Impact of institutional reforms and industry structural factors on market returns of emerging market rivals during acquisitions by foreign firms

B. Elangoa,*, Karthik Dhandapanib, Claudio Giachettic

a College of Business, Illinois State University, 345 SFHB, Normal, IL, 61790-5580, USA
b Indian Institute of Management, Tiruchirappalli, Tamil Nadu, 620 015, India
c Foscari University of Venice, Cannaregio 873, San Giobbe, 30121, Venice (VE), Italy

A B S T R A C T

This paper seeks to understand the joint impact of institutional reforms and industry structural factors on market returns earned by rivals in an emerging market during foreign acquisitions. We use a sample of 238 foreign acquisitions in India during the period 2004–2013 and find empirical evidence to support the notion that institutional reforms, foreign competition and business group competition positively impact the market returns of the rivals of acquired firms. Additionally, we find that the effects of foreign competition and business group competition on rivals’ market returns are shaped by the degree of institutional reforms in the industry, indicating that firms’ market returns in emerging markets during foreign acquisitions can be better understood through the incorporation of the joint role of industry structural factors and institutional reforms.

1. Introduction

Conventionally, the impact of foreign acquisitions on local rivals’ performance has been studied in the literature largely under the aegis of the Industrial Organization framework starting from Stigler (1950). This view of acquisitions, which is competition-centric (Uhlenbruck, Hughes-Morgan, Hitt, Ferrier, & Brymer, 2017), has been tested in various settings. While a certain degree of empirical evidence has been found across studies indicating the validity of this view, as one should expect, authors have suggested that several research questions remain unanswered, and thus “further research in this vein regarding M&A activity is certainly merited” (Clougherty & Duso, 2009: page 1385). Within this stream of literature, we observe a lack of studies examining whether and how the impact of foreign acquisitions on local rivals’ market returns is influenced by institutional reforms in the specific context of emerging markets. In recent years, many emerging markets have undergone much-needed institutional reforms to reduce the role of the state in the economy and increase the role of market forces operating in the economy (Williamson, 1990), with inevitable consequences on investment decisions of foreign firms (Kafouros & Aliyev, 2016) and industry dynamics in these markets (Popli, Akbar, Kumar, & Gaur, 2017).

Empirically, the fact that institutional reforms affect the performance of firms has been well-established (these studies are reviewed in Popli, Akbar et al., 2017). Still, some studies on this topic suggest that the impact of the implementation of institutional reforms on firm performance should not be examined in isolation, but the interplay with industry-level factors should be taken into account (e.g., Chittoor, Sarkar, Ray, & Aulakh, 2009; Pai & Morgan, 2007; Park, Li, & Tse, 2006). That is because reforms may have a different influence on firm performance depending on the structural characteristics of the industry the firm belongs to (e.g., concentration, business group affiliation, etc.). In this vein, in the specific context of our study, we should expect that during foreign acquisitions, market returns of rivals of an acquired local firm will be affected by the joint influence of industry structural characteristics and institutional reforms. Therefore, this paper seeks to incorporate the influence of institutional reforms and industry factors on performance outcomes for target firms’ rivals in emerging markets during foreign acquisitions.

In particular, this study will focus on two critical industry variables whose effect on market returns of rivals of the acquired firms is likely to be significantly influenced by institutional reforms: foreign competition and business group competition. We focus on foreign competition, as it is known that competition by foreign firms results in a special dynamic in the domestic marketplace by impacting productivity, knowledge spillover, profitability, and investments through the alteration of the nature of competition due to different resource positions (e.g., Blomström, 1986; Caves, 1974; Caves & Mehra, 1986). Many studies have highlighted foreign competition as one of the fundamental variables affecting industry characteristics and profitability (e.g., Elango &...
Pattnaik, 2013), as foreign firms are believed to bring major changes to local firm strategies (Hutzschenreuter & Gröne, 2009), in addition to changes to industry and institutional settings for domestic firms (Kumaraswamy, Mudambi, Saranga, & Tripathy, 2012).

The other variable we focus on is business group competition, as business groups represent a differentiating characteristic of emerging markets, and business group-affiliated firms are widely prevalent and a core element of the emerging market business landscape (Gaur & Kumar, 2009; Khanna & Rivkin, 2001). For example, it has been estimated that about two-thirds of firms in Indonesia, one-fifth of those in Chile (Khanna & Yafeh, 2007), and nearly half of all firms in India (Gaur & Kumar, 2009) are affiliated with business groups. As noted by some authors, empirical evidence on how and whether business groups affect competition is quite scarce, and results are decidedly mixed (Khanna & Yafeh, 2007). Some studies suggest business groups tend to collude as a form of deterrence against foreign competition, while others show that they tend to compete aggressively against each other (e.g., Encaoua & Jacquemin, 1982; Popli, Ladkani, & Gaur, 2017; Singh, Pattnaik, Gaur, & Ketençigilo, 2018; Weinstein & Yafeh, 1995). We aim at complementing this literature by examining how market returns earned by rivals in an emerging market during foreign acquisition of a local rival are influenced by the degree of business group competition.

Using a sample of foreign acquisitions in the Indian market, this study seeks to capture the impact of institutional reforms and industry forces on the market returns of local industry rivals. In particular, this paper will empirically seek to answer the following three questions: (1) How do industry structural characteristics impact market returns accrued to rivals of the target firm in an emerging market during foreign acquisitions? (2) How does the extent of institutional reform impact market returns accrued to rivals of the target firm in emerging markets during foreign acquisitions? and (3) What is the joint (i.e., interactive) influence of industry structural characteristics and institutional reforms on impacting market returns of rivals of the target firm in emerging markets?

