INTERNATIONAL TAKEOVERS:
A COMPETITIVE ACQUISITION MARKET

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──────────── ⟨ABSTRACT⟩ ────────────

This study investigates the wealth effect of foreign acquisition of U.S. based firms. Contrary to previous studies, this analysis demonstrates that after appropriate control of domestic-acquired targets, the wealth gains to the shareholders of targets in foreign takeovers are similar to those in domestic takeovers. This paper investigates the validity of the competitive acquisition market in cross-border takeovers and concludes that : 1) in cases of inward foreign direct investment into the U.S., foreign firms do not realize significant net benefits from acquisitions; and 2) the foreign acquirer is as well informed as its U.S. counterparts about the target's market. The results of this study are consistent with the view that each country has different motivations for investing in the U.S. market. Consider, for example, Japan. The evidence suggests that Japanese companies pay a considerable price for U.S. targets which have performed poorly before the takeover. While there is no specific rationale to explain why Japanese firms buy the most volatile and worst performing firms, international barriers may provide a possible reason for these anomalies. Overall, the evidence of this paper supports the view that foreign takeovers occur in a competitive acquisition market.

I. INTRODUCTION

Domestic mergers have been analyzed from a variety of points of view, such as motives, wealth effects, and performance.[1] Conversely, international mergers have not received equivalent attention, especially given the increasing importance of globalized finance

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1) See Jarrell, Brickley, and Netter [12] and Jensen and Ruback [14] for a comprehensive review.

over the last decade. This study compares the wealth gains to U.S. targets in cross-border acquisitions with those observed in 'pure' domestic takeovers.[2] In a rational and competitive market, where all information is widely available, the wealth effects of foreign acquisitions should not differ from those of domestic ones. Yet previous studies have demonstrated that shareholders of a U.S. target realize superior wealth gains when their firm is taken over by a foreign acquirer. However, these studies failed to appropriately control for the targets in domestic takeovers. This study implements an appropriate control group and analyzes the differences between foreign acquirers and domestic acquirers.

To the extent that each firm evaluates the potential target and offers a bid as long as it is advantageous to do so, the offer price is bid up to the level where the expected net present value of the target is negative for all but the successful bidder (Ruback [29]). In such a rational competitive acquisition market, there is no a *priori* justification for the gains to target firms in cross-border takeovers to exceed the gains generated in domestic takeovers. If the gains from cross-border transactions systematically exceed those realized in domestic acquisitions, there are two alternative explanations. Either foreign acquisitions significantly improve the acquirers' risk-return profiles and provide them with excess benefits (*net-benefit hypothesis*), or the foreign acquisition process creates a situation for the bidder to revise upward its expectations of the target's value (*information-deficiency hypothesis*).

While various hypotheses have been proposed regarding the net benefits to foreign acquirers and hence to targets, to date the empirical findings on the market's recognition of the value of international corporate expansion are inconclusive. Considering that the foreign acquirer is at least as well informed as its domestic counterpart about the target's market, this research concludes that foreign acquisitions of U.S. firms occur in a rational and competitive market.

Section II presents a discussion of the literature describing returns to acquiring and

2) A 'pure' domestic takeover is one in which both the acquirer and the target are U.S. based.

acquired firms in cross-border takeovers. It provides some evidence to refute the *net-benefit hypothesis* and the *information-deficiency hypothesis*. Section III describes the data and methodology and Section IV discusses the results and several alternative analyses of the observed phenomena. Summary and conclusions are presented in Section V.

II. CROSS-BORDER TAKEOVERS: RELATED THEORIES AND EVIDENCE

II-1. Net-Benefit Hypothesis

If foreign acquirers are expected to receive incremental benefits from cross-border takeovers, they can afford to pay larger premiums to target shareholders than can their domestic counterparts. Most studies of international acquisitions utilize theories of foreign direct investment (FDI) to spell out the motivation and systematic advantages inherent in multinational acquiring firms.[3] Several hypotheses have been presented regarding various aspects of the wealth effects of cross-border takeovers.

International acquisitions and the net benefits accruing to the acquiring firms have been concerned with national and international market imperfections and institutional restrictions such as tax codes, tariffs, and accounting regulations. Froot and Stein [7] suggest that foreign acquirers may have a purchasing advantage when the dollar is weak. While Scholes and Wolfson [30] argue that tax law changes in the U.S., especially in the 1980s, have given particular incentives to foreign buyers, Haas and Karls [8] assert that foreign companies may enjoy double tax benefits by forming a third-country subsidiary to finance the acquisition. In addition, Choi and Lee [4] suggest that foreign firms, particularly from the U.K., can pay more than U.S. firms due to the U.K.'s favorable accounting treatment of purchased goodwill.

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3) A multinstional corporation may choose to form a *de novo* subsidiary or to buy an existing company as an international investment. Wilson [33] notes that when a foreign company invests in the U.S., it is likely to acquire an established company and thereby secure a foothold in the market.

Doukas and Travlos [5] and Fatemi and Furtado [6] examine the wealth effects of international acquisitions on the shareholders of U.S. acquiring firms. They find that the shareholders of U.S. multinationals that expand into less developed countries reap significant wealth gains. The gains are particularly substantial when U.S. firms expand into new industries and geographic areas.

However, this "corporate multinationalism" does not seem to apply if foreign companies invest in developed regions (such as the U.S.), where they had prior business involvement, and where they seek related acquisitions.[4] Therefore, foreign acquisitions in the U.S. are not expected to produce positive wealth gains to the acquiring firms' shareholders. Kim and Lyn [16] find that foreign multinationals operating in the U.S. do not necessarily enjoy monopoly-oligopoly advantages over their U.S. competitors.

Mathur, Rangan, Chhachhi, and Sundaram [23] support the above argument-that in foreign takeovers of U.S. firms abnormal returns to the shareholders of the acquiring firm are negative and significant. In contrast, Cakici, Hessel, and Tandon [2] report that foreign acquirers realize positive and significant wealth gains. However, these gains are realized only when foreign firms acquire units spun off by a U.S. parent company; otherwise, these gains are insignificant. In sum, the existing evidence on the net-benefit hypothesis in foreign acquisitions of U.S. target firms does not appear to justify a large premium (if any) to the shareholders of U.S. targets. In this regard, the wealth effects to U.S. targets in cross-border takeovers must be reexamined.

The research regarding the effect of cross-border takeovers on U.S. target shareholders' wealth subsumes the benefits of FDI and analyzes the results accordingly. Harris and Ravenscraft [9], Marr, Mohta, and Spivey [21], and Shaked, Michel, and McClain [31] find that foreign-acquired targets have significantly higher abnormal returns than U.S.-acquired targets. Such gains are positively related to the strength of the bidder's home currency relative to the U.S. dollar. This finding is consistent with Froot and Stein's [7] exchange rate argument in FDI (Harris and

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4) Harris and Ravenscraft [9] report that 75% of cross-border takeovers occur in related industries and 52% of the foreign acquirers already
    have some U.S. operations.

Ravenscraft [9]). However, no conclusive evidence is found to determine whether the FDI-related factors cause the differential wealth gains between target firms in cross-border and domestic takeovers.

In a recent paper, Cebenoyan, Papaioannou, and Travlos [3] argued that "corporate multinationalism" enhances the value of the specialized resources of the targets. They suggested that the excess takeover gains from foreign takeovers are realized only when the competition for acquisitions is intense in a given industry. Furthermore, the authors found that the gains are specific to certain industries. Cebenoyan, Papaioannou, and Travlos [3] and Harris and Ravenscraft [9] note the concentration of foreign takeover activity as well as the substantial target wealth gains in high-technology or R&D-intensive businesses.[5] This industry effect in takeover gains suggests that the wealth consequences to U.S. target firms in cross-border and domestic takeovers are different from what previous studies have found, especially if some of the takeover characteristics (including an industry factor) are matched with or controlled for the respective targets. In fact, Cebenoyan, Papaioannou, and Travlos [3] observe that the wealth gains in cross-border takeovers are not always greater than those in domestic acquisitions. Although that study attributes the differing results to changes in taxation, regulation, and other competitive factors in the 1980s, their study argues that their findings may still be valid, regardless of time periods.

In order to evaluate the wealth gains in cross-border and domestic takeovers, one must control the domestic targets with respect to the following characteristics :
  (1) Industry : The industry of the foreign-acquired target is matched with that of the domestic-acquired target, since Lee [17] reports that in the period surrounding the takeover, the abnormal wealth gains differ by industry.
  (2) Method of payment : Since cash offers are associated with significantly higher abnormal returns than stock swaps (Huang and Walkling [10] and Wansley, Lane, and Yang [32]), the domestic-acquired targets are selected based on the

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5) The industry effects on target wealth gains between foreign and domestic gakeovers differ in two studies. While Cebenoyan, Papaioannou, and Travlos [3] find some evidence of the differential gains for high-technology, Harris and Ravenscraft [9] find no difference in wealth gains for R & D-intensive businesses and others.

method of payment. Most foreign acquirers pay cash (Harris and Ravenscraft [9]).

