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21 years of international M&As and joint ventures by Italian medium-sized listed firms: Value creation or value destruction?

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ABSTRACT

This study provides evidence of the value creation of different equity entry modes in a sample of international investments performed by all Italian medium-sized listed firms in the period 1986–2006. Our research shows a positive and significant market reaction to announcements of internationalization strategies. The results are largely affected by high-equity entry modes carried out in advanced economies. Low-equity entry modes and international operations performed in emerging countries show no significant market reaction. We also find that the relative size of the deal, the firm age, the country risk, and the evolution of information disclosure regulation, matter in explaining the outcomes.

1. Introduction

In the last 40 years, the intensity of the internationalization process of Italian firms has been growing. Unlike other developed countries, whose studies on internationalization are mostly related to large multinational corporations, the majority of Italian studies relies on SMEs (Zucchella and Maccarini,

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1999; Depperu, 1997) which are considered to be distinctive of the Italian entrepreneurial base. Italian SMEs are used to going abroad through either non-equity or low-equity entry modes, such as exporting and joint ventures because of their low confidence in international M&As. The propensity of Italian firms to go international through high-equity entry modes is more recent and in any case growing in the last years. Between 2002 and 2007, the Italian outward FDIs increased 3.6% if we look at the average growth rate of foreign shareholdings and 5.8% if we look at the number of subsidiaries (ICE, 2009, p. 290). It is worth noticing that medium-sized enterprises contributed the most to the above growth, despite their relatively low incidence on the total FDI stock (Mariotti and Mutinelli, 2009). These data led us to argue that internationalization strategies of SMEs are likely to be remarkably different depending on the specific size of constituent firms (e.g., micro, small, and medium firms).

In the Italian context, the use of SMEs as an undifferentiated concept does not give light to the specific behavior of each dimensional class (Coltorti, 2006). Medium-sized enterprises can be considered as a hybrid model between smaller and larger firms. On the one hand, they present the same structure as smaller ones; on the other hand, they have already experienced more complex market environments as larger firms. Medium firms rely on advantages and forces stemming from industrial district affiliation and niche products (Becattini et al., 2009) and, at the same time, they are structured as international networks and therefore can also benefit from the advantages of multinationality.

The amount of research focusing on market reaction in response to internationalization announcements made by medium-sized enterprises has been very limited with a mix of results. The study aims at investigating the market performance of those firms that choose to internationalize and accordingly we expect to find a positive and significant market reaction in response to internationalization announcements.

The remainder of the article is organized as follows: Section 2 provides the conceptual background according to the principal statements set by both theoretical and empirical contributions, in order to qualify the relationship between the internationalization process of the firm and its performance; Section 3 provides the description of the variables that are supposed to affect the value creation of internationalization strategies; Section 4 illustrates the sample and research design; Section 5 discusses results and limitations of the study; Section 6 tries to draw some conclusions and policy implications.

2. Literature review

In the last decades, the growth of international deals also involving small- and medium-sized firms led to the expectation that multinationality could generate advantages (Dunning, 1979; Kogut, 1983) by reducing the marginal cost of foreign investments of firms already involved in internationalization processes (Ietto Gillies, 2002). Although some literature suggests that foreign activities and country diversification processes do not affect corporate performance (Rugman, 1981), a number of studies (Beamish and Newfield, 1984; Rugman, 1986; Stopford and Dunning, 1983; Lu and Beamish, 2001) found that internationalization choices were linked to performance with different intensity. Specifically, multinational firms were able to increase their competitive advantage by coordinating international activities achieving benefits in terms of economies of scale and scope and economies of learning (Bartlett and Ghoshal, 1989). Additional value creations came from the ability to exploit different market, employment, and tax regulations in the host country.

Hsu and Boggs (2003) argue that firm financial performance is affected by the degree of international involvement according to an inverted U-shape relationship as a result of an escalation of risks, costs, and organizational problems. The positive relationship between internationalization and performance expected for small-sized firms engaged in international expansion is not inconsistent neither with the Uppsala school of thought proposing a step-by-step internationalization process with reference to experience, distance, and entry mode (Johanson and Vahlne, 1977), nor with the framework of born global firms (Oviatt and McDougall, 1994; Bloodgood et al., 1996; McDougall and Oviatt, 1996).

Hypothesis 1. Italian medium-sized listed firms are expected to show a positive stock market reaction to announcements of internationalization strategies.