This study seeks to contribute to three streams of literature. First, extant literature on the impact of acquisitions on rival firms (e.g., Uhlenbruck et al., 2017) that looks at cross-border acquisitions in particular (e.g., Burns & Liebenberg, 2011) – which originates from the strategic management, industrial organization, and finance fields – forms the basis of our main theoretical arguments about the performance outcome of rivals during foreign acquisitions. Second, we draw on the industry-based view of strategy (Porter, 1980; Rumelt, 1991) to examine industry-level antecedents of market returns of rivals during foreign acquisitions. Third, the institution-based view of strategy (Peng, 2002; Peng, Wang, & Jiang, 2008) is essential to theoretically consider whether market returns accrued to rivals are influenced by institutional changes.

A study of this nature is of interest to practitioners, as firms in emerging markets face an increasingly intense competitive environment due to the entry of foreign firms, in addition to revitalized business group firms actualized by the reforms. In 2013, Etihad Airways, the national airline of United Arab Emirates, made a deal to invest a 24% stake in India’s Jet Airways, the first deal after the Foreign Direct Investment policy was amended for the Indian aviation sector. A former federal minister commented that the deal would lead to a “certain demise of our national carrier Air India” (Knowledge@Wharton, 2013, April 25) which at that time commanded a market share of 19.2% (Shukla, 2014). Similarly, in their bankruptcy filing application in March 2018, the board of one of India’s oldest telecom firms, Aircel, attributed “troubled times to intense competition” following the disruptive entry of Reliance Jio Infocomm, backed by a prominent business group (Kundu, 2018).

In the following two sections of this paper, we present the theoretical underpinnings and develop hypotheses for the relationships that will be tested. Next, we present the sample, measures, and the methodology employed. We will then turn to the analysis of the study results along with the limitations of this research. In the final section, we discuss the study implications for research and practice.

2. Theory background

Extant literature has looked at acquisitions and its effect on rivals’ market returns in two different settings, namely, domestic acquisitions versus international acquisitions. These two settings present marked differences, and in fact some of the theoretical arguments offered apply only to one of these specific contexts, while others apply to both. For example, the acquisition of a firm has been conventionally viewed as a reduction in the number of rivals, thereby increasing the market power of all incumbent firms and the ability to potentially gain from economies of scope or scale (Uhlenbruck et al., 2017). Additionally, it is thought that acquisitions could create collusive synergies, due to the ability of firms in the industry to collectively raise prices in a collusive manner (Chatterjee, 1986). This view, based on increased market power (Eckbo, 1983, 1985; Eckbo & Wier, 1985), argued for benefits to all rivals due to increased concentration and greater bargaining ability with customers and suppliers. Therefore, the belief was that rivals of the merging firm would benefit collectively by such a transaction (Stigler, 1950). In the context of foreign acquisition of a local firm, however, a reduction in the number of firms does not happen, since “a local competitor is often replaced by a foreign competitor, thus the number of competitors does not change” (Clougherty & Duso, 2009: page 1370) and therefore the benefits accrued due to increased concentration and collusive synergy may be lacking to rivals operating in the industry.

Another perspective calling for beneficial effects for rivals during a foreign acquisition transaction is the notion of signaling, i.e., the signaling hypothesis (Jovanovic & Braguinsky, 2004; McCradie & Viswanathan, 1994), which suggests that market returns are an informative signal of the potential of the industry and indicative of the future of the industry. This leads to anticipation (anticipation hypothesis) of the value of the premium (or discount) a rival’s firms would receive (Malatesta & Thompson, 1985; Song & Walkling, 2000). By drawing on this literature, based on a sample of firms from China during the period 1993–2008, Gaur, Malhotra, and Zhu (2013) did find support for the hypothesis that market rivals of the acquiring firms experienced positive returns. The authors explained this relationship with what they call the growth profitability hypothesis, which suggests that when a foreign firm acquires a local rival, future potential of the industry is desirable and therefore rival firms would face positive returns. Similarly, Akhigbe and Martin (2000) find that stock prices of domestic competitors are benefitted with higher prices when acquisitions by foreign firms take place in the U.S. Clougherty and Duso (2009) offer a differing rationale as to why rival firms could face positive returns during horizontal mergers. They argue that, given the mixed evidence of the success of acquisitive transactions, rival firms could actually benefit due to difficulties faced by firms in restructuring and combining operations. Additionally, in the case of foreign investments in the emerging markets, there is also a likelihood that the rival firms in the host market would gain from spillover effects due to learning, along with other indirect benefits due to new investment opportunities in a market with growth potential (Zhang, Li, Li, & Zhou, 2010).

The topic of the impact of mergers and acquisitions on target rivals has received attention in the literature (Uhlenbruck et al., 2017). Therefore, we conducted a systemic literature review [based on the six steps offered by Gaur & Kumar, 2018] and found only four studies that looked at the factors driving market returns of rival firms during international acquisitions. We briefly review these studies in Table 1 to demonstrate the different conceptual framing as well as study sampling contexts. While these studies offer varied insights, we also believe several unanswered questions remain regarding the impact of the foreign acquisition on rivals of the target in an emerging market undergoing institutional reforms. In such markets, the institutional reform
دریافت فوری متن کامل مقاله

ایمکان دانلود نسخه تمام متن مقالات انگلیسی
ایمکان دانلود نسخه ترجمه شده مقالات
پذیرش سفارش ترجمه تخصصی
ایمکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
ایمکان دانلود رایگان ۲ صفحه اول هر مقاله
ایمکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
دانلود فوری مقاله پس از پرداخت آنلاین
پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات