2012) and Puranam et al. (2006) argue that post-merger integration represents an outcome, such as the termination of the target as a standalone firm.

Haspeslagh and Jemison (1986; 1991) stress the importance of post-merger integration in a successful merger transaction with the argument that deals can only create synergies following the transition period. Other studies also argue that the process of post-merger integration is one of the most important determinants of merger strategy achievement (Christensen et al., 2011; Schweiger and Goulet, 2005; Schweiger and Very, 2003).

Schweiger and Weber (1989) suggest that although a lower degree of integration tends to result in merger failure, too much integration might also lead to an unsuccessful deal due to increased cultural differences and managerial resistance. Therefore, employing the proper integration method is important for acquirers.

The literature identifies several frameworks for post-merger integration. Napier (1989) proposes three types of integration: redesign, extension and collaboration. Haspeslagh and Jemison (1991) suggest four types: symbiosis, holding, preservation and absorption, and that the determinant factor of integration strategy is organisational autonomy. Shrivastava (1986) reports three stages of post-merger integration: procedural, physical integration, managerial and sociocultural.

2.5 Merger and Acquisition Wealth Effect

The literature on corporate finance and management has investigated merger performance over the last few decades. The following sections discuss merger and acquisition wealth effects.

2.5.1 Measurements of Merger and Acquisition Performance

Previous studies have employed several measurements to evaluate merger performance. Zollo and Meier (2008) summarise 12 measurements of acquisition performance drawn from a sample of 88 merger transactions from 1970 to 2006: overall acquisition performance, short-term financial performance, long-term financial performance, accounting performance, integration process performance, innovation performance, variation in market share, customer retention, employee retention, acquisition survival, knowledge transfer, and systems conversion. Their findings show that most research uses event studies to measure merger performance (59%), while 28% of studies use accounting ratios as the measurement. This is confirmed by Cording et al. (2010) who find that 92% of M&A studies use event- and accounting-based measurements. However, financial methods cannot fully measure merger performance as cultural and organisational fit are also important (Appelbaum et al., 2013; Schweiger and Walsh, 1990; Stahl and Voigt, 2004; Shleifer and Summers, 1988).

2.5.1.1 Short-Run Event Study Methodology

An event study is used to evaluate firm performance with share price and was developed by Fama et al. (1969) to measure abnormal returns around the event date. Fama (1970) argues that stock price should immediately and unbiasedly react to any news regarding an event in an efficient capital market. Therefore, an event window is designed to capture such a reaction. For a short-term event study, a large body of literature on M&As employs two-day (-1, 0), three-day (-1, +1), five-day (-2, +2) or eleven-day (-5, +5) windows around the deal announcement date to evaluate a firm's abnormal stock returns.

With event windows, the potential leaks of information before the deal announcement and delayed information following announcement can be captured. Although more information might be collected with a longer event window, it could also include the effects of confounding firm activities. Following Jensen and Ruback (1983), stock abnormal return is computed as:

$$AR_{it} = R_{it} - E(R_{it})$$

where AR_{it} denotes stock i's abnormal returns on day t; R_{it} denotes stock i's actual returns on day t; and $E(R_{it})$denotes stock i's expected returns on day t. Previous studies develop various models to estimate $E(R_{it})$, such as market model and market-adjusted model (Brown and Warner, 1980; Brown and Warner, 1985; Sharpe, 1963), Fama-French 3-factor model (Fama and French, 1993), Fama-French plus momentum model (Carhart, 1997), and most recently Fama-French 5-factor model (Fama and French, 2015).

Cumulative abnormal returns (CARs) can be then computedvia cumulating abnormal returns over the event window $[T_1, T_2]$, which is as follows:

$$CAR_{i,T_1,T_2} = \sum_{t=T_1}^{T_2} AR_{it}$$

According to Brown and Warner (1980), $E(R_{it})$can be computed by using a value- or equal-weighted market index in a market model and market-adjusted model:

$$E(R_{it}) = \alpha_i + \beta_i R_{mt} + e_{it}$$

where R_{mt}denotesvalue- or equal-weighted market index returns.

Regarding the Fama-French three-factor model, in addition to the market index, Fama and French (1993) also consider the size and book-to-market ratio index for estimation of expected stock returns:

$$E(R_{it}) = \alpha_i + R_{ft} + b_i\left(R_{mt} - R_{ft}\right) + s_i SMB_t + h_i HML_t + e_{it}$$

where R_{ft}denotes risk-free stock returns; SMB_tdenotes returns of a diversified portfolio consisting of small and large stocks; HML_t denotes returns of a diversified portfolio consisting ofstocks with low and high book-to-market ratios.

In the Fama-French plus momentum model, Carhart (1997) includes the momentum factor in addition to those from the three-factor model:

$$E(R_{it}) = \alpha_i + R_{ft} + b_i\left(R_{mt} - R_{ft}\right) + s_i SMB_t + h_i HML_t + u_i UMD_t + e_{it}$$

where UMD_tisthe returns of a diversified portfolio consisting of stocks withthe up and downtrends.

More recent, Fama and French (2015) added two additional factors – profitability and investment indexes – to their 3 factors model:

$$E(R_{it}) = \alpha_i + R_{ft} + b_i\left(R_{mt} - R_{ft}\right) + s_i SMB_t + h_i HML_t + r_i RMW_t + c_i CMA_t + e_{it}$$

where $RMW_t$is returns of a diversified portfolio consisting of stocks with the most and the least profitability; and CMA_t isthe returns of a diversified portfolio consisting of aggressive and conservative stocks.

2.5.1.2 Long-Run Event Study Methodology

Long-term event study captures more delayed event effects (Barber and Lyon, 1997; Fama, 1998; Kothari and Warner, 1997; Lyon et al., 1999; Mitchell and Stafford, 2000). As merger performance measured by abnormal stock returns could be changed over time with more information revealed during the integration stage, the literature also involves long-term analysis in M&A performance study.

Buy-and-hold abnormal returns (BHARs) and calendar time portfolio (CTP) are the two most employed methodologies in long-horizon event studies. According to Barber and Lyon (1997), BHARs can be obtained by using:

$$BHAR_{iT} = \prod_{t=0}^{T}[1 + R_{it}] - \prod_{t=0}^{T}[1 + R_{pt}]$$

where R_{it} denotes stock i's returns in month t; and R_{pt} denotes referenceportfolio p's returns in month t.

In terms of CTP, Jaffe (1974) and Mandelker (1974) measure a stock's long-run performance with calendar time abnormal returns, which is expressed as follows:

$$MMAR = \frac{1}{T}\sum_{t=1}^{T} MAR_t$$

where MAR_t represents mean abnormal return of an equal or value-weighted portfolio $p$consisting of all event firms in every calendar month t:

$$MAR_t = \sum_{i=1}^{nt} x_{it}(R_{it} - R_{pt})$$

2.5.1.3 Long-term Accounting-Based Methodology

The literature also employs accounting-based methodology to measure merger performance in the long-term. The profitability ratio and operating cash flow ratio are the two most-employed metrics. For profitability ratio, studies generally use return on assets or return on equity to evaluate post-merger operating performance, which can be obtained by dividing a firm's net income by its total assets and by stockholder equity book value. Ratios are then adjusted by industry by deducting the median value of the industry (Alexandridis et al., 2013; Healy et al., 1992; Ramaswamy and Waegelein, 2003). The event windows can be two or three years around the deal announcement date.

2.5.2 M&A' Performance

Although there are many studies that have examined M&A performance, there is no consensus on whether they create value for companies. The following sections review the existing research regarding M&As valuation effect in both the short- and long-term.

2.5.2.1 Short-Term

A large body of literature has provided evidence on merger performance in the short-term by evaluating the acquirer's, target's and combined entity's abnormal stock returns. Generally, target shareholders experience positive stock returns, but acquirer shareholders have zero or below on average.

Thirteen empirical studies on merger performance around announcement were reviewed by Jensen and Ruback (1983) (Asquith, 1983; Asquith, Brunder and Mullins, 1983; Bradley, Desai and Kim, 1982; Bradley, 1980; Bradley, Desai and Kim, 1983; Dodd and

Ruback, 1977; Dodd, 1980; Eckbo, 1983; Jarrell and Bradley, 1980; Kummer and Hoffmeister, 1978; Malatesta, 1983; Ruback, 1983a; Wier, 1983). Among the studies, it is well-reported that there are sizeable gains earned by target shareholders in both failed and successful deals. In terms of successful deals, abnormal returns to target shareholders are 15.9% and 7.72% in a two-day and one-month event window, respectively, indicating that most abnormal stock returns are realised on the announcement day and the day before. Similar findings are reported for failed deals, which suggests that it is difficult to differentiate successful and unsuccessful mergers around deal announcements for investors. Nevertheless, by including deal outcome day into studies, target shareholders in failed deals suffer a small loss of -2.88%.

Regarding shareholders in acquiring firms, the thirteen studies show that acquirers earn positive returns in successful tender offers but the results in mergers are mixed. Additionally, regardless of the types and the success status of the merger transaction, abnormal stock returns to acquirer shareholders are much lower than those to target shareholders. In terms of acquirer shareholders in successful mergers, other than Asquith et al.'s (1983) finding that there are positive abnormal returns of 3.48% realised by acquirers, other literature finds that that abnormal returns are insignificant. Compared to successful deals, abnormal stock returns to acquirer shareholders are significantly negative, indicating that M&As are investments with positive net value.

Bruner (2002) offers a more comprehensive review of M&A performance by including over 100 studies between 1971 and 2001. The review shows that shareholders in target firms receive considerable positive returns while there are averagely zero abnormal returns received by acquirer shareholders. Of the 130 studies, 21 show that target firm

shareholders enjoy positive abnormal returns, which indicates that a takeover premium is incorporated in stock price and delivered to target shareholders. Among 44 studies investigating acquirer firms, 17 suggest M&As generate value for acquirer shareholders, 14 suggest value conservation and 13 suggest M&As reduce value.

Tuch and O'Sullivan (2007) also review the literature on M&As' valuation effect. In terms of acquirer shareholders, it is widely reported that they suffer from negative abnormal returns. For instance, Smith and Kim (1994) examine 177 US transactions between 1980 and 1986 and find that acquirer shareholders experience abnormal stock returns of -0.23%. Sudarsanam and Mahate (2003) investigate 519 UK deals between 1983 and 1995 and find that acquirer shareholders are subject to negative stock returns of -1.4% on average. Only Franks and Harris (1989) suggest that mergers create value for acquirer shareholders.

More recent studies show a decreasing market reaction to the merger announcement, which is in line with Andrade et al. (2001). Bruner (2002) shows that the 1960s and 1970s experienced better abnormal returns around the deal announcement date than the 1980s and 1990s. This is explained by Alexandridis et al. (2010) as increasing market competitiveness. Their results suggest that acquiring firms in highly competitive markets such as the US and UK tend to suffer from negative market reactions, while those in less competitive markets tend to experience positive reactions.

In addition to the valuation effect of bidders and target firms, abnormal returns to the combined company have also been examined. The evidence generally shows that M&As generate positive returns for the combined firm, supporting the view that M&As have net present value. According to Bruner (2002)'s review, in 11 of 20 studies, the combined

firms experienced large gains ranging from $9.95 million to $120 million (Bradley et al., 1983; Banerjee and Owers, 1992; Malatesta; 1983). Mulherin and Boone (2000) and Moeller et al. (2005) also provide more recent evidence that combined entity enjoy positive returns following the deal announcement.

2.5.2.2 Long-Term

The literature on long-term M&A performance investigates completed transactions where acquirer and target have been successfully merged. Both stock- and operating-performance are widely examined.

2.5.2.2.1 Stock Performance

The literature on long-term stock performance provides mixed evidence using various approaches. Fama (1998) reports that all models measuring abnormal stock returns in the long-term are subject to criticism, therefore an improved model is needed.

The literature largely reports that M&As destroy shareholder value in the long-term. With M&A samples in the US, Langetieg (1978), Asquith et al. (1983) and Franks et al. (1991) find that acquirer shareholders suffer losses following merger announcements. Langetieg (1978) finds that acquirers experience losses ranging from -2.23% to -2.62% during the six years following deal completion. Jensen and Ruback (1983) review 7 studies and conclude that shareholders of bidders are subject to a loss of, on average, 5.5% one year after the merger announcement. Asquith (1983) and Malatesta (1983) respectively report that there are negative abnormal stock returns of -7.2% and -7.5% by acquirer shareholders during the first year post-acquisition. Magenheim and Mueller (1988)

employ a three-year event window and provide supportive evidence on M&As value-decreasing effects over the long-term. Agrawal et al. (1992) investigate the acquirer's performance over five years following deal completion. Their findings show that acquirers experience a remarkable negative abnormal return of -10% when beta and size adjusted, which is consistent with Anderson and Mandelker (1993).

However, Loughran and Vijh (1997) suggest that prior studies are flawed due to the calculation of excess stock returns. Instead of employing a rebalancing strategy, they develop a new methodology to estimate buy-and-hold returns in the long-term with the adjustment of firm size and book-to-market ratio. Following this study, Rau and Vermaelen (1998) also adjust beta to calculate buy-and-hold abnormal returns and report a negative long-term return of -4%.

By adopting a calendar-time portfolio approach to examine acquirer's long-term performance, Mitchell and Stafford (2000) also find supportive evidence on M&A value destruction and suggest that a buy-and-hold approach can result in biased statistics. By calculating both calendar-time abnormal returns and buy-and-hold abnormal returns in 12,023 M&As, Moeller et al. (2004) find similar results that acquiring firms suffer from loss during the three years following deal completion.

In the UK market, studies show that acquirers experience larger negative returns than those in the US. Franks and Harris (1989) examine 1,800 mergers in the UK between 1955 and 1985 and find that acquirer shareholders experience a significant loss of -12.6% during the two years post-acquisition. With the same event window, Limmack (1991) shows considerable negative returns of -6.87% and -14.08%, employing an index model

and market model to estimate abnormal returns, respectively. This is consistent with Limmack and McGregor (1995) and with Gregory (1997).

As the prior literature generally investigate mergers and tender offers together (Dodd and Ruback, 1977; Asquith et al., 1983; Dodds and Quek, 1985; Magenheim and Mueller, 1988; Limmack, 1991; Franks et al., 1991; Anderson and Mandelker, 1993; Loughran and Vijh, 1997), Agrawal and Jaffe (2000) differentiate these two types of deal and find that post-deal underperformance is more likely to be experienced by acquirers in mergers than in tender offers, which provides a more complete picture of M&A's wealth effect in the long-term.

In addition to a large body of evidence on UK and US markets, the literature also examines other markets' acquirer performance. Dutta and Jog (2009) focus on M&As in Canada and find that acquirers earn insignificant abnormal returns regardless of the methodologies employed. Fatemi et al. (2017) examine a Japanese sample and find that acquirers enjoy a little gain in the long-term after deal completion.

Although the underperformance of acquiring firms is largely reported in these studies, there is inconsistent evidence. By using equally- and value-weighted portfolios to estimate market return, Franks et al. (1991) suggest that the underperformance of acquirers is only related to equally-weighted portfolios, while acquirers experience a positive return with value-weighted portfolios. Consequently, they indicate that the model's measurement error is the main reason for M&A value-decreasing in the long-term.

2.5.2.2.2 Accounting Performance

In addition to stock performance, the literature also measures merger long-term performance with firms' accounting ratios. Ratios related to cash flow and profitability are popular for the evaluation of a company's operating performance during the post-acquisition period. By using the cash flow ratio of 62 acquiring firms in the US, Ravenscraft and Scherer (1987) find that there is a remarkable drop in the acquirer's operating performance following deal completion. However, by using asset productivity as a proxy for operating performance and industry performance as a benchmark, Healy et al. (1992) find that acquirers enjoy higher asset productivity during the post-merger period. This is confirmed by Switzer (1996) who suggests that acquiring firms are subject to an increase of 1.97% in cash flow ratios. Parrino and Harris (1999) and Linn and Switzer (2001) also provide consistent findings that M&As improve a firm's operating performance during the five years after deal completion. The results in Healy et al. (1992) have been criticised by Ghosh (2001) as acquirers are compared with firms without conducting mergers. By choosing a control group with company size and performance considered, Ghosh (2001) find that acquirers have little improvement in their operation after completing acquisitions.

In the Japanese market, Kruse et al. (2002) find that firms conducting mergers from 1962 to 1992 experienced a modest and insignificant increase in operating performance in the long-term, while Kruse et al. (2007) find a significant improvement of 1.54% in the acquirer's long-term operating performance when deals were conducted between 1969 and 1999.

In the UK market, Powell and Stark (2005) examine 191 M&As announced between 1985 and 1993. With different proxies of operating performance, their results show that acquirers' accounting ratios increased between 0.13% and 3.1%. Martynova et al. (2007) investigate merger transactions conducted in the UK and Continental Europe and find that acquirer's accounting performance remarkably decreased following deal completion. They conclude that this could be attributed to change in the macroeconomic environment as the control group also experienced underperformance.

More recently, there has been evidence from emerging markets. Ramakrishnan (2008) focuses on the Indian market and finds that there is a considerable improvement of 5.2% in the acquiring firm's post-merger operations. Yen and André (2010) investigate mergers in 13 emerging markets and show that an increase in the acquirer's long-term operating performance is positively related to shares held by large stockholders.

The literature also provides evidence by using profitability-related measurements. For example, Hogarty (1970) uses acquirer's earnings per share to measure operating performance and shows that there is a considerable drop in acquirer's operating performance. By employing a return on assets ratio, Dickerson et al. (1997) also find that acquirers have worse post-acquisition outcomes. Sharma and Ho (2002) use various measurements including earnings per share, return on assets, return on equity and profit margin and find that acquirers experience an insignificant change in operating performance following deal completion, which is consistent with Ghosh (2001). Yeh and Hoshino (2002) examine the Japanese market and find a decrease in acquirers' return on assets and on equity following mergers. However, Bild et al. (2010) provide evidence

from the UK market that there is a remarkable increase in acquiring firms' operating performance.

2.5.2.3 Cross-Border M&As Performance

There is an increasing trend in cross-border mergers and acquisition. Bessler and Murtagh (2002) examine multinational transactions by Canadian banks and find that cross-border deals create more value for acquirers than domestic ones around the announcement date. Chari and Ouimet (2004) find that acquirers in foreign M&As are subject to higher announcement abnormal returns if the target is in a developing market and the acquirer is in an advanced country. This is confirmed by Liu (2007) who examine the valuation effect of cross-border mergers in the UK and Canadian markets between 1985 and 2005.

In terms of Chinese cross-border M&A performance, Boateng et al. (2008) investigate multinational mergers by Chinese companies and find that acquirers experience value-increase after the transaction. They are subject to 1.32% abnormal returns around merger announcement. This sample was limited and so subject to small sample bias. Wu and Xie (2010) study a sample of 165 cross-border M&As by Chinese firms and find that pre-acquisition performance and proportion of state shares have a significant positive impact on bidder performance. Nicholson and Salaber (2013) include a sample of 63 Chinese and 203 Indian cross-border mergers and show that acquirers conducting multinational deals receive significant shareholder gains. Chinese acquirers tend to benefit from deals in the manufacturing industry, while Indian acquirers tend to gain from transactions in countries with short cultural distance.

Some scholars focus on the integration of cross-border M&As by Chinese firms (Erel et al., 2012). This is an important aspect of cross-border M&As because of bidders' and targets' inherent barriers that undermine the performance of the bidder if one cannot overcome it in the post-acquisition phase, such as cultural and geographic differences. Luo et al. (2011), studying a sample of 1,355 Chinese private enterprises, find that they have advantages such as mass-production, low-cost positions and stronger operations in complex environments, which benefit their post-acquisition integration. In a similar vein, Xie et al. (2014) find state ownership discourages SOEs from entering the foreign markets.

Bhagat et al. (2011) extend the sample of cross-border M&As by emerging market firms and find that bidders generally enjoy positive announcement returns of 1.09%. These studies suggest the market tends to react positively to firms entering a country with a better institutional environment or corporate governance. Using an event study of 425 Indian firm-initiated cross-border M&As, Gubbi et al. (2010) find that bidders can generate higher abnormal returns when acquiring targets from advanced economic markets and institutional environments. The authors attributed their results to strategic motive and institutional theory. In line with their view, Uhlenbruck et al. (2006) suggest that the reason for higher value creation generated by emerging market firms' acquisitions of developed market firms is because the developed country provides access to resources to firms searching for growth, and such access enables emerging market firms to overcome development barriers and increase competitiveness compared to their domestic rivals. Soongswang (2010) provides some additional support by investigating a sample of cross-border M&As of firms from Thailand. His study shows that bidders can

generate positive abnormal returns of over 10% three to four months prior to the M&A announcement. However, Aybar and Ficici (2009) investigate 433 cross-border mergers conducted by acquirers in the emerging market between 1991 and 2004 and find a negative market reaction to cross-border deal announcements.

Francocur (2007) investigates the acquirer's long-term performance in cross-border deals. By calculating buy-and-hold abnormal returns, the findings show that there is no increase in the acquirer's performance. Chellan and Lin (2009) find consistent evidence that Chinese acquirers do not enjoy synergies in foreign transactions. Aybar and Ficici (2009) analyse multinational M&As conducted by firms in emerging markets and conclude that, on average, cross-border transactions in emerging markets do not generate value but rather reduce value for acquirers. Bertrand and Betschinger (2012) examine cross-border mergers' long-term operating performance with a sample of 120 Russian transactions and suggest that acquirers are subject to negative returns in multinational mergers due to their low experience and capability.

In terms of target performance in cross-border deals, Fraser and Zhang (2009) employ a sample of US banks taken over by non-US banks between 1980 and 2011. Their results show an improvement in the target firm's performance. Mann and Kohli (2011) investigate Indian cross-border deals and reports that target firms enjoy positive abnormal returns.

2.6 Determinants of M&A Wealth Effect

The determinants of M&A wealth effect have been widely examined to gain a better understanding of M&As. This section reviews the literature on various determinants that

are regularly taken into account in merger studies, including firm size, payment methods, listing status of the target firm and deal attitude.

2.6.1 Firm Size

It is extensively argued that the size of the acquirer and target can influence merger performance. Studies generally use a firm's market capitalisation four weeks prior to the deal announcement to measure firm size (Fuller et al., 2002). Jarrell and Poulsen (1989) find that acquirers with a small firm size tended to enjoy more gains in the 1960s, which is also confirmed by Loderer and Martin (1990). However, it is not clearly stated that better performance is influenced by the size effect.

The first study considering firm size is Agrawal et al. (1992) who find that acquirer size is significantly related to acquirer long-term performance. A more recent study by Moeller et al. (2004) examines 12,023 US mergers between 1980 and 2001 and finds that acquirers experience an abnormal return of 1.1%. When they take the size effect into consideration, the evidence shows that large firms experience an insignificant return of 0.076%, which is significantly lower than gains to small acquirers (2.318%). The difference persists after controlling for target firm listing status and the method of payment. Billett and Qian (2008) also find consistent evidence that the size of acquirers is negatively related to acquirer's announcement performance.

Black (2013) reviews the literature and summarises several explanations raised in previous studies. First, Demsetz and Lehn (1985) suggest that larger companies tend to have more severe agency problems as the manager and owner are likely to be different parties. Therefore, large firms conducting mergers are more likely to be driven by

managerial hubris and empire building (Roll, 1986; Jensen, 1986), which is in line with Jensen and Meckling (1976). Moeller et al. (2004) find that the size of the acquiring firm has a positive impact on deal premiums, which supports the explanation of managerial overconfidence. According to Mitchell et al. (2004), the short-term underperformance of the acquirer might be due to investors' short-selling before the announcement date. As short-selling tends to be experienced by larger firms, acquirers with a large firm size earning negative abnormal returns might be under price pressure.

Alexandridis et al. (2013) analyse 3,691 mergers and acquisition in the US market between 1990 and 2007 and find a negative relationship between the size of the target firm and acquirer announcement returns. The evidence shows that acquirers taking over larger targets experience lower abnormal returns of 2.37% compared to those taking over smaller targets. To test if the underperformance is caused by overpayment, Alexandridis et al. (2013) examine the relationship between target firm size and bid premium. Their findings show a negative relationship and this suggests that the complexity of large deals is the main reason behind acquirer's underperformance.

2.6.2 Relative Size

The relative deal size to acquirer size also has an influence on the valuation effect of M&As. It is computed in the literature as the ratio of the target firm's market capitalisation divided by the acquiring firm's market capitalisation 4 weeks prior to the merger announcement. Eckbo and Thorburn (2000) find that acquirers tend to be larger than target firms. The larger the relative size difference, the larger the influence of relative size on the M&A's wealth effect. Asquith et al. (1983) examine 214 mergers in

the US market between 1963 and 1979 and find that acquirers earn higher abnormal announcement returns when the relative size is large. Acquirers are subject to abnormal returns of 4.1% when the relative size is larger than one-tenth, which is 2.4% higher than their counterparts with a relative size smaller than one-tenth.

Jarrell and Poulsen (1989) find consistent evidence in 770 tender offers in the US that acquirers' announcement abnormal returns increase with the relative size. By examining private M&As, Loderer and Martin (1990) also find supportive results that mergers with a larger relative size (>30%) generate positive returns of 1.6% for acquiring firms, while ones with a smaller relative size create insignificant returns of 0.2%. More recently, Mulherin and Boone (2000) and Fuller et al. (2002) also report a positive relationship between acquirers' short-term performance and target size relative to acquirer size. However, Pettway and Yamada (1986) examine M&As in Japan and find inconsistent results. They show that deals with a smaller relative size generate more gains to the acquiring firm.

2.6.3 Method of Payment

Many studies examine the relationship between the method of payment employed by acquirers and the merger's wealth effect. The bid premium can be paid in cash, stock, or a mix of cash and stock. According to Modigliani and Miller (1958), in a market with perfect conditions, investors should react indifferently to various payment methods as they have all information about the firm. However, investors are subject to information asymmetry in the real world that is not a perfect market. As a consequence, different reactions to different payment methods will be shown.

The framework developed by Myers and Majluf (1984) shows the relationship between the investor's reaction and a company's investment decision when the information is not the same on both sides. Equity tends to be used by firms with private information on their own value when the firm's real value is lower than the market valuation of the equity. However, the framework also points out that the firm's behaviour can be detected by investors and therefore the stock price would be adjusted based on the real value.

Building on Myers and Majluf's (1984) model, Travlos (1987) investigates the effect of method of payment on merger performance by examining 167 public mergers in the US market between 1972 and 1981 and suggests that different payment methods convey different information to investors regarding the acquirer firm's value. The results show that acquirers with cash payment earn positive returns of 0.31% around merger announcement, while their counterparts with stock payment are subject to a significant loss of -2.09% during the same time period.

Further studies find supportive evidence for this. For instance, Moeller et al. (2004) find that acquirers with cash payments experience abnormal announcement returns of 1.38%, which is much higher than those with stock payment (0.15%). Martynova and Renneboog (2006) examine 1,721 European acquisitions announced between 1993 and 2001 and find that acquirers in 54% of transactions use 100% cash payment; those in 20% of transactions use 100% equity payment; and those in 25% use mix payment. Their findings show that acquirers in cash-financed mergers earn abnormal announcement returns of 0.6%, while acquirers in stock-financed mergers earn significant negative returns around the announcement. For a longer event window of six months, the findings show that cash-financed deals generate abnormal returns of -0.9% for acquirer

shareholders, which is much higher than returns related to stock-financed deals (-2.2%). Chemmanur et al. (2009) also find consistent evidence.

There is also research showing that stock-financed mergers do not always reduce value. For example, Chang (1998) and Fuller et al. (2002) include target listing states in the analysis and find that stock-financed transactions with private targets can generate positive returns for acquirer shareholders, which are even higher than gains in cash-financed mergers. Alexandridis et al. (2010) find that stock-financed mergers destroy less value in markets with less competition.

In addition to the acquirer's short-term performance, previous studies also investigate the relationship between payment method and performance in the long-term. Similar to evidence on short-term performance, many studies find that acquirers paying with cash enjoy better performance than those paying with stock. For example, Agrawal et al. (1992) employ a five-year event window and find a higher return for acquirers of cash-financed deals. With the same event window, Loughran and Vijh (1997) suggest that cash-financed deals generate significant positive returns of 61.7% for acquirer shareholders, while the long-term abnormal returns in stock-financed deals are -25%. More recent studies, such as Sudarsanam and Mahate (2003), Ang and Cheng (2006) and Bouwman et al. (2009) also reveal consistent corroborating evidence.

Evidence of the effect of payment methods on acquirer's long-term operating performance is similar to stock performance. Linn and Switzer (2001) find that acquirers paying with cash experience greater improvement in long-term operating performance than those paying with stock. The consistent evidence is also found in Australian and Malaysian markets by Lau et al. (2008) and Rahman and Limmack (2004), respectively.

Besides acquirer's shareholder gains, the relationship between payment methods and target performance has also been investigated. Wansley et al. (1983) suggest that cash-financed mergers generate more gains for target shareholders than stock-financed mergers, which is confirmed by Huang and Walking (1987) and Martynova and Renneboog (2006).

2.6.4 Target Listing Status

A huge body of literature shows that target listing states have an influence on acquirer's performance, including Hansen and Lott (1996), Ang and Kohers (2001) and Moeller et al. (2004). The performance of acquirers taking over a private or subsidiary company is superior to that of acquirers with public targets. Hansen and Lott (1996) find that acquirers with private targets experience abnormal announcement returns of 1.15%, while those with public targets are subject to returns of -0.98%. Chang (1998) shows that mergers with private targets generate positive returns of 1.45% for acquirer shareholders, which is significantly higher than those with public targets (-1.49%).

Ang and Kohers (2001) analyse a broad sample and summarise that there were about 22,000 deals involving private or subsidiary targets and only 8,000 involving public targets between 1984 and 1996. Their findings show that acquirers taking over unlisted target firms earn significant positive returns, regardless of stock or cash payment. However, acquirers taking over public targets suffer a significant loss when they pay with stock and experience insignificant returns when they pay with cash.

Fuller et al. (2002) examine three groups of US mergers, which are deals with unlisted stand-alone targets, unlisted subsidiaries and public targets. They find that mergers with

unlisted stand-alone targets and unlisted subsidiaries create gains of 2.08% and 2.75% respectively for acquirer shareholders, whereas deals with listed targets cause significant loss of -1%. By dividing the sample into the same groups, Moller et al. (2004) find US acquirers with private, subsidiary and public are subject to returns of 1.5%, 2% and -1.02%, respectively.

This evidence is also found in European markets. Faccio et al. (2006) investigate acquisitions in west European countries announced between 1996 and 2001 and find that acquirers taking over unlisted firms experience significant positive abnormal announcement returns, while those taking over listed firms experience losses (-0.38%). Draper and Paudyal (2006) examine mergers in the UK market and find that 88% of deals include private firms or subsidiaries. Their findings support previous studies that positive abnormal returns are earned by acquirers with unlisted firms.

2.6.5 Market-to-Book Ratio

Fama and French (1993) firstly suggest that studies of the acquiring firm's performance should take the book-to-market ratio into account. Rau and Vermaelen (1998) divide acquirers into two groups: value acquirers, or companies with lower market-to-book value because of stock underperformance; and glamour acquirers, companies with a higher market-to-book value because of better stock performance. Their findings show that value acquirers experience significant positive returns three years after merger completion. However, glamour acquirers suffer a significant loss of -17% in mergers during the same period. These findings can be explained by considering that firms with a higher market-to-book value ratio prior to the merger announcement (glamour acquirers)

are more likely to have managerial overconfidence, which leads managers to overestimate synergies generated from deals and therefore experience underperformance following deal completion (Roll, 1986). In terms of value bidders, acquisitions are selected carefully and not influenced by managerial overconfidence, which results in value-increasing investment. In addition, as glamour acquirers tend to be subject to stock overvaluation, investors are able to detect and adjust stock price following the deal announcement.

By studying a sample of 519 mergers in the UK market between 1983 and 1995, Sudarsanam and Mahate (2003) investigate the influence of acquirer's pre-merger valuation ratio on its short- and long-term performance. They define value and glamour acquirers with not only the market-to-book value ratio but also the price-to-earnings ratio. In terms of short-term performance, an insignificant difference between value and glamour bidders is found. However, with long-term performance, their findings show that glamour acquirers experience significant loss ranging from -47% to -17%, which is considerably lower than value acquirers (-9% to -2%). This is in line with Rau and Vermaelen (1998).

2.6.6 Industry Relatedness

Industry relatedness also plays an important role in determining merger performance. Taking over a target firm in an unrelated industry has become more popular in the US since the conglomerate merger wave in the 1960s. Rumelt (1974) describes industry relatedness in acquisition as acquirer and target firm in industries with related resources and markets. In empirical studies, industry relatedness is defined by whether the

industries of the acquirer and target firm have the same two- or four-digit Standard Industry Classification (SIC) code introduced by the US Federal Trade Commission.

Markowitz (1952) introduces diversification in modern portfolio theory, which suggests that investors prefer diversified portfolios. Contrary to this view, at firm level, prior literature shows that undiversified mergers generate more value for acquirers than diversified deals (Rumelt, 1974; Salter and Weinhold, 1981; Singh and Montgomery, 1987). The rationale is that taking over a target in a related industry is more likely to deliver managerial, financial and operational synergies. In terms of diversified deals, operational synergies are less likely to be generated due to unrelated business. Stulz (1990) reports that diversified deals destroying value can be attributed to a firm's inefficient operation, which is also confirmed by Lang and Stulz (1994) who suggest that companies' Tobin's Q is inversely related to the diversified operation.

Morck et al. (1990) find that acquirers conducting undiversified acquisition earn higher returns of 6.97% than those conducting acquisition across industries between 1975-1987. They also find that 45.6% of acquiring firms of undiversified deals experience positive returns, while 32.2% of diversified transactions earn gains. The underperformance of diversified deals might be explained by managerial motivation, which is also agreed by Berger and Ofek (1995) and Lins and Servaes (1999).

Dividing a sample into firms diversifying or focusing across markets and businesses, DeLong (2001) reports that mergers focused on both activity and geography generate gains of 2.21% for acquirers. Denis et al. (2002) also find consistent evidence that industrially and globally diversified mergers reduce acquirer's value by -2.6% and -3.4%, respectively. Graham et al. (2002) provide an explanation for the underperformance of

diversified deals by examining target firms and find that discounted target firms are likely to be acquired in an unrelated transaction, which suggests that considering only a standalone acquirer might be biased.

2.6.7 Deal Attitude

Deal attitude plays an important role in merger wealth effect. According to Manne (1965), hostile M&As can replace targets' inefficient management with acquirers' superior operation and therefore can create synergies. Nevertheless, Morck et al. (1988) suggest that friendly acquisitions are likely to be made for value creation while hostile ones are motivated by the discipline of the target's inferior management. This is confirmed by Franks et al. (1991) who find that acquirers conducting hostile mergers experience abnormal announcement returns of -3.54%, which is significantly lower than those conducting friendly mergers. However, Franks and Mayer (1996) and Kini et al. (2004) find little evidence that targets in friendly deals have better management performance than those in hostile deals.

In terms of UK evidence, Kennedy and Limmack (1996) compare the wealth effect of hostile and friendly M&As and find that hostile and friendly acquirers earn positive abnormal returns of 0.1% and 0.3% respectively during the first post-merger year. However, acquirers in both hostile and friendly mergers suffer worse performance during the second year following deal completion, with abnormal returns of -5.4% and -6.1%, respectively.

Cosh and Guest (2001) also provide evidence on UK hostile and friendly acquirers between 1985 and 1996. Their results show that acquirers who made hostile offers enjoy

a remarkable increase of 3.1% in the 3-year post-acquisition performance, while their counterparts who made friendly offers experience a drop in abnormal returns of -0.6%. Similar evidence is found by Conn et al. (2005). Sudarsanam and Mahate (2006) examine 519 acquisitions conducted in the UK market between 1983 and 1995 and argue that only hostile bidders making a single bid enjoy outperformance.

2.6.8 Determinants of Cross-border M&A Wealth Effect

"The concerns of boardrooms have generally shifted away from macro issues to valuation when it comes to a deal" June 2015, Wilhelm Schulz, Head of Europe, Middle East and Africa M&A at Citigroup.

Previous literature suggests that performance of cross-border mergers and acquisitions is influenced by economic and financial conditions of the home market. Kang (1993) examines M&As of US companies acquired by Japanese companies and finds that the gains of acquirers are positively related to the appreciation of the yen. This supports the model developed by Froot and Stein (1991), who hypothesis that foreign acquirers will have a comparative advantage in purchasing US target when acquirers' domestic currency is strong against the US dollar. In essence, the relative wealth of acquirers should be increased by an appreciation of its country's currency, which results in a higher capability to overcome the constraints of the capital market and therefore conduct cross-border mergers. More recently, Sharma (2016) examines UK bidding firms involved in cross-border mergers and documents that the appreciation of the Sterling Pound relative to currency in target country has an positive impact on acquirers' returns. Andriosopoulos and Barbopoulos (2017) also investigates cross-border mergers made by UK firms with

the announcement date between 1986 and 2010. Their findings show that cross-border M&As generate higher gains to British acquirers when deals are announced during periods of stronger Pound Sterling relative to target country's currency, which is consistent with Sharma (2016). In addition, Andriosopoulos and Barbopoulos (2017) is the first study examining the impact of relative equity market valuation between home and host countries on acquirers' gain from cross-border mergers, and find that acquirers of cross-border M&As conducted during periods of higher equity market valuation conditions at home market relative to that in host market earn higher abnormal returns in the short-term, but in the long-term they suffer considerable losses. This finding is consistent with Bouwman, Fuller and Nain (2009) who examines domestic mergers and the relation between stock market valuation and acquirers' performance.

Regarding the impact of international trade on cross-border mergers, De Benedictis and Tajoli (2011) suggests that bilateral trade relationship between home and host countries facilitates acquirers to tackle institutional tensions in cross-border mergers. This is confirmed by Yoon and Lee (2016) whose findings show that acquirers enjoy higher abnormal returns when there is a closer trade relationship between acquirer's and target's countries. Chakrabarti, Gupta-Mukherjee and Narayanan Jayaraman (2009) examines trade of target country and documents a negative relation between acquirers' performance and target trade levels. This might be explained by considering that more trade between target and the world represents more openness and results in more competitions, which could downplay the advantages from cross-border mergers.

Besides, there has been substantial discussion on the impact of institutional distance on acquirer's performance in cross-border M&As. Morosini, Shane and Singh (1998) firstly

examines the relation between cultural distance and cross-border mergers and finds that cultural diversity increasing with cultural distance lead to higher gains for acquirers, which is supported by Aybar and Ficici (2009) and Qian, Chun, Qi and Qi (2017). However, other studies, e.g. Du and Boateng (2015) and Basuil and Datta (2015), suggest that culture distance leads to higher transaction cost and deters post-integration, which result in worse cross-border merger performance.

2.7Merger Waves

Merger wave refers to a period of time with intense M&As conducted, which is regarded as one of the common characteristics of acquisition activities (Andrade et al., 2001). There have been five major merger waves since the late 19th century, which are driven by various factors such as exogenous shocks including economic, regulatory, and technological shocks and high market valuation (Stearns and Allan, 1996; Rhodes-Kropf and Viswanathan, 2004; Rhodes–Kropf, Robinson, and Viswanathan, 2005; Harford, 2005; Martynova & Renneboog, 2008).

The first merger wave occurred between 1897 and 1904 and peaked from 1898 and 1902 following the Depression of 1883, which was also known as the "great merger movement" and composed of mainly horizonral mergers in the manufacturing sector. Kleinert and Klodt (2002) suggest that the first merger wave was driven by industrial revolution and terminated as the enforcement of the Clayton Act and Sherman Act that prevent large firms from controlling a single sector and impede horizontal acquisitions. The second merger wave occurred during the period of 1920 – 1929 and ended with the stock market crash of 1929, which consists of mainly vertical mergers, i.e. target firms are from

different stages of supply chain process, and conglomerate mergers, i.e. target firms are from unrelated sectors. In terms of the third merger wave between 1965 and 1975, Kleinert and Klodt (2002) argue that it was driven by greater positive economic growth and a large amount of production in consumer goods sectors, which was composed of mainly conglomerate acquisitions. The fourth merger wave occurred during the period of 1984 – 1988 when Ronald Reagan served as the 40th President of the US and Europe and Europe prepared for completing the Single Market. During that time, the goal of enterprises was to achive synergies by developing technologies and therefore the fourth merger wave consisted of many firms in technoloy-intensive sectors. In addition, the fourth merger wave witnessed a larger number of hostiles deals than previous waves. For the fifth merger wave, it has started since 1995, which is mainly caused by deregulation and globalization.

Harford (2005) suggests that companies react to merger waves by redeploying resources and therefore leads to reorganization of industry assets. According to the industrial organization model, early movers may anticipate the reaction of competitors, which explains the interdependence of firms' decisions (Tirole, 1988). McNamara, Haleblian, and Dykes (2008) suggest that enterprises compete to obtain the optimum combination of industry assets during merger waves, and thus companies acting early in a merger wave tend to generate early mover advantages and position themselves ahead of other rival firms. This is also mentioned by Lieberman and Montgomery (1988) that early movers in a merger wave are likely to gain competitive advantages via maintaining technology leadership, rising client's switching costs, controlling rare resources, and reinforcing network effects. A more recent study of McNamara, Haleblian, and Dykes (2008)

document similar view that acquirers acting early within merger waves are able to get access to superior information, while acquirers acting late within waves just mimic actions due to hearding effect and therefore late movers are less likely to derive competitive advantages. Consistent with this view, their findings show a curvilinear relation between the entry timing of acquirers within a merger wave and the stock performance of acquiring firms.

Andonova, Rodriguez, and Sanchez (2013) and Carow, Heron, and Saxton (2004) are motivated to investigate the relation between the entry timing within merger wave and acquirers' performance. Specifically, Andonova, Rodriguez, and Sanchez (2013) examine colombian mergers and acquisitions announced between 1995 and 2008. Their results show that experienced acquirers conducting mergers late in waves enjoy better operating performance following deals, which significantly outperform acquirers carrying out mergers at the peak of waves. Carow, Heron, and Saxton (2004) suggest that only early movers taking over targets in related industries realize competitive advantages and experience superior abnormal returns.

Duchin and Schmidt (2013) and Xu (2017) argue that acquisitions carried out within merger waves entail greater uncertainty than their counterparters conducting merger outside the wave. For example, Haleblian, Mcnamara, Kolev, and Dykes (2012) suggest that mergers conducted in the earlier phase within a wave may not be regarded as legal operations. Xu (2017) argues that the risks of adverse selection and information asymmetry related to mergers are higher for early movers, which is likely to have influence in merger negotiation. Therefore, early movers within a wave tend to be companies with superior resources and information about target firms and they may take

over potential target firms first (Haleblian, Mcnamara, Kolev, and Dykes, 2012). Boulding and Christen (2001) and Makadok (1998) explain early movers' superior performance by considering that target firms could be acquirered with lower premiums early within waves, which is argued by Fuad and Sinha (2018) as well.

In terms of Chinese evidence, it is documented that there are four merger waves. The first merger wave occurred in 1984, with mergers and acquisitions activities first appearing in Wuhan and Baoding and then spreading to Beijing, Nanjing, Chongqing, Shenyang, etc. The first merger wave was composed of state-owned enterprises and collective enterprises as Chinese government implement the separation of two rights, i.e. ownership and management right. A series of policies were introduced to encourage mergers, e.g. in 1987, the rights of small state-owned enterprises can be transferred with compensation; 1989 introcuded China's first law on mergers and acquisitions. In the 1980s, there were 6,966 mergers throughout the country, with the transaction value over 8 billion yuan. In sum, the first merger wave has several characteristics: 1) the volume and value of mergers and acquisitions was rapidly growing and merger activities expanded from a few cities to the whole country; 2) it was composed of mainly horizonral mergers, i.e. target firms are from related sectors; 3) government's invention played an important role.

The second merger wave in China occurred during the period of 1992 – 1997, which was under the background of the former Chinese Communist Party leader Deng Xiaoping's Southern Tour and the establishment of capital market economic system aiming to reform economic structure. In addition, with the continus progress on the joint-stock system reform, listed firms in China stock market began to conduct mergers and acquisition, e.g. the acquisition of Baoan – Yanzhong in 1993 and the acquisition of Zhongyuan and

Zhongcheng in 1997. In sum, the second merger wave has several characteristics: 1) as the Chinese stock market was in the pilit stage, mergers and acquisitions was driven by obtaining financing channels through shell buying to resolve financial issues; 2) it was more standardized and the wave size was larger than the first merger wave in China; 3) investment bankings started to play an role in mergers and acquisitions.

The third merger wave started in 2001. Following Asian financial crisis and China's accession to WTO, China's enterprises started to develop rapidly, resulting in that the volume and value of mergers and acquisitions significantly increased. In addition, the Chinese governments have launched a structural non-tradebale share reform program in 2005, aiming at transforming non-tradable stocks of A-share listed companies into tradable stocks. There are many famous mergers activities counducted during the third merger wave that involved large enterprises, including Lenovo, Sohu, Tsingtao Beer, Hainan Airlines and China Everbright Group. In sum, the third merger wave has several characteristics: 1) mergers and acquisitions became more diversified; 2) mergers were mainly driven by improving core competitiveness; 3) the quality of mergers increased significantly as the Chinese authorities strengthened the information disclosure mechanism.

The latest merger wave has started since 2015 and is still going on. Following the global financial crisis in 2008, countries in emerging market has played an important role in mergers and acquisitions market. In addition, the Belt and Road Intiative offers huge opportunities for enterprises to grow. From 2014 to 2017, the amount of Chinese cross-border merger transactions arrived at over $500 billion, which peaked at 2016 with over $200 billion of transaction value.

Table 2. 1: Literature review on cross-border mergers and acquisitions conducted by companies in emerging market

Study	Objective	Theoretical Perspective	Sample	Key findings
Boatenget al.(2008)	Investigate the motivation and performance of Chinese multinational mergers.	Resource-based theory	144 Chinese cross-border mergers conducted between 2000 and 2004	Chinese cross-border mergers are mainly motivated by market expansion and diversification. Increasing market power and acquiring strategic resources are also motivations.
Nayyar(2008)	Investigate the motivation of Indian multinational mergers and outward FDI.	Institutional theory	10,873 Indian cross-border mergers conducted between 2000 and 2006	Indian cross-border mergers are mainly motivated by liberalization of policy systems and greater opportunities to enter financial markets.
Rui and Yip (2008)	Examine Chinese cross-border mergers and acquisitions	Resource-based theory	Conducting interview with three leading firms including Lenovo, Nanjing Automobile, and	These three Chinese firms conducting international deals are driven by acquiring strategic resources and

			Huawei Technology	taking advantage of institutional stimulus.
Deng (2009)	Examine the motivation of cross-border deals made by Chinese firms	Institutional theory	Case study with three large Chinese firms including Lenovo, TCL and BOE.	Chinese international transactions are influenced by Chinese institutional environment.
Pradhan (2010)	Investigate cross-border acquisitions made by Indian firms	Resource-based View	139 Indian international deals conducted between 2000 and 2009	Cross-border mergers are employed as a method to expand market and access strategic assets.

Chapter Three: The Roleof ValuationDifferences Playingin Chinese Cross-border Mergersand Acquisitions

3.1 Introduction

Cross-border M&As have been employed as growth strategies by firms in developed countries for many decades to increase efficiency, mainly through synergy or economies of scale. By entering a new market, firms are offered new opportunities by acquiring new capabilities and knowledge (Shimizu et al., 2004). Over the last two decades, there has also been a significant increase in the number of cross-border M&As conducted by firms in emerging markets. This can be attributed to rapid economic growth and market liberalisation in developing countries (Gubbi, et al., 2010). With cross-border transactions, acquirers from emerging markets can get access to advanced technology and valuable assets and management skills and conduct their internalisation strategy.

China, the largest emerging economy in the world, has been actively seeking multinational M&As opportunities over the last decade. With more than $3 trillion in foreign reserves, the second-largest sovereign wealth fund and four of the largest banks ranked by total assets, China is significantly well-capitalised and on a global shopping spree, as can be seen in Gelly Automotive's acquisition of Volvo, Shuanghui's acquisition of Smithfield and Lenovo's acquisition of IBM.

According to the World Investment Report 2017, cross-border deals made by acquirers from emerging markets accounted for 23.37% of global cross-border transactions, while 22.87% of multinational mergers conducted by developing economies are Chinese cross-border deals (UNCTAD, 2017). In 2016, China's cross-border mergers experienced a dramatic increase and soared to record levels in both transaction value and deal number. According to Dealglobe's special report on China cross-border M&As for 2018, there were 407 Chinese outbound mergers completed in 2016, with a total value of $203 billion,

up from $1.7 billion in 2000. Dealogic[3]data also shows that China surpassed the US as being the top country conducting cross-border mergers. Although 2017 saw a small drop in the aggregate value of Chinese cross-border mergers due to a deleveraging campaign and capital control, the global footprint of Chinese firms has been continuously expanding with 400 outward deals valuing at $147 billion.

Despite the remarkable increase in Chinese outbound M&As, the literature mainly examines the performance of cross-border transactions by employing samples from developed markets in either the short- or long-term and finds mixed evidence (Campa and Hernando, 2004; Jory and Ngo, 2014;). In the small part of the literature investigating cross-border mergers from developing countries, little evidence is provided on the Chinese market, especially in the long-term, not to mention exploring the determinants of cross-border mergers performance.

This chapter focuses on the role which valuation differences play in Chinese cross-border M&As. The Chinese market was chosen because of its unique characteristics. First, the total transaction value of Chinese cross-border mergers has been significantly larger than in other countries in recent years (Brunswick, 2016). Second, China has a unique institutional environment and a high level of government intervention; thus Chinese cross-border transactions are likely to be influenced by government policy and tend to be conducted by state-owned enterprises as these firms can get access to finance more easily than privately-owned enterprises. Therefore, the existing evidence might not be applicable to Chinese multinational M&As.

Two country-specific factors are examined in the following sections, currency appreciation and stock market valuation, which are valuation differences between

[3]Dealogic is a financial market platform providing integrated content to global financial companies.

acquiring firm and target firm countries. Over the last two decades, the Chinese stock market has grown exponentially. According to the latest data from Carpenter, Lu and Whitelaw (2019), China has the second-largest capital market in the world after the US, with more than 3,600 companies listed valued at about $7.5 trillion in market capitalisation. Given that China's stock market has a larger valuation than most countries in the world, it would help Chinese acquirers to potentially achieve higher returns in the long run with stock payments in cross-border transactions. The less stringent stock market regulation compared to that of advanced economic countries such as the UK and US would also encourage Chinese firms to acquire overseas targets from developed countries in an attempt to enter a higher quality stock market and thus to protect the wealth of their shareholders. Previous literature largely argues that a higher level of domestic stock market activity could have a positive effect on cross-border M&As. For example, Sudarsanam (2010) suggests that a buoyant market may result in a relatively high stock market valuation and therefore increase the number of outward transactions because of the relatively low cost. Similar conclusions are also reached by Di Giovanni (2005), Wang (2008), Neto and Brandao (2009) and Vencatachellum (2013).

In addition, the RMB has experienced rapid appreciation attributed to faster GDP growth and gigantic foreign exchange reserves. Since the revaluation and reform of the RMB in 2005, the nominal exchange has appreciated by 16%. With the support of the Chinese government increasing RMB offshore liquidity, the size and scope of the offshore RMB market have expanded remarkably and rapidly. According to Erel, Liao and Weisbach (2012), the difference in the exchange rate between the home and host countries is one of

the most important determinants of cross-border deals as a strong currency can increase the likelihood of a company seeking to expand internationally.

Despite the stock market valuation and currency appreciation over the last decades playing an important role in Chinese firms' decisions to conduct outward investment, little is known about the influence of these two factors on the performance of China's cross-border mergers. By using a sample of 1,174 Chinese cross-border M&As announced between 1 January 1995 and 31 December 2016, this chapter attempts to fill this gap by investigating whether any valuation effect generated from the appreciation of the RMB and the misvaluation of the stock market has been transformed into gains for acquirer shareholders in both the short- and long-term.

According to the market-timing theory proposed by Shleifer and Vishny (2003) and Rhodes-Kropf and Viswanathan (2004), firms can be valued deviated from their fundamentals. Managers of abidding firm with a relatively high stock valuation have a direct incentive to use higher-valued stocks as a cheap currency to buy the assets of a firm with relatively low stock valuation. However, mixed evidence on the wealth effect of valuation-motivated mergers has been reported (Fu, Lin and Officer, 2013; Savor and Lu, 2009; Moeller, Schlingemann and Stulz, 2005). Agency theory suggests that managers of acquiring firms might employ the inflated currency and overvalued stock to conduct mergers in their own interests to achieve private benefits and build empires, which might reduce shareholder value. The stock market misvaluation theory could also be applied to currency movements and the rationale would be the same. Acquirers from a country with a strongly appreciated currency can take advantage of its inflated value to take over targets in a country with a weaker currency.

This chapter obtains the country-level stock price in local currency for each country from DataStream. The data on exchange rates for each currency directly quoted with the US dollar as the base currency is also acquired from WM/Reuters via DataStream. To examine whether stock market fluctuations in home and host countries have an influence on cross-border deals' performance, it calculates the difference between the real stock market return of acquiring firm and target firm countries over the twelve-month prior to the deal announcement (STOCK12). In terms of analysis of currency movements, it computes the difference between dollar-based exchange rate returns of the acquirer and target firm countries during the twelve-month period before the merger announcement (CURRENCY12).

The findings show that there is a significant positive relationship between the wealth effects for acquirer shareholders and the difference between stock market returns of acquirers and target countries in the short-term. The results from univariate analyses suggest that cross-border deals with large stock market return differences generate 2.16% abnormal returns for acquirer shareholders over the 3 days around merger announcement, which is 1.64% significantly higher than their counterparts with small stock market return differences. Multivariate analyses provide consistent evidence. According to the regression, the estimates imply that every 1% increase in the stock market returns different results with an increase of 14.70% in acquirers' cumulative abnormal returns.

Similar evidence has been found on the effect of the difference between exchange rate returns of acquiring firm and target firm countries. The univariate results show that acquirers from countries with a more overvalued currency compared to the target country enjoy a 1.61% higher abnormal announcement returns than those from countries with a

less overvalued currency. After controlling for other determinant factors, the findings suggest that every 1% increase in the exchange rate return difference is associated with a 65.97% increase in acquirers' short-term abnormal returns.

Although acquirers can earn positive returns around announcement by taking advantage of valuation difference between acquirer nation and target nation, this chapter also conducts analysis on the long-term stock performance of cross-border M&As to test whether these are good deals which serve the interests of acquirer shareholders in the long-term. The results show that there is a significant negative relationship between acquirers' long-term performance and the difference between stock market returns of acquirers and target countries, while long-term performance is positively related to exchange rate return difference. This suggests that deals driven by higher stock valuation do not generate synergy gains, which might be because of taking target in a nation with relatively low market valuation results in the reversal of the acquirers' valuation. Alternatively, investors may overestimate deal synergies in high valuation stock markets and correct the stock price gradually as they realise that the initial expectations might not be fully realised. The valuation reversal is not found in the analyses of exchange rate returns, indicating that acquirers taking advantage of highly appreciated currency can create synergies in the long-term.

This chapter contributes to the existing literature in several ways. First, the results contribute to the literature on cross-border M&As (Rossi and Volpin, 2004; Chari, Ouiment and Tesae, 2009; Erel, Liao and Weisbach, 2012; Dinc and Erel, 2013; Karolyi and Taboada, 2014). Most of the existing studies focus primarily on the driving factors of multinational M&As and the influence of host-country characteristics on transactions.

This study adds to this literature by studying the effects of country-level factors of both home and host countries on the performance of cross-border M&As. Second, to the best of our knowledge, this is the first study that examines the effects of valuation differencesin stock valuation and currency between China and target nation on Chinese acquirer performance. Third, this study contributes to the literature on agency motive in M&As (Lin, Officer and Zou, 2011). Previous research mostly provides evidence on US domestic mergers, but this chapter reports that acquirers with relatively high-valued stocks or inflated currencies are less likely to generate returns for their shareholders and suggests that agency conflicts also exist in cross-border deals.

The remainder of this chapter is organised as follows. The next section presents the literature review. Section 3.3 develops hypotheses. Section 3.4 describes sample and methodology, and Section 3.5 records and analyses the empirical results. Section 3.6 conducts a robustness check and the last section concludes the study.

3.2 Literature review

3.2.1 Misvaluation and M&A activity

Previous literature largely argues that mergers and acquisitions are influenced by misvaluation. A model developed by Shleifer and Vishny (2003) examines the influence of valuation on M&As with the assumption of rational managers and less-than-fully-rational market. According to their model, acquirers tend to be those firms that are overvalued while target firms are those firms that are less overvalued or undervalued. Shleifer and Vishny (2003) also predict that acquirers tend to use cash as a payment method when target firms are undervalued while stock payment is likely to be employed

as a heap currency when target firms are overvalued but less than acquirers. For acquiring firms, their management has an intention to maximize shareholder value by exploiting market misvaluation in an inefficient market. For target firms, the misvaluation model suggests that target managers are irrational and tend to care more about short-term gains rather than long-term ones, and therefore acquirers' overvalued stocks are accepted for a cash-out purpose.

However, Rhodes-Kropf and Vismanthan. (2004) argue that target managers are rational and mistakenly accept acquirer's overvalued shares. According to their model, target managers overestimate merger synergies when market valuation is high and therefore accept acquirer's overvalued stocks. Following this study, Rhodes-Kropf, Robinson and Viswanathan (2005) suggest that there are three sources of valuation errors by decomposing the market-to-book-value ratio into three components: firm-specific error that is the difference between a firm's fundamental value and its market value, time-series sector error that is the deviations of a firm's fundamental value from long-run fundamental value, and long-run growth opportunity that is the deviations of a firm's long-run fundamental value from long-run book value. The findings show that acquirers with higher market-to-book-value ratio are likely to take over firms with lower market-to-book-value ratio, which is attributed to firm-specific error and time-series sector error.

Empirical studies provide supportive evidence on the misvaluation model. For example, Dong, Hirshleifer, Richardson and Teoh (2006) find that mergers conducted in market with high valuation are likely to be drive by misvaluation. With a large sample of 3,732 U.S. mergers announced between 1978 and 2000, the evidence shows that misvaluation theory has more explanatory power over mergers and acquisitions carried out after 1990,

while Q-theory offers a better explanation for mergers announced before 1990. In addition, the authors show that acquirers tend to be firms with a higher valuation while targets tend to be firms with a lower valuation. Furthermore, their findings show that more overvalued acquirers are likely to use stock payment instead of cash payment and tend to offer higher deal premiums. Ang and Cheng (2006)examine acquirer's long-run performance in stock-financed deals and find that acquirers experience better performance by paying with their overvalued stocks, which is consistent with Shleifer and Vishny (2003).

However, previous literature also finds inconsistent evidence. For example, Fu, Lin and Officer (2013) document that acquirers' shareholders only take advantages of overvalued stocks when takeover premiums are at a low level. Both stock and operating performance in the long-run are examined.

Specifically, their findings show that overvalued acquirers significantly underperform acquirers that are not overvalued in the long-run, which is due to overpayment and weakness in corporate governance structure. Eckbo, Thorburn and Wang (2016) challenges the misvaluation theory by suggesting that acquirers use stock payment due to financial constraint.

In terms of misvaluation-driven cross border mergers and acquisitions, previous literature suggests that Similar capital assets can be bought at different prices in different markets because markets in different countries are not perfectly integrated. The relation between valuation difference and cross-border mergers can be explained by differential misvaluation of host and home countries. Based on this hypothesis, acquirers of a country

with high valuation of stock market are able to use overvalued stocks as cheap financial capital to take over a target of a country with relatively lower stock market valuation, which is an application of the misvaluation model developed by Shleifer and Vishny (2003).

3.2.2 China's Mergers and Acquisitions in Overseas Markets

China's overseas merger market has experienced three stages since 1978 (Si, 2014). For the first stage from 1978 to 1991, both outbound and inbound acquisition were at a low level. From 1992 to 2005, China's merger market experienced a huge amount of inbound investment, but outbound investment is still not robust. The latest stage is from 2006, which has witnessed a rapid growth of outbound mergers. In 2016, over $200 billion was spent to acquirer overseas targets, which is six times the amount of money spent by foreign companies to take over Chinese firms. Although China's outward mergers has developed dramatically, the absolute level and volume of shares is still small in comparison with the U.S. and European markets (Yao, Dylan and Chen, 2010). For example, the value of Chinese outward mergers accounted for about 0.9% of China's GDP in 205, while this number for EU and US were 2% and 1.3%, respectively. Most of target firms of Chinese cross-border mergers are state-owned and large-scale firms from US, EU, Canada and Hong Kong, and European market has become increasingly import (Changqi & Ningling, 2010). In 2016, there was over $70 billion invested in European market, with Germany being the major destination of interest (Shepard, 2016).

There are several factors driving the development of Chinese cross-border mergers and acquisitions. First, Chinese cross-border mergers, especially mergers conducted by state-

owned enterprises (SOEs), are significantly supported by Chinese government and banks. Indeed, Dong and Guo (2013) document that SOEs play a leading role in China's outbound FDI activities. Although most of SOEs are publicly listed on stock exchange, senior executive officers are mostly appointed by Chinese government. However, compared to private firms, SOEs of cross-border mergers experience lower returns and more political obstruction (Wei, Xie and Zhang 2005). For example, the acquisition of China National Offshore Oil Corporation – Unocal (an American oil company) was withdrawn due to the strong political opposition in the US. This is confirmed by Chen and Young (2009), Wu and Xie (2010) and Tao, Liu, Gao and Xia (2017), which suggests that Chinese government ownership has a negative influence on acquirer's short- and long-run performance. According to Globerman and Shapiro (2009), there are conceptual concerns from US government to Chinese investment and the Committee on Foreign Investment in the US (CFIUS) was established to assess the threat of an inward investment to US interest.

Second, China is motivated to gain competitive advantages in the US and European markets and develop economy via inorganic growth. Cross-border mergers suffer various obstacles such as different political and legal systems, different regulation framework, different national cultures and etc. that can have negative influence on post-acquisition integration (Olie 1994; Clougherty 2005; Björkman et al. 2007; Dikova et al. 2010; Muehlfeld et al. 2012). However, cross-border mergers and acquisitions can also generate opportunities. Ghoshal (1987) and Barkema and Vermeulen (1998) suggest that a higher level of innovation could be achieved via exposure to geographical diversity as companies are likely to get access to new environment and new knowledge. Consistently,

a more recent research by Ahuja and Katila (2004) finds that companies are more likely to develop unique innovation paths when they experience a changing environment. As Chinese firms generally lag behind those from developed countries in the field of intangible resources, e.g. patents, intellectual property and technology, they are more likely to benefit from cross-border mergers and achieve inorganic growth (Deng 2004; Morck et al. 2008; Buckley et al. 2014). Fisch, Block and Sandner (2016) examine the relation between China's cross-border mergers and acquirer's innovation performance, and find that post-acquisition patent output significantly increases following deal completion.

There are several literature providing evidence on Chinese cross-border mergers. Wong and Cheung (2009) document that acquirers of Chinese multinational deals enjoy a positive return whereas target firms suffer a negative return of -2.4% around merger announcement. Boateng et al. (2008) suggest that the motivations behind Chinese cross-border mergers are associated with market power, including entering new markets and increasing market share. Nagano and Yuan (2013) investigate cross-border mergers with target firms from China and India and find that multinational acquisitions conducted in high-growth emerging markets enjoy higher synergy gains. Liu and Woywode (2013) examine Chinese acquirers in Germany and document that China's specific characteristics, e.g. long-term orientation and low individualism, have significant influences on the post-merger integration.

3.3Hypothesis development

National boundaries tend to be related to a set of factors that might exert influences on the benefits and costs of cross-border M&As, such as institutional and regulatory environment, tax environment, culture and physical distance. Due to these country-specific factors, markets around the world are not perfectly integrated and therefore there will be misvaluation across markets, i.e. valuation is biased from the theoretical price obtained in a perfectly integrated market. According to Baker, Foley and Wurgler (2009), misvaluation exists in every market, even the largest and most liquid, which can be attributed to limits to arbitrage on country-level or market irrational expectations. This suggests that arbitrage activity is likely to be conducted by multinationals. Erec, Liao and Weisbach (2012) examine the relationship between valuation level and multinational acquisition decisions and provide supportive evidence on the influence of mispricing in determining the likelihood of a firm expanding abroad.However, little is known about the relationship between the price level and the performance of cross-border mergers.

3.3.1 Misvaluation theory

Shleifer and Vishny (2003) proposes a behavioural theory in which company value diverges from its fundamental value, and assumes that managers are rational while the market is inefficient. Therefore, managers can identify deviations in a company's share price from its true value and take advantage of misvaluation in the inefficient market. Managers of companies whose stock prices are relatively higher-valued have the incentive to use their stocks to conduct acquisition and acquirer target firms with relatively low valuation. In an inefficient market, investors tend to have more confidence

in their managers and react positively to merger announcement, and therefore acquirers tend to enjoy higher abnormal returns around deal announcement when their stocks are overvalued more than target's.

However, in the long-term, after the overvaluation of acquirer's stock is corrected by the market, acquirers are likely to experience a reversal in stock performance that erases announcement gains or triggers losses. The long-run underperformance is confirmed by Petmezas (2009) who documents that the stock performance reversal is caused by investors' overestimation on the potential gains around deal announcement and correction of overestimated reaction in the long-run.

Although previous literature proposes arguments on the firm level, this is particularly interesting in the context of cross-border mergers in which differences in home and host countries' stock market valuation always exist. According to misvaluation theory, at a given level of stock market valuation at acquirer's country, acquirers are motivated to conduct mergers after identifying a target in a nation with the relatively low stock market valuation.

3.3.2 Hubris theory

Unlike misvaluation theory suggesting that managers are rational while the market is inefficient, the hubris hypothesis suggests that managers are irrational and the market is efficient (Roll, 1986). The hubris theory argues that acquirer managers tend to overestimate their ability to identify target firms, manage the acquisition and generate gains for shareholders. As a result, acquirers are likely to take over a target firm that is not as good as they believe. However, as the market is rational, investors tend to react negatively to the announcement of deals that are below expectations. Malmendier and

Tate (2009) provide consistent evidence that acquirers with an overconfident experience lower abnormal returns to deal announcement. In terms of long-run performance, as synergies are overestimated, deals might have lower quality than acquirers had expected, and thus acquirers are likely to suffer worse performance due to low acquisition quality.

3.3.3 Relative stock market valuation and gains from cross-border M&As

Based on different arguments, two sets of hypotheses are developed. First, following misvaluation theory, this study proposes the following hypotheses:

H1a: Acquirers of cross-border mergers and acquisitions with a larger stock market return difference between China and the target country will experience higher abnormal returns in the short-term.

H2a: Acquirers of cross-border mergers and acquisitions with a larger stock market return difference between China and the target country will experience lower abnormal returns in the long-term.

Alternatively, the hubris hypothesis leads to the following testable hypotheses:

H1b: Acquirers of cross-border mergers and acquisitions with a larger stock market return difference between China and the target country will experience higher abnormal returns in the short-term.

H2b: Acquirers of cross-border mergers and acquisitions with a larger stock market return difference between China and the target country will experience lower abnormal returns in the long-term.

3.3.4 Relative strength of currency and gains from cross-border M&As

Just as acquiring firms are motivated by using relatively high-valued stock to conduct mergers, acquirers of a country with an appreciated currency can also have incentives to create value by taking advantage of inflated currency to purchase target firms with less inflated or even depreciated currencies. This is because the appreciation of the home country's currency against that of the host country will potentially increase the bargaining power of the bidder. The premium offered to target firms tends to be less than the target's equilibrium value, resulting in relatively more gains to acquirers. Several studies provide evidence on the role of the strength of currency in the home country playing in determining cross-border mergers. Froot and Stein (1991) argues that acquirers tend to have a purchasing advantage when their currency is stronger than targets' currency. Harris and Ravenscraft (1991) finds that acquirers with a stronger currency experience higher abnormal returns around deal announcement. In terms of the relationship between long-term performance and exchange rate return difference between acquirers and target's countries, as currency appreciation is not related to stock market valuation and sentiment, there would be no price corrections by investors in the long-term. Chen, Officer and Shen (2014) investigate the role of currency appreciation in acquirer's performance in an international context and find that acquirers with a strongly inflated currency enjoy higher abnormal returns in both short- and long-term. Following this line of thought, this study proposes the following hypotheses:

H3a: Acquirers of cross-border mergers and acquisitions with a larger exchange rate return difference between China and the target country will have better stock performance in the short-term.

H4a: Acquirers of cross-border mergers and acquisitions with a larger exchange rate return difference between China and the target country will have better stock performance in the long-term.

However, the hubris hypothesis could also apply to the relationship between cross-border performance and exchange rate return difference between acquirers and target's countries. A relatively strong currency of acquirers compared to that of targets is likely to make acquirer managers be overconfident about the gains from acquisition and conduct mergers of low quality, which results in worse performance in both short- and long-run. Therefore, this study would expect:

H3b: Acquirers of cross-border mergers and acquisitions with a larger exchange rate return difference between China and the target country will have worse stock performance in the short-term.

H4b: Acquirers of cross-border mergers and acquisitions with a larger exchange rate return difference between China and the target country will have worse stock performance in the long-term.

3.4Data and methodology

3.4.1Sample selection

This study draws on a sample of Chinese cross-border M&As with the announcement date between 1 January 1995 and 31 December 2016 collected from the SDC database of Thomson Financial. There are 4,607 deals in the original sample. This period of two decades has witnessed a remarkable increase in Chinese outbound acquisitions. To conduct the analyses, the following restrictions are applied to determine the final sample:

1) Acquirers are Chinese companies, and target firms are registered in foreign countries.

2) Acquirers are publicly-held companies listed on the Shanghai or Shenzhen Stock Exchanges.

3) There are no restrictions on targets' public status, suggesting that target firms can be public, private and subsidiaries.

4) Acquirers have share prices and accounting data available on DataStream.

5) Both successful and unsuccessful deals are included in the sample.

The above criteria yield a final sample of 1,174 M&A deals. Among 1,174 Chinese cross-border mergers and acquisitions, 710 (60.48%) of them are completed.In addition, a set of deal characteristics is collected from Thomson One Banker, including DataStream code, deal announcement date, target nationality, effective date, and withdrawn date, public status, hostile attitude, method of payment, the status of tender offer, diversification status, state ownership and Standard Industrial Classification (SIC) code. Firms' characteristics are acquired from Thomson DataStream, including stock price, market capitalisation, leverage ratio, market-to-book ratio, total assets, cash flow ratio, etc. Country-level factors are obtained from the World Bank's World Development Indicators (WDI) dataset, including gross domestic product (GDP) and gross domestic product (GDP) per capita.

3.4.2 Measure of Key Explanatory Variables

To investigate whether stock market fluctuations exert influence on cross-border deals' performance, this study collects a country-level return index in local currency for acquirer and target countries (DataStream code: TOTMK) and calculates stock market returns over the twelve months prior to the merger announcement. The returns are then

deflated by using the Consumer Price Index (CPI) in the year 2000, which is labelled STOCK12.

To examine the role of currency movement in the performance of Chinese cross-border M&As, this study collects nominal national exchange rates from WM/Reuters (WMR) via DataStream for acquirer and target countries, which is directly quoted with the US dollar as the base currency. For each Chinese cross-border merger in the sample, nominal exchange returns for the twelve months before the deal announcement for acquirers and target countries are calculated. To calculate real exchange rate returns and get a more correct measurement on currency movement, this paper also collects inflation data of acquirer and target countries from DataStream, i.e. the Consumer Price Index (CPI) in the year 2000. Finally, it computes the average difference between the real exchange rate returns for acquirer and target countries, which is labelled CURRENCY12.

3.4.3 Descriptive and summary statistics

[Insert Table 3.1 Approximately Here]

Table 3.1 reports the summary statistics for the whole sample of Chinese cross-border M&As. Panel A presents the volume and value of transaction of the sample over time and shows that there has been a sizeable increase in the number and value of Chinese multinational mergers since 2001. 2016 saw 221 Chinese cross-border M&As, which is more than 20 times the number of deals conducted annually before 2001. This trend echoed the opening-up process in China and could be explained by several factors. First, China introduced the 'Go Global' policy in 1999, which encourages Chinese firms to actively engage in the global competition via internationalisation. Second, China joined the World Trade Organisation (WTO) in 2001, which was a milestone in China's

integration into the world economy. Third, outward direct investment is set to be one of the keystones of China's tenth five-year plan between 2001 and 2006 and the eleventh five-year plan between 2006 and 2010. Fourth, the One Belt, One Road initiative has been issued in 2013, which provides new cross-border M&A opportunities for Chinese firms. According to DealGlobe (2018), the aggregate value of China's outward mergers and investments in the Belt and Road countries increased from $16.4 billion in 2013 to $49.7 billion in 2017. These policies have facilitated Chinese companies to invest overseas and enabled them to be largely involved in the world economy and conduct cross-border business.

Panel B reports the industrial distribution of Chinese cross-border mergers, where the deals are divided using the Fama-French 12 industries classification. The statistics show that Chinese firms in the manufacturing industry and business equipment industry are more likely to acquire targets in other countries, representing 20.61% and 20.36% respectively. In contrast, Chinese firms in the telephone and television industry and the utility industries are less likely to conduct cross-border mergers. Therefore, the industry fixed effect is considered in multivariate analyses to control for the imbalance.

In terms of regional distribution, we identify six global regions. Panel C suggests that the biggest share of Chinese cross-border M&As is between China and countries in the Asia-Pacific region, which accounts for almost 50%. It is followed by Europe and North America, constituting 24.87% and 23.85% respectively. This can be attributed to the advantages of these two destinations, such as effective legal environment, sound financial systems, better corporate governance, advanced technology and tax transparency

(Anderson and Sutherland, 2015). Countries in the Middle East and Africa are less likely to be target countries and make up less than 2% of Chinese cross-border deals.

[Insert Table 3.2 Approximately Here]

Table 3.2 reports the summary deal and the firm's statistics for Chinese cross-border M&As. A list of characteristics likely to have an influence on merger performance are presented in Appendix A. A student's t-test is used to investigate whether significant differences in mean exist between sub-samples. For stock market return differences, Panel A equally divides the full sample into three groups based on the magnitude of the difference: small, moderate or large. The study observes that the transaction value (Deal Value) considerably increases with stock market return difference between acquirer and target countries. The average transaction value is $225 million for deals with a large stock market return difference, which is about $102 million larger than those with a small stock market return difference.

The statistics show that Chinese cross-border mergers with large stock market return differences are larger when comparing the relative size of the deal to acquirer's size (relative sizes are 0.4 and 0.3). It also shows that target firms in deals with a large stock market return difference are more likely to be public firms, possibly because stock price increases in China enhance the acquirer's financing abilities and they can thus afford to buy public targets that are relatively large. Moreover, this study finds that 6.26% of Chinese multinational mergers with large stock market return difference are paid entirely with stock and 23.36% are paid entirely with cash, in comparison with 3.27% and 31.37% for ones with small stock market return difference, respectively. Furthermore, the likelihood of deal completion significantly increases with stock market return difference

between acquirer and target countries, which might be explained with acquirer's greater bargaining power caused by a relatively high stock market valuation in the home country. However, the evidence of acquirer's cash flow ratio (A_CF2TA) shows little difference between deals with large and small stock market return differences, indicating that deals with a large difference tend to be paid in stock as they have a relatively higher stock market valuation, rather than lower cash flow.

Panel B shows the exchange rate return difference between acquirer and target countries. It shows that deals are 3.76% more likely to be paid entirely with stock if the RMB has higher exchange rate returns than target currencies and the difference is large, which has a statistically significant t-test result at 5% level. In addition, 47.06% of Chinese cross-border mergers with a large exchange rate return difference are diversified, i.e. acquirer and target firms have the different first two-digit of primary SIC code, which is 19.39% less likely than those with small exchange rate return difference. Moreover, the study observes that acquirers with a relatively strong currency compared to target's are more likely to complete deal.For firm-related characteristics, acquirers with more currency appreciation have a significantly higher return on assets and lower leverage ratio before deal announcement.

3.5Empirical analysis

3.5.1 The determinants of short-run performance of Chinese cross-border M&As

This study begins by examining whether Chinese cross-border mergers motivated by misvaluation create more gains for acquirer shareholders in the short-term. The event study methodology is employed to determine if there is any abnormal stock price

movement around the deal announcement. Both univariate and multivariate analysis are carried out.

[Insert Table 3.3 Approximately Here]

Table 3.3 reports results obtained from the univariate analysis. This study reports acquirers' average cumulative abnormal returns (CARs) over the three-, five- and eleven-day event window (ACAR3, ACAR5 and ACAR11, respectively). To capture the initial reaction of the stock market to a Chinese cross-border deal announcement, this study calculates abnormal returns by using the market-adjusted return model developed by Fuller et al. (2002):

$AR_{it} = R_{it} - R_{mt}$ (3.1)

, where AR_{it}represents the abnormal return for company i on day t; R_{it} represents stock returns for company i on day t; R_{mt} represents stock returns for the value-weighted stock exchange index, i.e. the Shanghai and Shenzhen market index on day t.R_{it} and R_{mt} are computed by taking the natural log of the stock price on day t divided by stock price on day $t-1$ for company i and the stock market, respectively.

The study adds the abnormal returns over three- [-1, +1], five- [-2, +2] and eleven-day [-5, +5] to obtain the cumulative abnormal returns (CARs), where 0 is the deal announcement day. CARs are calculated with the following equation:

$CAR_{i,T_1,T_2} = \sum_{t=T_1}^{T_2} AR_{it}$ (3.2)

, where the event period is from T_1 days prior to deal announcement to T_2 days after.

Panels A and B of Table 3 show acquirers' abnormal announcement returns across different levels of stock market return difference and exchange rate return difference between China and target countries, respectively. Overall, the evidence shows significant

differences between the sub-groups, suggesting valuation plays a significant role in acquirer's short-term performance.

In terms of stock market return differences, acquirers of Chinese cross-border mergers earn positive mean abnormal announcement returns, taking the value ranging from 1.36% to 2.43% across different event windows. After dividing the full sample by the magnitude of stock market return difference, the evidence suggests that the higher the acquirer's country-level stock market returns compared to those of target countries, the better the acquirer's announcement performance. Acquiring firms in deals with a large difference on average have returns of 2.16%, 3.59% and 3.7% for ACAR3, ACAR5 and ACAR11 respectively, which are 1.64%, 3.10% and 2.74% higher than those with small difference respectively and the difference is significant at 5% level. This is consistent with the hypothesis (H1a), which suggests that acquirers with a relatively high stock market valuation enjoy gains when targets have a relatively low market valuation.

Regarding exchange rate return differences, the statistics show a similar pattern to the relationship between stock market valuation and acquirer announcement returns, which is that acquirers earn higher abnormal returns when the RMB has appreciated more than the target's currency before deal announcement. For cross-border mergers with large exchange rate return difference, ACAR3, ACAR5, and ACAR11 of acquirers in Panel B are 2%, 4.03%, and 5.08% respectively, which are 1.61%, 3.97% and 4.41% significantly higher than acquirers of deals with a small difference. These findings are supportive of the hypothesis (H3a) that more currency appreciation of the acquirer has a positive influence on cross-border deals' performance.

The evidence obtained from univariate analyses might not be reliable as the firm- and deal-related factors that could influence deal performance are not included. To take related factors into account, this section further tests the influence of differences of stock market return and exchange rate return between acquirer's and target's countries on the deal's short-term performance by estimating the models:

$$ACAR5_i = \alpha_0 + \alpha_1 STOCK12_i + \alpha_2 Firm_i + \alpha_3 Deal_i + \alpha_4 Country_i + f_Y + f_{industry} + \varepsilon_i \quad (3.3)$$

$$ACAR5_i = \alpha_0 + \alpha_1 CURRENCY12_i + \alpha_2 Firm_i + \alpha_3 Deal_i + \alpha_4 Country_i + f_Y + f_{industry} + \varepsilon_i \quad (3.4)$$

where the dependent variables in Equations (3) and (4) are the acquirer's cumulative abnormal returns over the 5-day event window. The main variables of interest are *STOCK12* and *CURRENCY12*, defined in the previous section.

In terms of control variables, we include a comprehensive set of acquirer and deal characteristics following previous studies (Moeller, Schlingemann and Stulz, 2004; Morch, Shleifer and Vishny, 1990; Harford, 1999; Lang, Stulz and Walkling, 1991; Travlos, 1987; Chang, 1998). Misangyi, Elms, Greckhamer and Lepine (2006) suggest that 31.7% - 44.2% of merger performance variance can be explained by firm-level factors. $Firm_i$ is a vector of firm explanatory variables, which includes firm size measured by thelogarithm of the acquirer market value 4 weeks before the merger announcement (*A_LNMV*), the ratio of cash flows to sales measured by the funds from operations divided by the sales at the fiscal year-end before the M&As announcement (*A_CF2SALE*), the leverage ratio to represent a firm's financial risk measured by acquirer's total debt divided by total capital at the fiscal year-end before the M&As announcement (*A_Leverage*), the book-to-market ratio measured by the market value of

acquirer's assets one month prior to the deal announcement divided by the book value of acquirer's assets (*A_M2B*), stock price run-up during a six-month period ending one month before merger announcement (*A_Runup*). $Deal_i$ is a vector of deal-related factors, which includes the ratio of cross-border deal size to bidder's market value 4-week prior to the announcement (*Relative Size*), the dummy variable that equals 1 if the deal is 100% paid by stock (*STOCK*), the dummy variable that equals 1 if there is more than one bidder (*Competing Bid*), the dummy variable that equals 1 if the deal is identified as a tender offer (*Tender*), the dummy variable that equals 1 if the acquirer and the target have the different first two-digit of primary SIC code (*Diversification*), the dummy variable that equals 1 if the target is a public firm (*Public*), and the dummy variable that equals 1 if the acquiring firms is a state-owned enterprise (*State Owned*). To account for the influence of country-level variables, we also control for GDP growth rate of acquirer and target countries (*A_GDP* and *T_GDP*), the nature logarithm of their GDP per capita (*Ln(A_GDPpercapital*) and *Ln(T_GDPpercapital)*), the nature logarithm of the great-circle distance between acquirer and target country that is calculated with latitude and longitude of their capital cities (*Ln(Distance)*).We also consider year and industry fixed effectsf_Y and $f_{industry}$in all models.

[Insert Table 3.4 Approximately Here]

Table 3.4 presents the results. In the models in Panel A, the study regresses ACAR5 on the stock market return difference between acquirer and target countries (*STOCK12*) and in Panel B the 5-day CARs of acquirers are regressed against *CURRENCY12*. In Panel A, the evidence shows that the coefficients of *STOCK12* are positive and significant in all specifications, which suggests that the acquirer's abnormal announcement returns

increase with the difference in country-level stock returns between acquirer and target. The estimates imply that a one-unit increase in the stock return difference during the year before the deal announcement is related to a higher announcement return of 14.7% in specification 3 with related factors controlled for. This is consistent with the previous univariate results and hypothesis H1a. One explanation could be that higher stock market valuation makes acquirers wealthier and target firms cheaper, leading to lower cost of capital and therefore more profit (Froot and Stein, 1991). Alternatively, the outperformance could be explained by the differential mispricing of stocks between acquirer and target, suggesting that acquirers take advantage of the overvalued stock and make a profitable investment (Shleifer and Vishny, 2003).

Panel B shows evidence of the influence of exchange rate return difference. In line with the univariate results and hypothesis H3a, there is a significant positive relationship between acquirer announcement performance and differences in currency returns between acquirer and target. Every unit rises in *CURRENCY12* increases the acquirer's short-term abnormal returns by 65.97% after controlling for the firm- and deal-related characteristics. This could be because of the greater appreciation of the home country currency against that of the host country can increase the bargaining power of the bidder and create value for acquirer shareholders.

With regard to control variables, ACAR5 is significantly lower if the acquirer has a larger firm size (*A_LNMV*), which suggests that the market is less in favour of Chinese cross-border mergers involving larger acquirers and is consistent with Moeller et al. (2004). In addition, the coefficients on acquirer's cash flow ratio are significantly negative, which provides supporting evidence for Jensen's (1986) free cash flow theory that acquiring

firms with excessive cash holdings tend to conduct poor deals. Chinese cross-border acquisitions that are fully paid with stock significantly reduce value for acquirer shareholders, which is consistent with Travlos (1987). Last, there is a positive relationship between the target country's annual growth rate of GDP per capita and acquirer's short-term performance.

3.5.2 The determinants of long-run performance of Chinese cross-border M&As

In the previous section, the findings suggest that acquirers benefit from misvaluation and those with relatively higher stock market valuation and more inflated currency experience higher abnormal returns around cross-border mergers announcement. To examine whether these misvaluation-driven cross-border mergers eventually create synergies for acquirers, this study assesses acquirers' long-term performance based on their post-acquisition stock performance. The accounting-based methodology is not employed as the requirement of post-merger accounting ratio during the 3-year following deal completion results in a large drop in the sample size. This study also concerns the reliability of accounting data in countries with weak governance. Therefore, stock abnormal returns are calculated to investigate the market valuation of cross-border acquisitions. Only completed Chinese cross-border mergers are included and both univariate and multivariate analyses are carried out.

[Insert Table 3.5 Approximately Here]

To investigate market evaluation in the long-term, this study employs the buy-and-hold abnormal returns (BHARs) methodology, which is widely employed for examining long-run stock performance following major corporate events. Although Fama (1998) and

Mitchell and Stafford (2000) criticize the BHAR approach due to potentially biased statistical inferences and strongly recommends calendar time portfolio (CTP) methodology, Barber and Lyon (1997) and Lyon, Barber, and Tsai (1999) instead advocate the use of BHAR method because it most accurately reflects investor experience. More importantly, Loughran and Ritter (2000) argues that the CTP approach fails to detect abnormal returns when events are clustering in a month as it averages over months of the high and low event activity, which results in extremely weak tests if managers time the market. As mergers and acquisitions tend to be clustered across time, the power of the CTP methodology might be lowered and therefore it is not well suited in this analysis.

Table 3.5 reports the results obtained from the univariate analysis, which are long-term abnormal stock returns over 12-, 24- and 36-month event windows and draws a comparison between BHARs of sub-samples. Following Lyon et al. (1999), the acquirers' BHARs are calculated using market-to-book ratio- and size-adjusted returns and the t-statistics are bootstrapped to avoid rebalancing and new listing biases related to asymmetric criteria for sample selection in reference portfolios. BHARs are computed as follows:

$$BHAR_{it} = \prod_{t=0}^{T}[1 + R_{it}] - \prod_{t=0}^{T}[1 + R_{pt}] \quad (3.5)$$

where $R_{it}$and R_{pt}refer to the monthly stock returns on stock i and on reference portfolio in month t, respectively.

The specific steps to build a reference portfolio follow Bouwman et al. (2009). First, in June of each year t from 1995 to 2016, all Shanghai stock exchange companies are grouped into appropriate size decile portfolios and then each portfolio is divided into

quintiles based on their market-to-book ratio in year t-1, introducing fifty benchmark portfolios. Firms are allocated as listed on the Shenzhen stock exchange into benchmark portfolios by considering their size and market-to-book ratio. Last, companies conducting cross-border deals during the year the reference portfolio generated are deleted from the portfolios.

Panels A and B of Table 5 show acquirers' long-term abnormal returns across different levels of stock market return difference and exchange rate return difference between China and target countries, respectively. Overall, the evidence shows that Chinese cross-border mergers generally reduce value for acquirers' shareholders in the long-term regardless of the event window employed and there are significant differences between the sub-groups. This might be explained by considering that it is difficult for bidders to effectively conduct integration management of foreign target firms due to environment differences (Ahern, Daminelli and Fracassi, 2012).

After dividing the sample based on the magnitude of stock market return differences between acquirer and target countries, the evidence shows a significant negative relationship between stock market return differences and acquirers' BHARs. Acquirers in the large difference group experience abnormal returns of -9.63%, -20.51% and -32.83% over the 12-, 24- and 36-month periods after the deal announcement, respectively, which are -6.19%, -18.40% and -29.61% lower than their counterparts with small stock market return difference. The findings are in line with H2a, indicating that the acquirer's valuation might be reversed due to that the initial expectations from managers of highly valued firms might be overestimated and not fully met.

In terms of exchange rate return differences, the evidence shows that the magnitude of difference between acquirers' and targets' countries is positively related to acquirers' BHARs, which supports hypothesis H4a that Chinese acquirers with larger inflated currency can benefit from currency appreciation and enjoy better long-term performance. Chinese cross-border mergers with large exchange rate return difference generate abnormal returns of -2.34%, 0.32% and 2.11% over the event window of 12-, 24- and 36-months following deal completion, respectively, while those with small difference experience abnormal returns of - 5.18%, -8.19% and -19.17% during the same event windows respectively. The differences are significant at the 1% level, regardless of the event window employed.

To confirm the evidence of Chinese cross-border mergers in Table 5, multivariate analyses were performed to take related determinants of merger performance into account by estimating the models as follows:

$$BHAR36_i = \alpha_0 + \alpha_1 STOCK12_i + \alpha_2 Firm_i + \alpha_3 Deal_i + \alpha_4 Country_i + f_Y + f_{industry} + \varepsilon_i \quad (3.6)$$

$$BHAR36_i = \alpha_0 + \alpha_1 CURRENCY12_i + \alpha_2 Firm_i + \alpha_3 Deal_i + \alpha_4 Country_i + f_Y + f_{industry} + \varepsilon_i \quad (3.7)$$

, where the dependent variables $BHAR36_i$ refers to the buy and hold abnormal returns for company i over 36-month after Chinese cross-border acquisitions completion. The same set of independent variables is included in the models, which are the main variables of interest STOCK12 and CURRENCY12, firm characteristics $Firm_i$ and deal characteristics $Deal_i$. Year and industry effects are also included.

[Insert Table 3.6 Approximately Here]

Table 3.6 provides the results of the long-term OLS regression analysis. Panel A examines the relation between BHAR36 and stock market return difference, while Panel B investigates the influence of exchange rate return difference on BHAR36. In Panel A, this study finds that the estimated coefficient on STOCK12 is negative and significant in all columns, implying that Chinese cross-border mergers motivated by stock misvaluation are not beneficial for acquirer shareholders in the long-run. More specifically, one unit increases in the stock return difference during the one-year before deal announcement worsens 3 years buy-and-hold abnormal returns for Chinese cross-border bidders by 27.79 percentage point in column 3 with the firm, deal and country-level characteristics accounted for. This is inconsistent with the short-run evidence, suggesting that the valuation of acquirers with large stock market return difference experiences a reversal in the long-run.

In Panel B, the evidence shows that there is a significant positive relation between CURRENCY12 and BHAR36 across models. This suggests that acquirers with relatively more appreciated currency before merger announcement experience significantly higher long-run abnormal returns, which is in line with the univariate analysis. Specifically, the dependent variable is acquirer's abnormal stock returns over the 36-month following deal completion. As shown in the table, acquirer's long-run performance improves by 11.46% with a one percent increasing in the exchange rate return difference between host and home countries. After related factors controlled, the coefficient on the key variable CURRENCY12 is 0.5932, suggesting that every unit increases in the exchange rate return difference is associated with a 59.32% increase in BHAR36. This finding implies that

acquirers can take advantage of inflated currency and create synergies in the long-run, which is consistent with Lin, Officer and Shen (2014).

In terms of control variables, the findings show a significant negative coefficient on A_LNMV, suggesting the market reactions are less favourable to large acquirers, which is in line with Moeller et al. (2004) arguing that large firms are likely suffering from managerial hubris and therefore conduct value-destroying investment. In addition, the coefficient on A_Leverage is positive and significant at the 1% level, which is consistent with Harford (1999) and Ghosh and Jain (2000) that highly leveraged acquiring firms may be severely monitored by banks and therefore these firms would cautiously and efficiently carry out mergers that create value. Moreover, this study finds that stock payment exerts a significantly negative effect on acquirer's abnormal returns in the long-term, which provides supportive evidence for the signalling effect of stock offers and is consistent with Travlos (1987). Furthermore, the evidence shows that for cross-border acquisitions with publicly listed target firms, there are significant negative abnormal returns of 34.52% to acquirers, which is supportive of Chang (1998), Fuller et al. (2002) and Faccio et al. (2006).

3.6 Robustness Check

This section tests the robustness of the results on the relationship between acquirer's short-run performance and differences in country-level factors between acquirers and targets. According to Ang and Cheng (2006) who finds supportive evidence on the misvaluation theory, not only are acquirers have relatively high stock valuation than target firms, but also successful acquirers have relatively high stock valuation than

unsuccessful acquirers. Therefore, to examine whether the results are mainly driven bysuccessful sample, this section divides the whole sample into two subsamples for successful and unsuccessful deals and conducts a univariate analysis to compare results in subsamples.

[Insert Table 3.7 Approximately Here]

Table 3.7 showsthe results obtained from the univariate analysis. After dividing the full sample by deal completion, the evidence from Panel A suggests that in both subsamples, the higher the acquirer's country-level stock market returns compared to those of target countries, the better the acquirer's announcement performance, which are consistent with the hypotheses and the results of the whole sample in the previous section. Specifically, acquirers in successful deals with a large difference on average have returns of 2.16%, 4.39%, and 4.23% for ACAR3, ACAR5, and ACAR11 respectively, which are significantly higher than those with small differences. Similar results are also found in unsuccessful deals. This is consistent with the hypothesis (H1a), which indicates that acquirers with relatively high stock valuation taking over targets with relatively low valuation can create gains for acquirers. Regarding exchange rate return differences, the statistics in Panel B show a similar pattern to the relationship between stock market valuation and acquirer announcement returns, i.e. in both of successful and failed samples, acquirers earn higher abnormal returns when the RMB has appreciated more than the target's currency before deal announcement. These findings are supportive of the hypothesis (H3a) and the evidence on the whole sample.

3.7Conclusion

This paper investigates the wealth effects of Chinese cross-border M&As. By collecting a comprehensive sample of 1,174 deals, it offers evidence on two country-level factors that affect cross-border merger performance in both the short- and long-term, including stock market return difference and exchange rate return difference between China and the target countries. The main findings show that Chinese acquirers enjoy better stock performance around deal announcement when there are larger differences in stock market returns and exchange rate returns between home and host countries. This suggests that acquirers with relatively highstock valuation and relatively strong currency can generate gains in the short-term by acquiring target firms withrelatively low stock valuation and relatively weak currency and taking advantage of the valuation difference.

Regarding the long-term performance of Chinese cross-border mergers, this study finds that there is a negative relationship between stock market return difference and long-term stock performance, while exchange rate return difference is positively related to long-term performance. Acquirers with large stock market return difference experience reversal in abnormal returns in the long-term, this may be because investors overestimate deal synergies when stock market valuation is high and correct the stock price over time as they realise that the initial expectations might not be fully achieved. For acquirers with inflated currencies, as currency appreciation is not related to stock market sentiment, the benefits of misvaluation are not offset by other factors and acquirers also enjoy a better long-term performance. Overall, the evidence suggests that the role of valuation difference plays an important role in determining Chinese acquires' performance.

Table 3. 1 – Summary Characteristics

This table shows the summary characteristics of the Chinese cross-border M&A sample between 1995 and 2016. Panel A reports the distribution of sample M&As by year. Panel B reports the industrial distribution of the sample M&As. Fama-French 12-industry classification is employed. Panel C reports the distribution of sample M&As by geographical region.

	N	% of Sample	Value of Transaction ($mil.)	% of Sample
Panel A: Year Distribution				
1995	2	0.17	3.229	-
1996	2	0.17	0.636	-
1997	3	0.26	13.85	-
1998	2	0.17	1.01	-
1999	3	0.26	73.73	0.05
2000	5	0.43	1.538	-
2001	7	0.6	146.83	0.11
2002	14	1.19	1,805.76	1.33
2003	12	1.02	418.86	0.31
2004	31	2.64	269.63	0.20
2005	19	1.62	259.25	0.19
2006	33	2.81	6,490.77	4.77
2007	68	5.79	11,871.51	8.72
2008	69	5.88	11,070.40	8.13
2009	65	5.54	6,461.34	4.74
2010	60	5.11	9,754.36	7.16
2011	74	6.3	2,391.39	1.76
2012	90	7.67	5,479.72	4.02
2013	96	8.18	6,366.98	4.67
2014	107	9.11	13,970.99	10.26
2015	191	16.27	22,240.59	16.33
2016	221	18.82	37,114.89	27.25
Total	1,174	100	136,207.30	100
Panel B: Industrial Distribution				
Consumer NonDurables	98	8.35	3,636.15	2.67
Consumer Durables	73	6.22	3,014.31	2.21
Manufacturing	242	20.61	24,801.59	18.21
Energy, Oil, Gas and Coal	47	4	13,162.42	9.66
Chemicals	54	4.6	8,031.70	5.90
Business Equipment	239	20.36	16,765.71	12.31
Telephone and Television	14	1.19	55.02	0.04
Utilities	16	1.36	2,258.692	1.66

Wholesale and Retail	34	2.9	3,333.066	2.45
Healthcare and Med. Equip	76	6.47	4,205.29	3.09
Finance	138	11.75	36,111.71	26.51
Other	143	12.18	20,831.62	15.29
Total	1,174	100	136,207.30	100
Panel C: Regional Distribution				
North America	273	23.25	35,034.07	25.72
Europe	292	24.87	33,541.01	24.62
Middle East	11	0.94	9,071.76	6.66
Asia / Pacific	559	47.61	46,485.86	34.13
Latin America	34	2.9	6,340.74	4.66
Africa	5	0.43	5,733.83	4.21
Total	1,174	100	136,207.30	100

Table 3. 2– Descriptive Statistics

This table shows the descriptive statistics of the Chinese cross-border M&As. Panel A reports deal- and acquirer-related characteristics based on country-level stock market return difference between acquirer and target. Panel B reports related characteristics according to exchange rate return difference between acquirer and target. Panel C B reports related characteristics based on bilateral trade flows between acquirer and target. M&A transactions are restricted by criteria as follows: (1) the deal was announced between January 1, 1995 and December 31, 2016; (2) the bidder is a publicly listed firm; (3) the bidder has stock price and accounting data available in Datastream database. We report the values for the full sample and subsamples. The t-test is used to test for statistical significance of means. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and *, respectively.

Panel A	**Stock Market Return Difference**												
		Full Sample (I)			**Small (II)**			**Moderate (III)**			**Large (IV)**		**T-Test (IV) - (II)**
	N	**Mean**	**SD**	**N**	**Mean**	**SD**	**N**	**Mean**	**SD**	**N**	**Mean**	**SD**	**Difference**
Deal Characteristics													
Deal Value ($mil)	720	182.19	596.38	232	123.41	349.81	233	193.33	648.38	255	225.50	711.60	102.09**
Relative Size	717	0.35	1.84	231	0.30	1.69	232	0.37	1.99	254	0.40	1.85	0.10**
All Stock	887	4.57%	0.20	281	3.27%	0.20	302	3.98%	0.17	304	6.26%	0.22	2.99%**
All Cash	887	26.61%	0.44	281	31.47%	0.45	302	28.15%	0.45	304	23.36%	0.42	-8.11%
Competition	1107	0.57%	0.07	369	0.54%	0.07	369	0.43%	0.00	369	0.81%	0.09	0.27%
Diversification	1107	58.46%	0.50	369	53.93%	0.50	369	59.62%	0.49	369	61.83%	0.50	7.9%*
Hostile	1107	0.44%	0.07	369	0.27%	0.05	369	0.54%	0.07	369	0.59%	0.07	0.32%
Tender	1107	1.75%	0.12	369	0.54%	0.07	369	1.90%	0.14	369	2.90%	0.14	2.36%**
Public	1107	15.56%	0.36	369	12.47%	0.33	369	15.45%	0.36	369	19.16%	0.39	6.69%***
Deal Completion	1107	60.48%	0.49	369	57.14%	0.49	369	60.35%	0.50	369	63.95%	0.50	6.81%*
Acquirer Characteristics													
Ln(Acquirer Size)	1043	14.77	2.37	343	14.89	2.22	350	14.78	2.37	350	14.64	2.51	-0.25
Return on Assets	1068	4.22%	0.08	353	4.38%	0.08	358	3.63%	0.07	357	4.66%	0.08	0.28%
Cash Flow to Sales	1045	15.05%	24.06	345	14.83%	24.79	351	14.91%	23.16	349	15.41%	24.28	0.58%
Leverage	1065	49.79%	164.41	352	44.81%	157.57	356	54.99%	209.87	357	41.40%	110.59	-3.41%

Panel B		Exchange Rate Return Difference											
		Full Sample (I)		Small (II)			Moderate (III)			Large (IV)			T-Test (IV) - (II)
	N	Mean	SD	N	Mean	SD	N	Mean	SD	N	Mean	SD	Difference
Deal Characteristics													
Deal Value ($mil)	609	160.53	499.06	202	158.35	526.72	203	154.85	522.95	204	168.34	446.14	9.99
Relative Size	605	0.34	1.70	199	0.18	0.68	202	0.42	2.15	204	0.41	1.89	0.23
All Stock	741	4.86%	0.22	250	2.80%	0.17	247	5.26%	0.22	244	6.56%	0.25	3.76%**
All Cash	741	28.34%	0.45	250	25.20%	0.44	247	31.17%	0.46	244	28.69%	0.45	3.49%
Competition	923	0.52%	0.06	310	0.65%	0.08	307	0.41%	0.00	306	0.33%	0.06	-0.32%
Diversification	923	58.72%	0.49	310	66.45%	0.47	307	62.54%	0.48	306	47.06%	0.50	-19.39%***
Hostile	923	0.54%	0.07	310	0.00%	0.00	307	0.65%	0.08	306	0.98%	0.10	0.98%*
Tender	923	1.84%	0.13	310	2.58%	0.16	307	1.30%	0.11	306	1.63%	0.13	-0.95%
Public	923	17.33%	0.38	310	18.71%	0.39	307	14.33%	0.35	306	18.95%	0.39	0.24%
Deal Completion	923	58.72%	0.49	310	58.34%	0.49	307	57.21%	0.49	306	60.61%	0.50	2.27%
Acquirer Characteristics													
Ln(Acquirer Size)	874	14.85	2.35	296	14.95	1.99	282	14.67	2.67	296	14.91	2.37	-0.04
Return on Assets	895	4.13%	0.08	305	3.70%	0.07	290	3.53%	0.09	300	5.15%	0.07	1.45%***
Cash Flow to Sales	879	14.55%	24.71	298	15.47%	19.42	284	11.06%	31.15	297	16.96%	22.04	1.49%
Leverage	891	43.47%	174.75	302	42.46%	165.18	288	48.47%	232.92	301	40.15%	104.71	-2.31%*

Table 3. 3– CAR Analysis

This table shows acquirer's announcement performance over three event windows on Chinese cross-border M&A transactions. CAR3, CAR5 and CAR11 represent cumulative abnormal returns (CARs) to acquirers during the 3-, 5-, and 11-day window surrounding the announcement date. Abnormal returns are computed by using market-adjusted model. First, we present the values for the full sample. Next, we report the values for sub-samples that are divided according to the level of stock market return difference and exchange rate return difference between acquirer and target in Panel A and B, respectively. The Student's t-test is used to test for statistical significance. For brevity, we do not report the t-statistics. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

	Full Sample (I)		Small (II)		Medium (III)		Large (IV)		T-Test (IV) - (II)
	N	Mean	N	Mean	N	Mean	N	Mean	Difference
Panel A - Stock Market Return Difference									
CAR3	1107	0.0136***	369	0.0052***	369	0.0140***	369	0.0216***	0.0164**
CAR5	1107	0.0190***	369	0.0048***	369	0.0165***	369	0.0359***	0.0310**
CAR11	1107	0.0243***	369	0.0097***	369	0.0262***	369	0.0370***	0.0274**
Panel B - Exchange Rate Return Difference									
CAR3	923	0.0122***	310	0.0038**	307	0.0130***	306	0.0200***	0.0161**
CAR5	923	0.0191***	310	0.0006	307	0.0168***	306	0.0403***	0.0397**
CAR11	923	0.0253***	310	0.0068***	307	0.0185***	306	0.0508***	0.0441**

Table 3. 4– OLS Regressions of Acquirer Short-Term Performance

This table shows results of OLS regression of acquirer's announcement performance. All models in Panel A regress the five-day cumulative abnormal returns against the key variable *STOCK12*. Model (I) only include the key explanatory variable; Models (II) and (III) further control for firm- and deal-related characteristics. All models control for industry and year fixed effects. For brevity, their coefficients are not reported in the table. All variables are defined in Appendix A. All continuous variables are winsorized at the 1% and 99% levels. T-statistics are reported in parentheses. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

Panel A	**Model (I)**	**Model (II)**	**Model (III)**
STOCK12	0.3198**	0.2748**	0.1470**
	(2.38)	(2.41)	(2.05)
A_LNMV		-0.0013**	-0.0041***
		(-2.60)	(-4.61)
A_M2B		0.0130	0.0267
		(0.57)	(0.77)
A_CF2SALE		-0.0406**	-0.0552**
		(-2.46)	(-2.48)
A_Leverage		0.0017	0.0030**
		(0.3)	(2.29)
A_Runup		0.0044*	0.0048*
		(1.97)	(1.85)
Relative Size			0.0004
			(0.19)
Stock			-0.0575***
			(-3.53)
Competing Bid			-0.0218
			(-0.48)
Diversification			0.0085
			(1.39)
Hostile			-0.0532
			(-1.29)
Tender			0.0058
			(0.31)
Public			-0.0142*
			(-1.91)
State Owned			-0.0079
			(-0.80)
Ln(A_GDPpercapital)			0.0776
			(0.52)
Ln(T_GDPpercapital)			-0.0059
			(-1.23)
T_GDP growth			0.0234*
			(1.91)
A_GDP growth			-0.0003
			(-0.07)
Ln(Distance)			0.0107
			(1.32)
Constant	-1.2133	-2.1097	10.7024

	(-1.36)	(-2.1)	(0.46)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
R^2	0.006	0.037	0.094
Adjusted R^2	0.004	0.029	0.032
N	1107	1027	333

All models in Panel B regress the five-day cumulative abnormal returns against the key variable *CURRENCY12*. Model (I) only include the key explanatory variable; Models (II) and (III) further control for firm- and deal-related characteristics. All models control for industry and year fixed effects. For brevity, their coefficients are not reported in the table. All variables are defined in Appendix A. All continuous variables are winsorized at the 1% and 99% levels. T-statistics are reported in parentheses. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

Panel B	**Model (I)**	**Model (II)**	**Model (III)**
CURRENCY12	0.8886*	0.7670***	0.6597**
	(1.69)	(2.71)	(2.32)
A_LNMV		-0.0027**	-0.0049***
		(-2.15)	(-5.35)
A_M2B		0.0104	0.0236
		(0.12)	(0.66)
A_CF2SALE		-0.0653**	-0.0781**
		(-2.28)	(-2.39)
A_Leverage		0.00015	0.0021*
		(0.71)	(1.68)
A_Runup		0.0173*	0.0271**
		(1.83)	(2.42)
Relative Size			0.0093
			(0.2)
Stock			-0.0228***
			(-3.08)
Competing Bid			-0.054
			(-1.11)
Diversification			0.0102
			(1.25)
Hostile			0.0075
			(0.2)
Tender			0.0035
			(0.16)
Public			-0.0124*
			(-1.86)
State Owned			-0.0097
			(-0.78)
Ln(A_GDPpercapital)			-0.2764
			(-1.44)
Ln(T_GDPpercapital)			-0.0047
			(-0.89)
T_GDP Growth			0.0481*
			(2.02)
A_GDP Growth			0.0147

			(1.43)
Ln(Distance)			0.0172*
			(1.78)
Constant	-0.6422	-1.6036	-54.2183*
	(-0.67)	(-1.47)	(-1.68)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
R^2	0.008	0.052	0.118
Adjusted R^2	0.005	0.043	0.038
N	923	862	257

Table 3. 5– BHAR Analysis

This table shows acquirer's long-run performance over three event windows on Chinese cross-border M&A transactions. BHAR12, BHAR24 and BHAR36 represent buy and hold abnormal returns (BHARs) to acquirers during the 12-, 24-, and 36-month window following the announcement date. First, we present the values for the full sample. Next, we report the values for sub-samples that are divided according to the level of stock market return difference and exchange rate return difference between acquirer and target in Panel Aand B, respectively. The Student's t-test is used to test for statistical significance. For brevity, we do not report the t-statistics. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

	Full Sample (I)		Small (II)		Moderate (III)		Large (IV)		T-Test (IV) - (II)
	N	Mean	N	Mean	N	Mean	N	Mean	Difference
Panel A - Stock Market Return Difference									
BHAR12	894	-0.0560***	296	-0.0344***	255	-0.0268***	343	-0.0963***	-0.0619***
BHAR24	714	-0.0563***	293	-0.0211***	254	0.0108***	167	-0.2051***	-0.1840***
BHAR36	614	-0.1067***	254	-0.0321***	196	-0.0179***	164	-0.3282***	-0.2961***
Panel B - Exchange Rate Return Difference									
BHAR12	746	-0.0408***	179	-0.0518***	288	-0.0314***	279	-0.0234***	0.0284**
BHAR24	602	-0.0325***	162	-0.0819***	259	-0.0222***	181	0.0032**	0.0787***
BHAR36	519	-0.0982***	140	-0.1917***	216	-0.1276***	163	0.0211***	0.2128***

Table 3. 6– OLS Regressions of Acquirer Long-Term Performance

This table shows results of OLS regression of acquirer's long-run performance. All models of Panel A regress the 36-month buy and hold abnormal returns against the key variable *STOCK12*. Model (I) only include the key explanatory variable; Models (II) and (III) further control for firm- and deal-related characteristics. All models control for industry and year fixed effects. For brevity, their coefficients are not reported in the table. All variables are defined in Appendix A. All continuous variables are winsorized at the 1% and 99% levels. T-statistics are reported in parentheses. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

Panel A	**Model (I)**	**Model (II)**	**Model (III)**
STOCK12	-01260*	-0.1488***	-0.2779**
	(-1.75)	(-2.76)	(-2.30)
A_LNMV		0.0082**	-0.0224***
		(2.38)	(-2.97)
A_M2B		0.0836*	-0.0924
		(1.81)	(0.66)
A_CF2SALE		0.0010	0.0020
		(0.68)	(0.82)
A_Leverage		-0.0004*	-0.0007
		(-1.70)	(-1.19)
Relative Size			0.0846
			(0.17)
Stock			-0.0257**
			(-2.05)
Competing Bid			-0.5976
			(-0.96)
Diversification			-0.0428
			(-0.51)
Hostile			-0.2268***
			(-2.48)
Tender			0.2021
			(0.88)
Public			-0.1786*
			(-1.81)
State Owned			-0.0264
			(-0.24)
Ln(Distance)			0.2086**
			(2.11)
Ln(A_GDPpercapital)			-0.6254
			(-1.44)
Ln(T_GDPpercapital)			-0.0073

			(-0.89)
T_GDP Growth			0.0279
			(1.02)
A_GDP Growth			0.0472
			(1.43)
Constant	-138.3487***	-154.7286***	-74.7426**
	(-8.36)	(-8.55)	(-2.24)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
R^2	0.13	0.182	0.161
Adjusted R^2	0.126	0.172	0.105
N	614	559	240

All models of Panel B regress the 36-month buy and hold abnormal returns against the key variable *CURRENCY12*. Model (I) only include the key explanatory variable; Models (II) and (III) further control for firm- and deal-related characteristics. All models control for industry and year fixed effects. For brevity, their coefficients are not reported in the table. All variables are defined in Appendix A. All continuous variables are winsorized at the 1% and 99% levels. T-statistics are reported in parentheses. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

Panel B	**Model (I)**	**Model (II)**	**Model (III)**
CURRENCY12	0.1146**	0.7872*	0.5932**
	(2.04)	(1.82)	(2.37)
A_LNMV		0.0149	-0.0363**
		(0.85)	(-2.24)
A_M2B		-0.0030	-0.0027
		(-0.86)	(-0.89)
A_CF2SALE		-0.0014	-0.0032
		(-0.67)	(-0.89)
A_Leverage		0.0026*	0.0024***
		(1.91)	(3.53)
Relative Size			-0.2644
			(-0.36)
Stock			-0.0136**
			(-1.99)
Competing Bid			-0.4461
			(-0.52)
Diversification			0.1552
			(1.20)
Hostile			-0.196
			(-0.39)
Tender			0.3573
			(1.19)
Public			-0.3452**
			(-2.44)
State Owned			-0.1331
			(-0.79)
Ln(Distance)			0.0914
			(0.58)
Ln(A_GDPpercapital)			-0.3525
			(-1.21)
Ln(T_GDPpercapital)			-0.0055
			(-0.94)
T_GDP Growth			0.0193
			(1.08)

A_GDP Growth			0.0327
			(1.29)
Constant	-148.0346***	-172.4428***	-75.2144
	(-6.39)	(-6.84)	(-1.59)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
R^2	0.100	0.132	0.187
Adjusted R^2	0.095	0.119	0.116
N	519	475	187

Table 3.7 – Robustness Check

This table shows acquirer's announcement performance over three event windows on Chinese cross-border M&A transactions. CAR3, CAR5 and CAR11 represent cumulative abnormal returns (CARs) to acquirers during the 3-, 5-, and 11-day window surrounding the announcement date. Abnormal returns are computed by using market-adjusted model. First, this study presents the values for the full sample. Next, this study sub-dividesthe sample based on whether the deal is completed and the level of acquisition experience. Then, this study further divides the sample according to the level of stock market return difference and exchange rate return difference between acquirer and target in Panel A and B, respectively.The Student's t-test is used to test for statistical significance. For brevity, we do not report the t-statistics. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

		Full sample	Successful sample				Failed sample			
			Small (1)	Moderate (2)	Large (3)	Dif. (3)-(1)	Low (4)	Moderate (5)	High (6)	Dif. (6)-(4)
Panel A - Stock Market Return Difference										
ACAR3	Mean	0.0136***	0.0011***	0.0227***	0.0216***	0.0205**	0.0100***	0.0062***	0.0215***	0.0115*
	N	1,107	199	173	211		170	196	158	
ACAR5	Mean	0.0190***	0.0039***	0.0230***	0.0439***	0.0400**	0.0058***	0.0107***	0.0251***	0.0192*
	N	1,107	199	173	211		208	192	99	
ACAR11	Mean	0.0243***	0.0095***	0.0363***	0.0423***	0.0329**	0.0099***	0.0172***	0.0299***	0.0200
	N	1,107	199	173	211		208	192	99	
Panel B - Exchange Rate Return Difference										
ACAR3	Mean	0.0122***	0.0043***	0.0191***	0.0232***	0.0189**	0.0034***	0.0069***	0.0162***	0.0128*
	N	923	141	154	164		169	153	142	
ACAR5	Mean	0.0191***	-0.0030***	0.0207***	0.0598***	0.0629**	0.0036***	0.0129***	0.0277***	0.0141*
	N	923	141	154	164		169	153	142	
ACAR11	Mean	0.0253***	0.0027***	0.0219***	0.0701***	0.0674**	0.0102***	0.0151***	0.0386***	0.0184
	N	923	141	154	164		169	153	142	

Chapter Four: Chiinese Cross-border Mergersand Acquisitionsandthe Roleof International Trade

4.1 Introduction

With China's economic transformation and industrial upgrading, Chinese enterprises are encouraged to more actively engage in outward investment and there has been a steady growth in outbound foreign direct investment (OFDI) from China. Although global foreign direct investment declined by almost a fifth in 2018, China bucked the trend and realised a 4.2% increase to approximately $130 billion. According to China's Ministry of Commerce, non-financial OFDI appeared to have plateaued at around $120 billion, while financial OFDI more than doubled to nearly reach $10 billion. The rapid development of OFDI activities reflects not only China's integration in the global economy but also its overseas expansion to acquire strategic assets, natural resources, advanced technologies, brand and new markets.

Among OFDI activities in China, cross-border M&As are the most prevalent form of FDI. Although 2018 saw a drop in China's outward mergers mainly due to the Sino-US trade war, with a total value of $106 billion, the aggregate values of Chinese cross-border deals were still approximately one-third higher than the levels prior to the 2016 record high. This upward trend started with the implementation of the 'Go Global' policy in 1999, which encourages Chinese enterprises to pursue an internationalisation strategy and commit to greater global integration. Accompany this trend has been a series of events, including China's accession to the World Trade Organisation in 2001, the emphasis of overseas investment in the tenth and eleventh five-year plans, and the Belt and Road Initiative.

While recent years have seen a significant increase in China's cross-border deal, research on multinational M&As mainly focuses on developed countries (Conn, et al., 2005; Chari and Ouimet, 2004; Fraser and Zhang, 2009; Bessler and Murtagh, 2002). The small number of studies on Chinese cross-border transactions mainly investigate financial motivations behind deals decision (Du and Boateng, 2012) and the influence of firm-level factors on acquirer's performance (Boateng et al., 2008; Deng, 2009; Zhang and Ebbers, 2010). Little evidence has been provided on the relationship between country-level determinants, such as currency appreciation, current account balance or labour shortages and cross-border merger outcomes.

To fill this gap, this study focuses on the effects of the bilateral trade between home and host countries on the wealth gains of Chinese bidders in outbound mergers. Bilateral trade is chosen as the level of bilateral trade between the two countries can reflect multinational trade and investment barriers. For cross-border acquisitions, many country-level barriers might have a negative influence on a deal's completion and integration, including legal and political differences, cultural and business practise differences, corporate taxation differences, labour costs, geographical distance and economic competitiveness policy differences (Larsson and Risberg, 1998; Olie, 1996; Slangen, 2006). Bilateral trade network and openness, as a by-product of globalisation, could make countries more interconnected and therefore could build a strong connection between acquirer and target countries, which would assist acquirers of cross-border mergers to overcome those barriers and conduct deals smoothly (De Benedictis and Tajoli, 2011; Yoon and Lee, 2016).

Chinese cross-border mergers also provide a unique testing ground for examining the role of bilateral trade flows. This is not only because recent years have witnessed a significant increase in the volume and value of China's outward deals, but also because Chinese multinational

acquisitions tend to be carried out by state-owned enterprises and have high ownership concentration. Therefore, Chinese cross-border transactions are likely to be influenced more strongly by the institutional environment and traditional culture. China, as an emerging market country, is also likely to encounter foreign resistance when they acquire advanced knowledge and technology. These characteristics result in more barriers to Chinese cross-border mergers and therefore the role of the bilateral trade network and openness might be even more important to Chinese acquirers.

Previous research shows a positive relationship between bilateral trade flows and the outcome of cross-border deals. For example, Erel, Liao and Weisbach (2010) use a comprehensive sample of 56,978 cross-border mergers covering 48 countries and find that bilateral trade significantly increases the likelihood of cross-border acquisitions. This evidence is also found by Rossi and Volpin (2004) and Chakrabarti et al., (2009). Yoon and Lee (2016) find that bilateral trade has a remarkable and positive influence on the acquirer's stock performance. Based on this line of previous work, this study focuses on Chinese cross-border mergers and investigates whether deals with more bilateral trade flows between China and target countries will have a greater likelihood of completion and create more abnormal returns for acquirer shareholders.

This study employs a data set of 1,130 Chinese cross-border M&As with an announcement date between 1 January 2001 and 31 December 2016. Following Erel, Liao and Weisbach (2012) and Ferreira et al. (2010), this paper uses bilateral trade flow as a proxy for the degree of bilateral trade openness of home and host countries, which is measured by the maximum of bilateral imports and exports between China and target countries 12 months before the merger announcement. The data on trade flows is collected from the United Nations Commodity Trade Statistics database.

The study firstly shows that Chinese acquirers are more likely to complete a cross-border deal when there is a higher level of bilateral trade flow between China and the target country. Every unit increase in bilateral trade flows enhances the likelihood of cross-border deal success by 8.41%. Both univariate and multivariate analyses show that acquirers experience significantly higher abnormal returns around deal announcement when China and the target country have more trade exchanges. This suggests that the market is more in favour of cross-border deals involving two countries with stronger trade relations. There is also a significant positive relationship between acquirers' long-term stock performance and bilateral trade flows between China and target countries, which indicates that more in-depth trade relations between home and host countries can help acquirers generate synergy gains.

This chapter contributes to the literature in several ways. First, it makes contributions to the literature on cross-border M&As by providing evidence from China. Extensive research has focused on the effects of these macro-economic factors on M&As in the context of advanced economic countries (Georgopoulos, 2008; Choi and Leon, 2010; Uddin and Boateng, 2011). However, the booming economy of the emerging markets, especially the Chinese market, over the past two decades has contributed to an upward trend of M&A volume and makes the emerging market firms more likely to be bidders in cross-border M&As. Second, to the best of our knowledge, this is the first study examining the influence of bilateral trade flows on Chinese cross-border mergers. Despite the significance of trade relations between acquirer and target countries, only a small number of studies include data on import and export trade volume (Rossi and Volpin, 2004; Chakrabarti et al., 2009). Third, the findings have important implications for acquirers in emerging markets, which is that taking over a target in countries with fewer trade barriers can assist in conduct the integration process during the post-acquisition period.

The remainder of the paper is organised as follows: Section 2 develops the hypotheses; Section 3 presents the data and methodology; Section 4 analyses the results; and Section 5 concludes the study.

4.2 Literature review

The last two decades have witnessed that the world economy has become more integrated. The literature largely argues that the relationship between trade and foreign direct investment (FDI) plays a significant role in the integration process, and the relationship could vary with the determinants of FDI. Cross-border mergers and acquisitions are one of the most important forms of FDI. Empirical research on the determinants of FDI focuses on firm-specific and country-specific characteristics, including R&D intensity, technology advance, culture distance, regional integration, openness to FDI, bilateral trade, infrastructures, development distance, relative exchange rate, exchange rate volatility, relative labour costs, geographical distance, economic and political environment and so on, which is summarised and reviewed in the rest of this section.

4.2.1 Country-specific characteristics and FDI

Previous literature suggests that FDI is mainly driven by country-specific factors (Doytch and Eren, 2012;Kang and Jiang, 2012;Cavallari and D' Addona, 2013). However, most of the research focuses on country-specific characteristics associated with the host country and little evidence is provided on home country factors. First, market size is an important determinant of firms' FDI decisions(Omanwa, 2013).Bhaumik and Co (2011) suggest that the volume of FDI significantly increases with the size of host market and the prospects for host market growth, which could be explained by considering that larger host market enables acquirers to easily benefit from economies of scale and exploit ownership advantages (Cuyvers et al.,2011). This is

also confirmed by Kravis and Lipsey (1980), Contrator (1991), Sethi et al. (2003), Bevan and Estrin (2004) and Buckley et al. (2007). In addition, Kimino et al., (2007) argue that larger market size is likely to have greater availability of tangible and intangible assets, e.g. capital resources, expertise and knowledge, which can be utilised by acquirers to create synergies. With the internationalization of Chinese firms, many studies provide evidence on China's outbound investment and suggest that there is a positive relation between host market size and outward FDI (Taylor, 2002; Deng, 2004; Kolstad and Wiig, 2012). To measure market size, previous studies widely used GDP, GDP per capita and economic growth rate as proxies (Grosse and Trevino, 1996; Cuyver et al., 2011).

Second, previous research largely argues that the quality of institutions plays an important role in determining FDI activity, particularly FDI activities in developing markets (Flores and Aguilera, 2007; Blonigen et al., 2005). A host country with a well regulated institutional environment, e.g. low political risk, less ownership restriction and non-corrupt bureaucracy, makes a target firm more attractive and has a significant positive impact on FDI activity (Loree and Guisinger, 1995; Chakrabarti, 2001; Grosse and Trevino, 2005; Omanwa, 2013). Tallman (1988) suggests that FDI is likely to flow into countries with a higher quality of institutional environment when the home country has a poor business environment. However, the findings on the developed market do not provide supportive evidence on the positive effect of institution quality. For the Chinese market, previous literature shows a negative relation between the political stability of host countries and china's outbound FDI activities (Buckley et al., 2007). This could be explained with higher state ownership and strong supports from the Chinese government and therefore Chinese firms do not regard the quality of institutions as an important factor (Voss et al., 2009; Kang and Jiang, 2012; Ramasamy et al., 2012; Child and Rodrigues, 2005). There are a number

of proxies employed for institution quality, most of which are related to a country's political, economic and legal environment. For instance, the Governance Indicators of the World Bank offer scores on factors including government effectiveness, regulatory quality, corruption control, voice and accountability, rule of law and so on. A higher score represents a higher quality of the institutional environment.

Third, a number of studies suggest that FDI decision is influenced by host country's resources including physical infrastructure, natural resources and technology (Loree and Guisinger, 1995; Cheng and Kwan, 2000; Flores and Aguilera, 2007; Asiedu, 2002). According to the findings, the costs of operations are likely to be reduced with high-quality infrastructure. Besides, natural resources are also a driver for a country's outward investment, especially for resource-seeking motivated investment (Dunning. 1993). This is also confirmed by literature on China's FDI, which suggests that China's FDI are significantly motivated by cheap and high-quality natural resources due to the low level of per capita natural wealth (Deng, 2004; Ramasamy et al., 2012; Kang and Jiang, 2012; Kolstad and Wiig, 2012; Wu and Sia, 2002). Resource-seeking investment is often conducted in the petroleum sector and mineral sector, e.g. the China National Petroleum Corporation(CNPC) acquisition of PetroKaz. Moreover, Dunning (1993) documents that the host country's technological development is also important for home country FDI as it could lower the cost of R&D investment (Harris and Ravenscraft, 1991).

Fourth, FDI decision takes the tax effect into consideration as it is closely related to the cost and profitability, which also explains that the government attempts to cut taxes to attract FDI (Bilgili et al., 2012; Aqeel and Nishat, 2005). Although theoretical research suggests a positive reaction of outward FDI to tax reduction, the empirical studies document mixed results. For example, Slemorod (1990) and Kemsley (1998) find that inward FDI is negatively related to tax rates cut

by using US data, while Scholes and Wolfson (1990) document evidence of the opposite and Wheeler and Mody (1992) and Porcano and Price (1996)document insignificant relation between FDI and tax rates.

The fifth important determinant of FDI is market openness, including openness to trade and regional economic cooperation and integration. Previous literature, e.g. Kravis and Lipsey (1980), Pistoresi (2000), Chakrabarti (2001), and Aqeel and Nishat (2005), suggest that a country's market openness has a positive impact on FDI inflows, i.e. a country with more trade openness is more likely to be a destination for FDI. This could be explained by considering that trade costs increase with trade barriers and therefore FDI is attracted to markets with a higher level of market openness (Kravis and Lipsey, 1980; Culem, 1988; Pantelidis and Kyrkilis, 2005). In terms of Chinese FDI, Kang and Jiang (2012) find supportive evidence on the positive effect of host countries' openness, which is because of fewer trade barriers to foreign market access, e.g. export quotas and antidumping actions against Chinese firms. However, Wei and Zhu (2007) and Chakrabarti (2000) find an insignificant effect of market openness on FDI. For regional cooperation and integration, Cuyver et al. (2011) and Blomström and Kokko (1997) suggest that an integrated region is more likely to be a destination of FDI as all participating countries make the region a larger market with more efficient market resource allocation and faster economic development. Kreinin and Plummer (2008) document that regional integration has a mixed effect on FDI, i.e. the existence of an integrated region attracts more FDI inflows from other countries but results in a reduction of FDI outflows from partner countries.

Another determinant of FDI is inflation. According to previous studies, the uncertainties related to a country's outward investment increase with a volatility of inflation rates as volatile inflation

leads to more difficulties in setting a price and anticipating profit. In addition, a higher inflation rate tends to increase investment costs and makes the local currency devaluate.

4.2.2 The influence of host and home country's characteristics on FDI

The correlation between host and home country's characteristics has important influences on FDI activities. The first determinant is the geographical distance between host and home countries, which has been examined a lot in previous literature and mixed evidence is founded (Wei and Liu, 2001; Cuyver et al., 2011). Bevan and Estrin (2004) document that the geographical distance could be a measurement of transportation cost of conducting outward investment, and therefore there is a negative relation between geographical distance and outward FDI. This is confirmed by Wei (2004) who suggests that monitoring and transportation costs of outbound investment increase with geographical distance, which generates managerial issues and informational uncertainty. Therefore, firms are more likely to invest in countries that are closer to home countries (Grosse and Trevino, 1996; Frenkel et al., 2004; Gao, 2005; Guerin, 2006). However, there is literature suggesting that geographical distance has a positive effect on FDI (Buckley and Casson, 1981; Horstman and Markusen, 1987; Brainard, 1997; Markusen and Venables, 1998; Wei and Liu, 2001; Pan, 2003; Bevan and Estrin, 2004). It is argued that firms are likely to access to geographically proximate countries through export and more distant countries via FDI activity.

Besides the geographical distance, the distance in development stage also plays a role in determining FDI activities (Bhaumik and Co, 2011). On the one hand, firms in developing markets are likely to conduct outbound investments in developed countries as they can get access to advanced technology and skills. On the other hand, firms carrying out outward FDI to

countries with similar development stage could utilise the existing experiences and skills to gain competitive advantages.

The distance in the culture of home and host countries has also been largely investigated. Previous literature, e.g. Kogut and Singh (1988), Rauch (1999), Yiu and Makino (2002), Guerin (2006), Flores and Aguilera (2007), Buckley et al. (2007b), Bhaumik and Co (2011) and Kang and Jiang (2012), suggests that conducting investment in countries with shorter cultural distance could reduce operating cost because of similar demand in product and easier communication and therefore firms are more likely to undertake FDI in countries sharing similar culture. Several proxies have been employed to represent cultural distance, including Hofstede's index, common language, common religion and immigration population.

Moreover, prior research suggests that differences in the institutional environment, e.g. political and legal systems, can influence FDI decisions (Goerzen and Beamish, 2003;Dow and Karunaratna, 2006). By using a data set of US FDI, Globerman and Shapiro (2009) find that outbound FDI of the US is more likely to locate in countries with English common law, indicating that similar legal environment could lower investment uncertainties and operation costs. However, Kang and Jiang (2012) document inconsistent evidence that Chinese outward FDI tends to flow into countries with a larger difference in the institutional environment, which could be explained by considering that Chinese market is heavily regulated and therefore Chinese enterprises are attracted by the less regulated market (Scott, 2003; Mayer et al., 2009; Peng et al., 2008).

Furthermore, relative costs such as relative borrowing costs and relative labour costs are regarded as significant determinants of FDI. In terms of borrowing costs, Tolentino (2010) suggests that firms could have lower borrowing costs when the home country has a relatively

low-interest rate, which increases the probability and profitability of outward investment as firms could establish overseas business with lower cost (Barrell and Pain, 1996; Wei and Liu, 2001; Pan, 2003; Farrell et al., 2004;Cuyver et al., 2011). Similarly, traditional trade theory largely argues that outward FDI is motivated by lower labour costs in the host country by employing differences in wage rates and average labour productivity, i.e. GDP divided by the total number of labour hours, to represent labour cost. (Culem, 1988; Kumar, 1994; Jun and Singh, 1996;Barrel and Pain, 1999; Taylor, 2002; Hatzius, 2000; Wei and Liu, 2001; Bevan and Estrin, 2004; Kimino et al., 2007; Dunning and Lundan, 2008; Bilgili et al., 2012). In contrast, Gupta (1983),Wheeler and Mody (1992), Lucas (1993),Miller (1993), Meyer (1995), Wang and Swain (1997) and Love and Lage-Hidalgo (2000) document that lower wage rate not only indicates lower labour cost but also means lower labour quality, which is not an important determinant of FDI. This is confirmed by evidence on Chinese outward FDI, which could be explained with China's abundant labour supply and thus labour cost is not necessarily an important driving force (Sethi, et al., 2003; Wei and Liu, 2001; Bevan and Estrin, 2004; Buckley et al., 2008).

The last but not least factor that largely investigated by prior literature is the exchange rate, including the changes in the exchange rate between two currencies and the volatility of the exchange rate (Blonigen, 2005). It is largely argued that outbound FDI is motivated by the appreciated home country's currency and deferred by the depreciated home country's currency (Aliber, 1970; Stevens, 1998; Benassy-Quere et al., 2001). This could be explained by considering that the foreign currency denominated assets tend to be cheaper when home country currency strengthens, and therefore result in more profit for outward investment (Blonigen, 1997;Scott-Green and Clegg, 1999; Buckley, et al., 2007b;Yu and Walsh, 2010). Empirical studies provide supportive evidence on the positive effect of home country currency appreciation

on outward FDI, e.g. Froot and Stein (1989; 1991), Blonigen and Feenstra (1996), Grosse and Trevino (1996), Kiyota and Urata (2004), and Kimino, Saal and Driffield (2007). However, there is also research finding insignificant relation between changes in the exchange rate and FDI (Pain and Van Welsum, 2003). In terms of volatility of exchange rate, Tolentino (2010) suggests that currency volatility is positively related to investment uncertainties and outward FDI is motivated when there is higher volatility of home country's currency, which is also confirmed by Swenson (1994), Kogut and Chang (1996), and Blonigen, et al. (2005).

4.3Hypothesis development

The existence of institutional barriers is of particular interest for literature on cross-border mergers and acquisition as these deals can be influenced by a wide range of factors and hurdles at the country level. For example, typical factors having a determinant influence on trade in goods can be related to cross-border mergers and acquisitions, including the legal framework, corporate and capital taxation, geographic distance, cultural and political differences, and time zones (Dikova et al., 2010). Bittlingmayer and Hazlett (2000) provide three possible reasons to explain these institutional hurdles. First, the barriers are motivated by private benefits, such as protecting the interests of local companies. Second, they are driven by bureaucratic self-interest, such as competition regulators and antitrust lawyers being rewarded with favourable coverage from legal proceedings. Third, institutional barriers are induced by political extraction, i.e. the government can extract gains from the process of lobbying by firms (Zhang et al., 2011).

Ahern et al. (2015) suggests that costs of cross-border mergers increase with these frictions. As a result, in making decisions of conducting cross-border mergers, acquirers tend to consider not only the characteristics of target firms but also the relationship between home and host country

(Didier, Herrador and Magali Pinat, 2019). One of the most important factors is the size of bilateral trade between acquirers' and targets' countries, which facilitates acquirers to overcome country-level hurdles existing in cross-border mergers (De Benedictis and Tajoli, 2011). Di Giovanni (2005) investigates the impact of trade flows from acquirer's country to target's country on cross-border mergers, and finds a positive and significant relationship between the number of cross-border deals counted between the two countries and trade flows between these two countries. Ferreira et al. (2010) show that multinational deals are more frequent between countries with greater bilateral trade as they are more economically integrated. Consistently, Erel, Liao and Weisbach (2010) find a significant positive relationship between bilateral trade and cross-border acquisition completion. This is also confirmed by Monteiro (2012) with a more recent dataset.

4.3.1 Deal Completion

A bilateral trade relationship between the two countries can increase their personal ties and mutual understanding, which is at the heart of a successful investment. One of the reasons behind is that strong trade connectivity between acquirers' and targets' countries might allow acquirers to take additional measures to enhance the efficiency of due-diligence processes before acquisitions and integration (Chakrabarti et al., 2009; Zhang and He, 2014). Successful due diligence would lead to a smooth negotiation between acquirer and target and set the deal (Howson, 2003). Alternatively, it would enable the acquirer to detect potential problems and have a chance to walk away without announcing the deal. Another reason is that a strong trade relation might be related to a lower level of economic nationalism which condemns free trade and criticizes globalization. Dinc and Erel (2013) documents that the target country's governments tend to prefer companies owned domestically instead of acquired by foreign

companies in the context of economic nationalism. Their findings show that it is less likely for acquirers in cross-border mergers to complete the deal when the government in the target's country against the deal. Therefore, a stronger bilateral trade relationship is more likely to facilitate the cross-border deal completion. Following this line of thought, this study proposes the following hypothesis:

H1: Cross-border M&As with a higher level of bilateral trade flows between acquirers' and targets' countries will have a higher success rate.

4.3.2 Deal Performance

The level of economic nationalism is also related to the performance of cross-border mergers. Previous literature documents a negative relationship between economic nationalism and acquirer's performance in cross-border deals. For example, Zhang and Mauck (2018) employs bilateral political relationship as a proxy for economic nationalism and finds that improving bilateral political relations have a positive impact on Chinese acquirer's short- and long-run performance. Yoon and Lee (2016) find that stronger bilateral trade relations result in higher abnormal announcement returns to acquirers. This might be explained by considering that takeover premiums are likely to be lower in cross-border mergers with relatively strong relations (Bertrand et al., 2016). In addition, less deal risk under the circumstances of a lower level of economic nationalism would also exert a positive influence around deal announcement and during post-merger integration process, which results in better performance of acquirers. By using the bilateral trade flows between acquirer country and target country as a proxy for economic nationalism, this study develops the following hypotheses:

H2: A greater bilateral trade relations between China and target countries is related to higher abnormal returns to acquirers in the short-term.

H3: A greater bilateral trade relations between China and target countries is related to more synergies gains to acquirers in the long-term.

4.4Data and Methodology

4.4.1 Sample selection

This study obtains data on Chinese cross-border M&As from the SDC database of Thomson Financial. As the last two decades have seen a surge in Chinese outward investment because of China's foreign policy and involvement in the WTO, a time frame from 1 January 2001 to 31 December 2016 is chosen for the study. A sample of 4,514 acquisitions constitutes the original sample. Then, following previous research, a number of criteria are employed to identify the final sample:

(1) Acquirers are from China, while target firms are from other countries.

(2) Acquirers hold less than 50% of target firms' ownership prior to the merger announcement.

(3) Acquirers are public firms listed on the Shanghai or Shenzhen stock exchanges.

(4) Target firms can be publicly listed firms, privately held firms or subsidiaries.

(5) Acquirers have available data on stock price in DataStream from 300 days prior to the deal announcement and three years after the deal announcement.

(6) Acquirers have available data on accounting information from DataStream.

(7) Data on bilateral trade flows between China and the target country is available.

The final sample set consists of 1,157 Chinese cross-border acquisitions, which involves 90 countries between 2001 and 2016. Among 714 Chinese cross-border mergers and acquisitions, 411 (57.56%) of them are completed.The deal characteristics are obtained from Thomson Financial and include DataStream code, mergers' announcement date and completion date, target nationality, target firm's public status, the form of payment, the deal attitude offer type, state ownership, an indicator that the acquirer and its target are in related industries, an indicator of whether the deal involves more than one bidder, and the Standard Industrial Classification (SIC) code. In terms of firm characteristics, this study collects data from the DataStream database, which includes the market value, total assets, long-term debt obligation, operating cash flow, and capital expenditure. For country-level characteristics, gross domestic product (GDP) and GDP per capita are collected from the World Bank's World Development Indicators (WDI).

4.4.2 Measurement of Key Explanatory Variable

To examine whether there is a relationship between bilateral trade relations and cross-border merger outcomes, this study follows Erel, Liao and Weisbach (2012) and Ferreira, Massa and Motos (2010) and calculate bilateral trade flows as the maximum of bilateral imports and exports between the two countries. Specifically, this study firstly calculates bilateral imports as imports by the target nation from China as a percentage of total imports by the target nation. And then bilateral exports are calculated as exports by the target nation to China as a percentage of total exports by the target nation. Last, this study takes the maximum value between bilateral imports and bilateral exports as the proxy for bilateral trade flows, which is labelled as *MAXTRADE12*:

$$MAXTRADE12 = Max\left(\frac{\text{the value of imports (exports)by target country from (to)acquirer country}}{\text{total imports (exports)by target country}}\right) \quad (4.1)$$

, where the data on trade flows is obtained from the United Nations Commodity Trade Statistics database.

4.4.3 Descriptive and summary statistics

[Insert Figure4.1 Approximately Here]

Figure 1 shows both the volume and value of Chinese outbound mergers in the sample. Similar patterns are shown in the figure; there has been a growing trend for the number of the value of cross-border mergers conducted by Chinese acquirers, which peaks in 2016. There are 221 Chinese cross-border acquisitions with a total value of over $37 billion in 2016, compared with 7 deals and a total value of less than $1 billion in 2001. After three decades as a major recipient of foreign direct investment, China has become a major outward investor which trend corresponds to China's Go Global policy. The policy was firstly introduced in 1999, aiming to encourage Chinese enterprises to go abroad and participate in the competitions of the global market. This was followed by joining the World Trade Organisation (WTO) in 2001 and promoting RMB internationalisation in 2009. Since 2013, the Chinese government has adopted the One Belt, One Road initiative to build connections between China and countries lying on the ancient Silk Road and the new Maritime Silk Road.

[Insert Table 4.1 Approximately Here]

Table 4.1 shows the distribution of sample Chinese cross-border M&As by geographical region. The evidence shows that a large number of targets of Chinese cross-border mergers are located in Asia/Pacific, accounting for 47.8% This could be attributed to the significant growth of regional trade networks and regional economic integration in Asia/Pacific. North America and Europe are the second and third most popular regions for targets of Chinese cross-border mergers,

constituting 24.89% and 22.99% respectively, which is mainly because of their advanced financial system, legal environment, advanced technology and talent. In contrast, Chinese acquirers are less likely to take over target firms in the Middle East, Latin America and Africa.

[Insert Table 4.2 Approximately Here]

Table 4.2 presents the summary statistics of sample Chinese cross-border M&As, which includes a comprehensive collection of firm and deal characteristics that are likely to influence acquisition outcome. Appendix A shows the description of variables. The full sample is equally grouped into three sub-samples based on bilateral trade flows between China and the target countries. A student's t-test is conducted to examine whether there is a significant difference in mean between low level and high level of bilateral trade flows.

The evidence shows that the average deal value is $136.83 million for the group of high-level bilateral trade flows, which is $21.9 million smaller than the group of low-level bilateral trade flows. However, with smaller absolute deal sizes, acquirers tend to conduct relatively large mergers when there are more bilateral trade flows between China and target countries (Relative size for the two groups are 0.66 and 0.23). In addition, 65.55% of Chinese cross-border mergers in the group of a high level of bilateral trade flows are diversified transaction, which at 10.93% is significantly higher than that of in the group of low level. This might be because having stronger trade relations with the target country may result in fewer cultural and political differences and more understanding, which encourages acquiring firms to make braver decisions. Moreover, Chinese cross-border mergers in the group of a high level of bilateral trade flows are 1.26% more likely to be tender offers and 2.53% less likely to involve public firms than the counterparts in the group of low-level bilateral trade flows. Furthermore, the likelihood of deal completion significantly increases with bilateral trade flows between acquirer and target countries, which

might be explained by considering that a stronger bilateral trade relationship is related to a lower level of economic nationalism and therefore facilitate the cross-border deal completion. In terms of firm characteristics, acquirers' firm size and leverage ratio are significantly negatively related to the level of bilateral trade flows.

4.5Empirical Analysis

4.5.1 The influence of bilateral trade on the probability of cross-border mergers success

This study begins by examining whether bilateral trade flows between acquirer's and target's countries have an influence on the chance of completing cross-border mergers by estimating the following probit model:

$$Pr(Deal\ Completion_i = 1) = \Phi(\alpha_0 + \alpha_1 MAXTRADE12_i + \alpha_2 Firm_i + \alpha_3 Deal_i + \alpha_4 Country_i + f_y + f_{industry} + \varepsilon_i) \quad (4.2)$$

, where *Prob*refers to probability, and Φrepresents the Cumulative Distribution Function of the standard normal distribution. The dependent variable ($Deal\ Completion_i$) is equal to one if the cross-border acquisition i is successfully completed, and zero otherwise. $MAXTRADE12_i$ is the key independent variable, which is defined in the previous section. $Firm_i$ and $Deal_i$ are the vector of acquirer's and deal's characteristics, respectively, which are likely to have an influence on merger outcomes based on prior literature (Stulz, 1990; Moeller, Schlingemann and Stulz, 2004; Morch, Shleifer and Vishny, 1990; Jensen, 2005; Harford, 1999; Lang, Stulz and Walkling, 1991; Travlos, 1987; Chang, 1998; Jensen and Meckling, 1976; Koeplin, Sarin, and Shapiro, 2000; Officer, 2007; Megginson, Morgan and Nail, 2004; Dos Santos, Errunza and Miller, 2008). Specifically, this study includes the natural logarithm of acquirer's market value measured 4 weeks before the announcement (*A_LNMV*), the ratio of total debt by total capital (*A_Leverage*),

the market-to-book ratio (*A_M2B*), the ratio of cash flows by the total assets (*A_CF2TA*), the ratio of cross-border deal size by acquirer's size 4 weeks before the announcement (*Relative Size*), the indicator of stock payment (STOCK), the indicator of whether there is more than one bidder (*Competing Bid*), the indicator of tender offer (Tender), the indicator of if the target is a public firm (Public), the indicator of whether the acquirer is a state-owned enterprise (State Owned), the indicator of acquisition attitude (Hostile), and the indicator of whether the acquirer and the target have the same first two-digit of primary SIC code (Diversification). $Country_i$ is a vector of country-level control variables, including China and target countries' GDP growth rate (A_GDP and T_GDP) and the nature logarithm of GDP per capita(Ln(A_GDPpercapital) and Ln(T_GDPpercapital)), and the distance between acquirer and target's country measured by using latitude and longitude of capital cities(Ln(Distance)). Year effect (f_y) and industry effect ($f_{industry}$) are also controlled in the model.

[Insert Table 4.3 Approximately Here]

Table 4.3 shows the marginal effects of the analysis. The coefficient on *MAXTRADE12* is positive and highly statically significant in all models, indicating that the probability of completing a cross-border acquisition increases with bilateral trade flow between China and the target's country. The model I only includes the main independent variable and shows that every unit increase in *MAXTRADE12* is related to a 12.63% increase in the likelihood to complete a cross-border merger. Acquirer's and deal's characteristics are further controlled in models II and III. Although the marginal effects of *MAXTRADE12* drop to 0.1023 and 0.0841 in models II and III respectively, the coefficients are still statistically significant at the 1% level. The results are consistent with the hypothesis H1 and Rossi and Volpin (2004), Chakrabarti et al., (2009) and

Erel, Liao and Weisbach (2012). This can be explained by considering that a stronger bilateral trade relationship helps reduce institutional barriers and facilitate deal completion.

In terms of control variables, the evidence shows that the acquirer's size and cash flow ratio are negatively related to deal completion, which suggests that acquirers with larger firm size and more free cash flow are less likely to complete transactions. In addition, the coefficients of hostile offer indicator (Hostile) and the competing bid indicator (Competing bid) are negative and significant at the 1% level, which indicates that the probability of cross-border merger completion decreases when the deal attitude is hostile and there is more than one bidder. The results also show a significant negative relationship between Ln(Distance) and cross-border acquisition completion, suggesting that Chinese acquirers are more likely to take over targets in countries closer to China.

4.5.2 The influence of bilateral trade on the short-run performance of Chinese cross-border mergers

This section explores whether bilateral trade has an influence on acquirer's short-term performance. The short-window event study methodology is used to measure the abnormal stock returns around merger announcement. This study conducts both the univariate and multivariate analyses.

[Insert Table 4.4 Approximately Here]

Table 4.4 shows findings of the univariate test and reports acquirers' average cumulative abnormal returns (CARs) over the three-, five- and eleven-day event windows (ACAR3, ACAR5 and ACAR11, respectively) of a cross-border deal announcement between 2001 and 2016. Abnormal returns are estimated with the market-adjusted return model to capture the market

reaction to the cross-border merger announcement, which follows Fuller et al. (2002) as the following equation:

$AR_{it} = R_{it} - R_{mt}$ (4.3)

, where AR_{it}refers to the abnormal return for company i on day t; R_{it}refers to stock return for company i on day t; R_{mt}refers to stock return for the value-weighted Shanghai and Shenzhen market index on day t.R_{it} and R_{mt} are calculated by taking the natural log of share price on day t divided by share price on day $t-1$ for company i and stock market *m*, respectively.

Next, this study calculates CARs as follows:

$CAR_{i,T_1,T_2} = \sum_{t=T_1}^{T_2} AR_{it}$ (4.4)

, where the event window is between T_1 days prior to deal announcement and T_2 days following deal announcement. ACAR3, ACAR5 and ACAR11 are obtained by summing up abnormal returns over [-1, +1], [-2, +2], and [-5, +5] event windows, respectively, where 0 represents to the announcement day of mergers.

As shown in Table 4, Chinese acquirers experience statistically significant positive CARs around the deal announcement, with values ranging from 1.51% to 3.04% over different event windows. After dividing the sample based on the level of bilateral trade flows, this study finds that there is a significant positive relationship between bilateral trade flows and acquirer's announcement performance, regardless of the event windows employed. Bidders perform better around deal announcement when there is a high level of bilateral trade flows between China and target countries, with the excess returns of 0.45%, 3.32% and 4.95% higher than bidders of deals with a low level of bilateral trade flows. The differences are statistically significant. This is consistent with hypothesis H2, suggesting that more business undertaken between acquirer and target

countries can reduce institutional barriers such as cultural distance and therefore the market reacts favourably.

As the univariate test does not take firm- and deal-related characteristics into account, this study conducts a multivariate test to investigate whether there is a positive relationship between bilateral trade flows and acquirer's short-term performance after controlling for related factors. The following model is estimated:

$$ACAR5_i = \alpha_0 + \alpha_1 MAXTRADE12_i + \alpha_2 Firm_i + \alpha_3 Deal_i + \alpha_4 Country_i + f_Y + f_{industry} + \varepsilon_i \quad (4.5)$$

, where the dependent variable $ACAR5_i$ refers to acquirer's cumulative abnormal returns over the 5-day event window. The key independent variable MAXTRADE12 is defined in the previous section. As for other independent variables, this model includes a set of acquiring firm, deal and country-level characteristics that have been described in Equation (2), including A_LNMV, A_M2B, A_Leverage, A_CF2TA, Relative size, Stock, Competing Bid, Diversification, Hostile, Tender, Public, State-Owned, Ln(A_GDPpercapital), Ln(A_GDPpercapital), T_GDP growth, A_GDP growth, and Ln(Distance). The model also controls for year fixed effects and industry fixed effects.

[Insert Table 4.5 Approximately Here]

Table 4.5 presents the results. The 5-day CARs of acquirers are regressed against MAXTRADE12 in all models. The evidence shows that the amount of bilateral trade flow increases the acquirer's abnormal announcement returns in all models, which is consistent with the previous results and hypothesis H2. The coefficient on MAXTRADE12 in model III suggests that every percentage increases in the bilateral trade flows are related to 11.68% higher CARs over the 5-day around the deal announcement. The outperformance could be explained by considering that more trade businesses conducted between acquirers' and targets' countries could increase mutual understanding and economic integration.

In terms of firm-specific factors, the evidence shows that acquirer's announcement abnormal returns decrease with acquirer size increasing in models II and III, which could be explained by the potential managerial hubris existing in large firm decisions (Moeller et al., 2004). This study also overserves that the coefficient on A_CF2SALE is significant and negative, which is consistent with Jensen (1986) and Harford (1999) and indicates that acquirers with higher cash flow are likely to conduct value-decreasing mergers. There is also a significant positive relationship between the acquirer's leverage ratio and short-term performance, suggesting that acquirers with a higher leverage ratio may carefully conduct mergers due to the bank's close monitoring (Ghosh and Jain, 2000). As for deal characteristics, the findings show that the use of full stock payment in Chinese cross-border mergers is associated with 3.30% lower announcement returns to acquirers, which is supportive of Travlos (1987).

4.5.3 The influence of bilateral trade on the long-run performance of Chinese cross-border mergers

This section conducts long-term event studies with the buy-and-hold abnormal returns (BHARs) methodology to examine acquirers' long-term stock performance using only completed cross-border mergers and both univariate and multivariate analyses.

[Insert Table 4.6 Approximately Here]

Table 4.6 presents the acquirer's long-term abnormal returns over 12-, 24- and 36-month event windows. The full sample is divided into three groups based on bilateral trade flows between China and the target country. As Barber and Lyon (1997) and Lyon et al. (1999) point out, three sources of biases that can produce misspecified statistics in BHARs: new listing bias, rebalancing bias and skewness bias. This study follows Lyon et al. (1999) to calculate BHARs

by using size- and market-to-book ratio-adjusted returns and bootstrapping t-statistics. BHARs are calculated as follows:

$$BHAR_{it} = \prod_{t=0}^{T}[1 + R_{it}] - \prod_{t=0}^{T}[1 + R_{pt}] \quad (4.6)$$

, where $R_{it}$and R_{pt}refer to monthly stock returns on firm*i* and on reference portfolio *p*in month t, respectively.

The reference portfolio is constructed by following Bouwman et al. (2009). First, in June of each year t from 2001 to 2016, all firms listed on Shanghai stock exchange are grouped into decile portfolios based on firm size. Second, each portfolio is grouped into quintile portfolios based on the market-to-book ratio in year t-1, resulting in 50 benchmark portfolios. Third, this study allocated firms listed on Shenzhen stock exchange into 50 benchmark portfolios based on firm size and market-to-book ratio. Fourth, firms carrying out cross-border mergers during the year the benchmark portfolio is created are dropped from the portfolios.

As seen in Table 6, there is a significant decrease in acquirers' long-term abnormal returns regardless of the event windows employed (BHAR12=-5.81%, BHAR24=-3.58%, BHAR36=-10.28%), which is contrary to the evidence from the analysis of the acquirer's short-term performance. After dividing acquirers into three subsamples, the results show that cross-border mergers in the group of a high level of bilateral trade flows significantly generate more abnormal returns for acquirer shareholders in the long-term, with excess returns of 6.11%, 1.59% and 5.76% higher than acquirers of deals with a low level of bilateral trade flows. The evidence is in line with H3, indicating that acquirers can enjoy synergy gains when there is more trade business between home and host countries.

To confirm the findings, this study conducts a multivariate analysis to control for related determinants of acquirer's long-term performance by estimating the model as follows:

$$BHAR36_i = \alpha_0 + \alpha_1 MAXTRADE12_i + \alpha_2 Firm_i + \alpha_3 Deal_i + \alpha_4 Country_i + f_Y + f_{industry} + \varepsilon_i \quad (4.7)$$

, where $BHAR36_i$ is acquirer's buy and hold abnormal returns for acquirer i over 36-month following the deal announcement. The main interest of variable MAXTRADE12 measures the bilateral trade flows between China and target's country. A set of control variables is included, including $Firm_i$, $Deal_i$, $Country_i$, f_Y, and $f_{industry}$, which are described in the previous sections.

[Insert Table 4.7 Approximately Here]

Table 4.7 shows the findings of the long-term OLS regression analysis. The evidence shows that there is a significant positive relationship between MAXTRADE12 and BHAR36, which suggests that acquirers experience higher long-term abnormal returns when there is a higher level of bilateral trade flow between acquirers and target countries. After taking firm, deal and country characteristics into account, the coefficient on MAXTRADE12 is 0.0887, indicating that every percentage increase in bilateral trade flows is related to an 8.87% increase in acquirer's long-term abnormal returns, which is consistent with the previous result and hypothesis.

As for control variables, the results show negative coefficients on A_LNMV and Relative Size, indicating that larger acquirers and relatively larger deals experience lower abnormal returns in the long-run. The evidence is consistent with Agrawal, Jaffe, and Mandelker (1992), Moeller, Schlingemann, and Stulz(2004) and Billett and Qian (2008) that acquirer size is significantly and negatively related to acquirer's stock performance. This could be explained by considering that large firms are likely to be subject to severe agency conflicts and therefore mergers conducted by

large acquirers might be driven by empire building (Jensen and Meckling, 1976; Demsetz and Lehn 1985; Roll, 1986; Jensen, 1986). For evidence on relative size, it is in line with Pettway and Yamada (1986) but inconsistent with Jarrell and Poulsen (1989). In addition, the coefficient on Stock is negative and significant at the 1% level, which is consistent with Travlos (1987). Moreover, the evidence shows that Hostile is significantly negatively associated with acquirer's long-run performance, which is in line with Morck et al. (1988) suggesting that friendly mergers are likely to be conducted for value generation while hostile mergers are driven by the discipline of target firm's poor management. Furthermore, the findings show that the coefficient on Public is significantly negative, suggesting that acquirers with public target firms significantly underperform those with private targets. This is consistent with Hansen and Lott (1996) and Chang (1998).

4.6Conclusion

Chinese firms have experienced a significant increase in cross-border M&As since the late 1990s. Despite the rapid pace of development, the vast majority of literature on cross-border mergers has studied the US market. Studies on Chinese cross-border M&As mainly investigate the strategic and financial motivation behind deals (Du and Boateng, 2012) and neglect the factors determining performance. This paper examines the Chinese M&A market and offers evidence on the bilateral trade flows of China and target countries that affect merger performance in the short- and long-term.

The findings show that Chinese acquirers are more likely to complete cross-border mergers when there is a higher level of bilateral trade flow between acquirer and target countries. More bilateral trade flows also lead to higher abnormal returns to acquirer shareholders in both the short- and

long-term. Overall, the results indicate that bilateral trade networks and openness could help countries build a strong connection, which helps acquirers in cross-border mergers overcome those barriers and generate synergy gains.

Figure 4. 1– China Outward M&A Volumes and Value

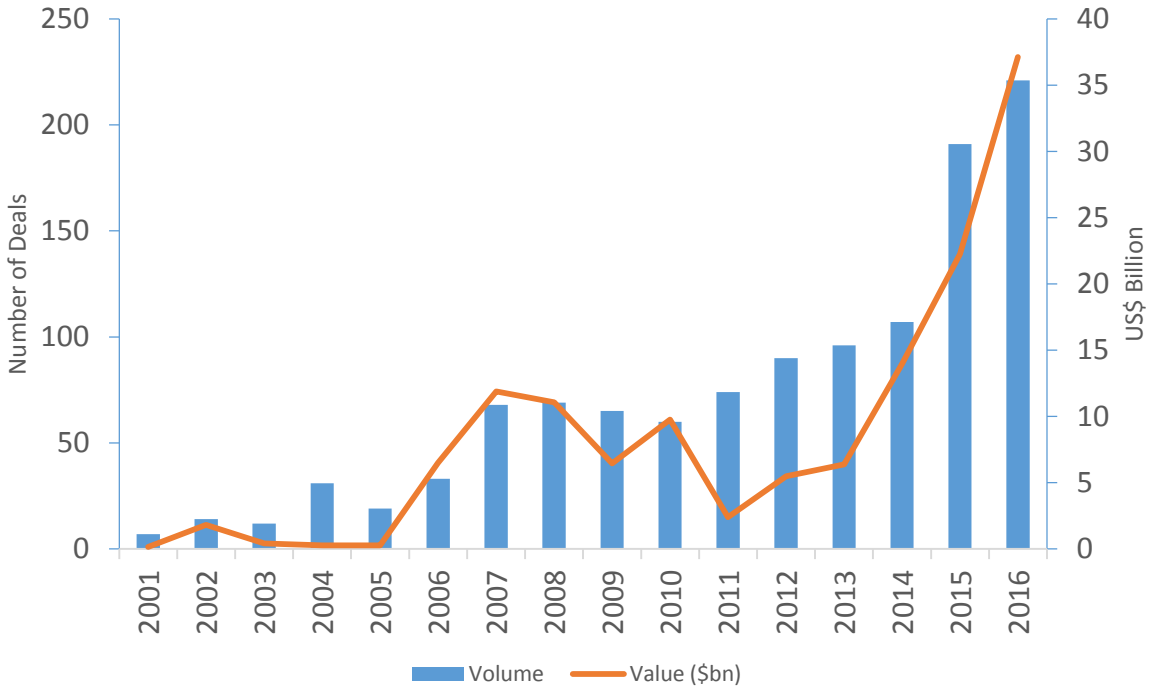

Table 4. 1– Regional Distribution

This table shows the summary characteristics of the Chinese cross-border M&A sample between 2001 and 2016. It reports the distribution of sample M&As by geographical region.

	N	% of Sample
Regional Distribution		
North America	266	22.99
Europe	288	24.89
Middle East	11	0.95
Asia / Pacific	553	47.80
Latin America	34	2.93
Africa	5	0.43
Total	1,157	100

Table 4. 2– Descriptive Statistics

This table shows the descriptive statistics of the Chinese cross-border M&As. The table reports related characteristics based on bilateral trade flows between acquirer and target. M&A transactions are restricted by criteria as follows: (1) the deal was announced between January 1, 2001 and December 31, 2016; (2) the bidder is a publicly listed firm; (3) the bidder has stock price and accounting data available in Datastream database. We report the values for the full sample and subsamples. The t-test is used to test for statistical significance of means. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and *, respectively.

	Bilateral Trade Flow											
	Full Sample (I)			Low (II)			Moderate (III)			High (IV)			T-Test (IV) - (II)
	N	Mean	SD	N	Mean	SD	N	Mean	SD	N	Mean	SD	Dif.
Deal Characteristics													
Deal Value ($mil)	473	164.47	488.44	149	158.73	594.27	157	199.32	499.78	167	136.83	356.13	-21.90
Relative Size	469	0.40	1.90	148	0.23	1.14	157	0.27	1.52	164	0.66	2.62	0.43*
All Stock	556	5.22%	0.22	175	4.57%	0.21	183	4.37%	0.21	198	6.57%	0.25	2.00%
All Cash	556	34.17%	0.47	175	36.00%	0.48	183	32.24%	0.47	198	34.34%	0.48	-1.66%
Competition	714	0.52%	0.06	238	0.35%	0.00	238	1.26%	0.11	238	0.55%	0.00	0.20%
Diversification	714	57.42%	0.49	238	54.62%	0.50	238	52.10%	0.50	238	65.55%	0.48	10.93%**
Hostile	714	0.70%	0.08	238	0.42%	0.06	238	1.26%	0.11	238	0.42%	0.06	0.00
Tender	714	2.24%	0.15	238	0.42%	0.06	238	4.62%	0.21	238	1.68%	0.13	1.26%***
Public	714	17.93%	0.38	238	14.29%	0.35	238	27.73%	0.45	238	11.76%	0.32	-2.53%**
Deal Completion	714	57.56%	0.50	238	52.2%	0.50	238	55.46%	0.50	238	65.16%	0.50	12.96%***
Acquirer Characteristics													
Ln(Acquirer Size)	678	14.817	2.46	228	15.05	2.18	236	14.95	2.63	214	14.41	2.51	-0.64***
Return on Assets	694	4.32%	0.08	233	4.70%	0.07	237	4.65%	0.07	224	3.57%	0.09	-1.13%
Cash Flow to Sales	682	14.52%	24.94	232	15.74%	24.09	232	13.53%	25.93	218	14.27%	24.82	-1.47%
Leverage	693	45.36%	190.61	233	55.09%	209.39	236	46.47%	105.18	224	40.74%	234.12	-14.35%**

Table 4. 3– Probit models of cross-border merger completion

This table reports results of probit regressions of deal completion. All models regress the *Deal Completion* dummy against the key dummy variable *MAXTRADE12*measuringthe maximum of bilateral imports and exports trade data between China and target's country. *Deal Completion* dummy equals one if the takeover transaction is completed, and zero otherwise. Model 1 only includes the key independent variable *MAXTRADE12*; Model 2 and 3 further control for firm and deal characteristics. All models include industry and year fixed effects. All variables are defined in Appendix A. All continuous variables are winsorized at the 1% and 99% levels. The table reports marginal effects and t-statistics (in parentheses). Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

Deal Completion	**Model (I)**	**Model (II)**	**Model (III)**
MAXTRADE12	0.1263***	0.1023***	0.0841***
	(4.78)	(5.31)	(4.30)
A_LNMV		-0.0030	-0.0034***
		(-0.81)	(-4.14)
A_M2B		0.0118	0.0285
		(0.62)	(0.86)
A_CF2SALE		-0.0526***	-0.0461***
		(-3.28)	(-3.09)
A_Leverage		0.0218	0.0266**
		(0.71)	(2.08)
Relative Size			0.0011
			(0.21)
Stock			0.0328***
			(3.08)
Competing Bid			-0.0482***
			(-4.56)
Diversification			0.0091
			(1.31)
Hostile			-0.0195***
			(-2.99)
Tender			0.0445**
			(2.31)
Public			-0.0731***
			(-4.93)
State Owned			-0.0088
			(-0.68)
Ln(A_GDPpercapital)			0.1024
			(1.63)
Ln(T_GDPpercapital)			-0.0061

			(-0.59)
T_GDP growth			0.0282**
			(2.24)
A_GDP growth			0.0044
			(0.34)
Ln(Distance)			-0.0331***
			(-3.41)
Constant	-1.5842	-2.2876	3.5518
	(-0.48)	(-1.13)	(0.68)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
Chi^2	256.3184	247.2349	2452.5217
N	623	562	157

Table 4. 4– CAR Analysis

This table shows acquirer's announcement performance over three event windows on Chinese cross-border M&A transactions. CAR3, CAR5 and CAR11 represent cumulative abnormal returns (CARs) to acquirers during the 3-, 5-, and 11-day window surrounding the announcement date. Abnormal returns are computed by using market-adjusted model. First, we present the values for the full sample. The Student's t-test is used to test for statistical significance. For brevity, we do not report the t-statistics. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

	Full Sample (I)		Low (II)		Moderate (III)		High (IV)		T-Test (IV) - (II)
	N	Mean	N	Mean	N	Mean	N	Mean	Difference
CAR3	714	0.0151***	238	0.0143***	238	0.0113***	238	0.0188***	0.0045**
CAR5	714	0.0223***	238	0.0113***	238	0.0165***	238	0.0445***	0.0332***
CAR11	714	0.0304***	238	0.0163***	238	0.0092***	238	0.0658***	0.0495***

Table 4. 5– OLS Regressions of Acquirer Short-Term Performance

This table shows results of OLS regression of acquirer's announcement performance. All models regress the five-day cumulative abnormal returns against the key variable *MAXTRADE12*. Model (I) only include the key explanatory variable; Models (II) and (III) further control for firm- and deal-related characteristics. All models control for industry and year fixed effects. For brevity, their coefficients are not reported in the table. All variables are defined in Appendix A. All continuous variables are winsorized at the 1% and 99% levels. T-statistics are reported in parentheses. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

Panel C	**Model (I)**	**Model (II)**	**Model (III)**
MAXTRADE12	0.1018**	0.0262*	0.1168**
	(2.29)	(1.68)	(2.00)
A_LNMV		-0.0063***	-0.0011**
		(-4.45)	(-2.31)
A_M2B		0.0175	0.0176
		(0.41)	(0.14)
A_CF2SALE		-0.0231**	-0.0143**
		(2.35)	(-2.21)
A_Leverage		0.0019*	0.0026**
		(1.92)	(2.36)
A_Runup		-0.0087	-0.0213*
		(-1.55)	(-1.73)
Relative Size			-0.0146
			(-0.24)
All Stock			-0.0330***
			(3.32)
Competing Bid			-0.0804
			(-1.49)
Diversification			0.0083
			(0.82)
Hostile			0.0263
			(0.68)
Tender			-0.008
			(-0.33)
Public			-0.0114*
			(-1.89)
State Owned			-0.0232
			(-1.44)
Ln(A_GDPpercapital)			-0.3097
			(-1.31)
Ln(T_GDPpercapital)			-0.0063
			(-0.97)
T_GDP growth			0.0127**

			(-0.95)
A_GDP growth			0.0028
			(0.76)
Ln(Distance)			0.0055
			(0.42)
Constant	1.0473	-3.4842**	-61.1207
	(2.29)	(-2.44)	(-1.58)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
R^2	0.009	0.038	0.16
Adjusted R^2	0.004	0.026	0.050
N	714	667	182

Table 4. 6– BHAR Analysis

This table shows acquirer's long-run performance over three event windows on Chinese cross-border M&A transactions. BHAR12, BHAR24 and BHAR36 represent buy and hold abnormal returns (BHARs) to acquirers during the 12-, 24-, and 36-month window following the announcement date. First, we present the values for the full sample. The Student's t-test is used to test for statistical significance. For brevity, we do not report the t-statistics. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

	Full Sample (I)		Low (II)		Moderate (III)		High (IV)		T-Test (IV) - (II)
	N	Mean	N	Mean	N	Mean	N	Mean	Diffrence
Bilateral Trade Flows									
BHAR12	714	-0.0581***	238	-0.0915***	238	-0.0443***	238	-0.0304***	0.0611***
BHAR24	575	-0.0358***	196	-0.0631***	171	0.0298***	208	-0.0472***	0.0159***
BHAR36	497	-0.1028***	168	-0.1140***	146	-0.0881***	183	-0.0564***	0.0576***

Table 4. 7– OLS Regressions of Acquirer Long-Term Performance

This table shows results of OLS regression of acquirer's long-run performance. All models of the table regress the 36-month buy and hold abnormal returns against the key variable *MAXTRADE12*. Model (I) only include the key explanatory variable; Models (II) and (III) further control for firm- and deal-related characteristics. All models control for industry and year fixed effects. For brevity, their coefficients are not reported in the table. All variables are defined in Appendix A. All continuous variables are winsorized at the 1% and 99% levels. T-statistics are reported in parentheses. Significance at the 1%, 5% and 10% levels is denoted by ***, ** and * respectively.

	Model (I)	**Model (II)**	**Model (III)**
MAXTRADE12	0.1812***	0.1443***	0.0887***
	(4.10)	(3.80)	(3.16)
A_LNMV		-0.0047	-0.0480*
		(-0.21)	(-1.93)
A_M2B		-0.0052	-0.0023
		(-0.65)	(0.36)
A_CF2SALE		-0.0021	-0.0015
		(-0.13)	(-0.19)
A_Leverage		-0.0017**	-0.0019
		(-2.18)	(-1.20)
Relative Size			-0.0496*
			(-1.73)
Stock			-0.0189**
			(-2.01)
Competing Bid			-0.624
			(-1.00)
Diversification			0.0469
			(0.48)
Hostile			-0.1313***
			(-2.55)
Tender			0.2433
			(1.11)
Public			-0.2152**
			(-2.08)
State Owned			-0.0454
			(-0.38)
Ln(Distance)			0.0988
			(0.42)
Ln(A_GDPpercapital)			-0.6254
			(-1.44)
Ln(T_GDPpercapital)			-0.0073
			(-0.89)
T_GDP Growth			0.0279
			(1.02)
A_GDP Growth			0.0472

			(1.43)
Constant	-218.0327***	-201.4955***	-148.6001***
	(-8.35)	(-7.26)	(-3.95)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
R^2	0.1	0.13	0.245
Adjusted R^2	0.095	0.117	0.178
N	519	459	186

CHAPTER FIVE: CONCLUSION

5.1 Summary

The main objective of this thesis is to offer a comprehensive understanding of China's cross-border mergers and acquisitions including deal completion and acquirer's performance in both short- and long-term. The last two decades have witnessed a rapid growth in cross-border mergers and acquisitions. Previous literature has investigated cross-border M&As from various perspectives, for example, Datta and Puia(1995), Moeller and Schlingemann(2005), Dos Santos et al., 2008, and Bertrand and Betschinger(2011). However, the research largely focuses on the developed market such as the US and European market, and little evidence is provided on the Chinese market despite the surge in volume and value of Chinese outward deals. To fill this gap, this thesis examines the influence of three macro-economic factors on Chinese cross-border merger outcomes, including country-level stock price movements, currency movements, and bilateral trade flows of China and target countries.

Chapter three investigates the influence of valuation differences, i.e. differences in currency appreciation and stock market valuation, on the performance of Chinese cross-border mergers and acquisitions. Overall the findings show that the valuation difference between home and host countries plays a significant role in China's cross-border mergers, and Chinese acquirers could take advantage of the misvaluation effect and enjoy better performance. With 1,174 Chinese cross-border mergers and acquisitions announced between 1995 and 2016, Chapter Three finds that the wealth effects for acquirer shareholders significantly increases with the differences in stock market returns and exchange rate returns of acquirers' and targets' countries. Specifically, the results show that every unit increases in the stock return difference during the one-year before deal announcement is

related to a higher announcement return of 14.7% after controlling for other factors. This could be explained by considering that higher stock market valuation makes acquirers wealthier and target firms cheaper, leading to lower cost of capital and therefore more profit (Froot and Stein, 1991). Another explanation is that acquirers take advantage of the overvalued stock and make a profitable investment (Shleifer and Vishny, 2003).In terms of differences in currency appreciation, the result suggests that every unit rises in *CURRENCY12* is related to a 65.97% increase in acquirer's short-run abnormal returns. This is consistent with Lin, Officer and Shen (2014) arguing that the larger appreciation of the home country currency against that of the host country can increase the bargaining power of the bidder and create value for acquirer shareholders.

When examining Chinese acquirer's long-run performance, Chapter Three documents a significant negative relation between acquirers' long-term performance and the difference in stock market returns of acquirers and target countries, which is not consistent with the short-run evidence, suggesting that the valuation of acquirers with large stock market return difference experiences a reversal in the long-run. In contrast, the findings show that acquirers with relatively more appreciated currency before merger announcement experience significantly higher long-run abnormal returns.The valuation reversal is not found in the analyses of exchange rate returns, indicating that acquirers taking advantage of highly appreciated currency can create synergies in the long-run.

Chapter Four examines the effects of bilateral trade between home and host countries on Chinese cross-border mergers outcomes. With a data set of 1,130 Chinese cross-border mergers and acquisitions conducted during the period of 2001 – 2016, the findings show that the probability of completing a cross-border

acquisition increases with bilateral trade flows between China and target's country. Specifically, every unit increases in MAXTRADE12 is related to a 12.63% higher likelihood to complete a cross-border mergers, which is consistent with Erel, Liao, and Weisbach (2012) suggesting that a stronger bilateral trade relation helps reduce institutional barriers and facilitate deal completion. In addition, the results show that acquirers experience significantly higher abnormal returns in the short-run when China and the target country have more trade exchanges. Every percentage increase in the bilateral trade flows is related to 11.68% higher CARs over the 5-day around deal announcement. Similar evidence is found in acquirer's long-run performance. These findings suggest that the market is more in favour of cross-border deals involving two countries with strongertrade relations as more trade businesses could increase mutual understanding and economic integration.

5.2 Limitations and Future Research

Some of the limitations encountered in this paper can be addressed in future studies. First, only Chinese cross-border mergers and acquisitions are included in this research. Although the Chinese market accounts for a large percentage of cross-border mergers of the emerging markets, there is also a rapid growth in cross-border deals in other developing countries. It would be valuable iffuture studies could investigate the influence of valuation differences and bilateral trade between host and home countries on cross-border merger outcomes by using a sample from other emerging economies, such as India. Second, only stock performance in the long-run is examined in Chapter Three and Chapter Four. Future research may find more information if the operating performance could also be investigated.The third limitation of this thesis is that only merger

completion and acquirer's performance are examined. There is no evidence on other merger outcomes, e.g. method of payment and take premiums, which could be tackled in future studies. Fourth, only public acquirers are included in this research due to data limitations. However, over half of the Chinese cross-borderdeals are conducted by private firms. To have a better picture of the Chinese cross-border merger market, future studies could include private deals if the data is available to them.

APPENDIX A: DESCRIPTIONOF VARIABLES

Variable	Definition
Panel A:	
Dependent Variables	
ACAR5	Cumulative abnormal return of the acquiring firm in the 5-day event window (−2, +2) surrounded on the announcement day. Following market-adjusted return model, the expected firm return is equal to the market return for that period. The value-weighted Shanghai and Shenzhen market index are used in this thesis. (Source: Datastream)
BHAR36	Buy-and-hold abnormal return of the acquiring firm from size-adjusted model in the 36-month event window following the announcement. (Source: Datastream)
Deal Completion	Dummy variable that equals 1 if merger transaction is completed. (Source: Thomson Financial)
Panel B:	
Key Independent Variable	
STOCK12	The difference between the annual local real stock market return of the acquirer country and targetcountry. We obtain total value-weighted return indices in local currency for each country (Datastream code: TOTMK) and calculate stock market returns over the twelve months prior to the merger announcement. The returns are then deflated by usingthe 2000 consumer price index (CPI) in each country to calculate real stock returns. (Source: Datastream) $\left(\frac{\text{Acquirer stock price at time t}}{\text{Acquirer stock price at time t}-1}-1\right) - \left(\frac{\text{Target stock price at time t}}{\text{Target stock price at time t}-1}-1\right)$
CURRENCY12	The difference between the annual real bilateral U.S. dollar exchange rate return of the acquirer countryand target country. Wecollect nominal national exchange rates from WM/Reuters

(WMR) via DataStream for acquirer and target countries, which is directly quoted with the US dollar as the base currency. For each Chinese cross-border merger in the sample, nominal exchange returns for the twelve months before the deal announcement for acquirers and target countries are calculated. These indices are then deflated usingthe 2000 constant dollar consumer price index (CPI) in each country to calculate real exchange rate returns (inU.S. dollars). (Source: Datastream)

$$\left(\frac{\text{USD/RMB at time t}}{\text{USD/RMB at time t}-1}-1\right) - \left(\frac{\text{USD/TargetCurrency at time t}}{\text{USD/TargetCurrency at time t}-1}-1\right)$$

MAXTRADE12 The maximum of bilateral import and export between a country pair. Bilateral import (export) is calculated as the value of imports (exports) by the target country from (to) the acquirer country as a percentage of total imports (exports) by the target country. (Source: UN commodity tradedatabase)

$$Max\left(\frac{\text{The value of imports (exports)by target country from (to)acqu}}{\text{Total imports (exports)by target country}}\right.$$

Panel C:

Firm Characteristics

A_LNMV The logarithm of the acquirer market value measured 4 weeks before the merger announcement. The market value is calculated as the number of shares outstanding multiplied by the respective stock price at 4 weeks before the M&A announcement. (Source: Datastream)

$$\text{Ln(Number of Shares Outstanding} * \text{Stock Priceat 4 weeks before M\&}A)$$

A_M2B The ratio of market value by book value of the acquirer's assets.(Source: Datastream)

$$\frac{Market\ Capitalization}{Book\ Value}$$

A_CF2SALE The ratio of acquirer’s cash flows by salesat the fiscal year end

	before the M&A announcement. (Source: Datastream) $$\frac{\text{Operating cash flows}}{\text{Sales}}$$
A_Leverage	The ratio of acquirer's total debt by total capital at the fiscal year end before the M&A announcement.(Source: Datastream) $$\frac{\text{Total Debt}}{\text{Total Debt} + \text{Total Equity}}$$
A_Runup	The market-adjusted return of acquirers over the period from 200 trading days to 2 months before the issuance announcement. (Source: Datastream) $$CAR_{i,T_1,T_2} = \sum_{t=T_1}^{T_2} AR_{it}$$ $$AR_{it} = R_{it} - R_{mt}$$
Return on Assets	the ratio of acquirer's net income to total assetsat the fiscal year end before the M&A announcement. (Source: Datastream) $$\frac{\text{Net Income}}{\text{Total Assets}}$$
Panel D:	
Deal Characteristics	
Relative Size	The variable was calculated as merger transaction value divided by the acquirer market value of equity 4 weeks before the merger announcement. (Source: Thomson Financial, Datastream) $$\frac{\text{Deal Value}}{\text{Number of Shares Outstanding} * \text{Stock Priceat 4 weeks before M\&}A}$$
Stock	Dummy variable that equals 1 if the deal is 100% paid by stock. (Source: Thomson Financial)
Cash	Dummy variable that equals 1 if the deal is 100% paid by cash. (Source: Thomson Financial)
Competing Bid	Dummy variable that equals 1 if there are more than one bidder. (Source: Thomson Financial)
Diversification	Dummy variable that equals 1 if the acquirer and the target have the different first two-digit of primary SIC code. (Source: Thomson Financial)

Hostile	Dummy variable that equals 1 if the deal attitude is identified as hostile.(Source: Thomson Financial)
Tender	Dummy variable that equals 1 if the deal is identified as a tender offer. (Source: Thomson Financial)
Public	Dummy variable that equals 1 if the target is a public firm.(Source: Thomson Financial)
State Owned	Dummy variable that equals 1 if the ultimate shareholder of a firm is a government institution.(Source: Shareholder Information Database of China Stock Market & Accounting Research (CSMAR))
Panel E:	
Country Characteristics	
Ln(A_GDPperc apital)	The logarithm of the acquirer country's GDP per capitain the year before the acquisition. (Source: World Bank's World Development Indicators Database)
Ln(T_GDPperca pital)	The logarithm of the target country's GDP per capitain the year before the acquisition. (Source: World Bank's World Development Indicators Database)
T_GDP growth	The target country's annual GDP growth ratein the year before the acquisition. (Source: World Bank's World Development Indicators Database)
A_GDP growth	The acquirer country's annual GDP growth ratein the year before the acquisition. (Source: World Bank's World Development Indicators Database)
Ln(Distance)	Thedistance between acquirer and target's country measured by using latitude and longitude of capital cities. (Source: Kristian Skrede Gleditsch Wesite,http://ksgleditsch.com/data-5.html) $a = \sin^2(\Delta\varphi/2) + \cos\varphi_1 * \cos\varphi_2 * \sin^2(\Delta\lambda/2)$ $c = 2 * \text{atan2}(\sqrt{a}, \sqrt{(1-a)})$ $d = R * c$ where φ is latitude, λ is longitude, R is earth's radius (mean radius = 6,371km)

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