(3) Time: A variety of political and economic conditions in the 1980s created a particularly competitive atmosphere for takeovers (Jarrell, Brickley, and Netter [12] and Jensen [13]). The domestic-acquired targets are chosen according to the decade of transaction (i.e., 1970s vs. 1980s).

(4) Industrial Relatedness : Related industries are defined as those with the same two-digit SIC code. Most cross-border takeovers are in related industries (Harris and Ravenscraft [9]).

(5) Exchange: The stock exchange listings of the targets are matched to others on the same exchange to consider any effect of size on the abnormal returns.[6]

II-2. Information-Deficiency Hypothesis

Another possible explanation for the high premium is that the foreign acquirer is not fully informed about the target's market and other important valuation parameters. As a result, it falls victim to the "winner's curse," thus overpaying for the target (Shaked, Michel, and McClain [31]).[7] As the uncertainty associated with the future performance of the target or with expected takeover gains increases, it is more likely that bidders will base their offers on different assessments. Since the uncertainty associated with the assessment of the target's cash flows may be greater for foreign than for U.S. acquirers, foreign acquirers contemplating the purchase of a U.S. firm may be more willing than their domestic counterparts to pay a higher price for the target.

To examine the *information-deficiency hypothesis*, this study employs two kinds of information-related measures. First, to assess the overall uncertainty of the target up for bid, the study uses the standard deviation of the daily stock returns including dividend.[8] Second, pre-takeover performance of the foreign-acquired targets is compared with that of domestic-acquired targets. It is hypothesized that if foreign acquirers' information is deficient compared to that of domestic acquirers, foreign

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6) Due to the limited sample size, the control process focuses focuses mainly on the first three variables (industry, method of payment, and time). The other two conditions are applied whenever an acceptable size is available.

7) For the conditions under which the winner's curse is likely to occur, see Lee [18].

8) Since this study evaluates the volatility of the targets in isolation with the acquiring companies, the total risk(α) rather than the systematic risk (β) in portfolio context is more relevant.

acquirers are more likely than U.S. acquirers to buy poorer performing and/or more volatile companies.

III. RESEARCH DESIGN

III-1. Sample Data

The initial sample was drawn from the "Research Company" database on COMPUSTAT between 1970s and 1980s.[9] As of March 15, 1990, 3462 merger-related research companies were identified. To belong to the final sample, takeovers must meet the following criteria :

(1) Major Exchange : If a firm is not listed on the NYSE, AMEX, and OTC, it is excluded.

(2) CRSP (Center for Research in Security Prices) Availability: If a company is not listed on the database, it is excluded.

(3) Partial Acquisition : If less than 50% of controlling interests of a firm is involved, that firm is excluded.

(4) Wall Street Journal Index (WSJI) : If no information about the acquisitionis available, the company is excluded.

(5) Data Availability : A firm is required to have data available on both the CRSP tapes and the COMPUSTAT database for a period of approximately five years ending one year prior to the announcement.[10]

(6) Divestitures and LBOs (Leveraged Buyouts) are excluded since they may exhibit different characteristics than mergers.

(7) Multiple Bidding: If there is more than one bidder involved, the transaction is excluded.[11]

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9) The COMPUSTAT database classifies companies as either "active" or "research." While an "active" company is on the exchanges, a "research" company is a company that was delisted from the exchanges due to mergers, bankruptcy, and so forth. The database provides information for the last 20 years.

10) If security returns are not available for this entire 60-month period, a shorter interval of not less than 30 months is used.

11) Targets acquired in multiple bidding situation exhibit significantly higher abnormal returns than those acquired in a single bidding situation (Bradley, Desai, and Kim [1]). This study excludes targets involved in a multiple bidding because of the difficulty in separating the effect that foreign acquisitions and multiple bidding have on shareholder returns.

Exhibit 1

SAMPLE CONSTRUCTION AND SCREENING PROCESS

Research companies counted 3/15/90	5,575

The screening process to obtain the final sample is as follows:

Non-merger[1]	(2,113)
Merger-related Research Company	=3,462
Non-major Exchange	(509)
CRSP Availability	(220)
Partial Acquisition or No Information	(850)
Available Deals	=1,883

Among 1,833 deals identified, final targets for analysis are obtained as follows:

	1,883
Data Availability	(834)
LBOs	(85)
	=964

964 companies are divided into:

Foreign-Acquired Targets   135   829   **Domestic-Acquired Targets**

Multiple Bidding[2]	(35)	(119)
Foreign Group	=100	
		=710

Two groups of domestic-acquired targets are separately obtained from final 710 co.s:

after careful control	159	Domestic Control Group
random selection	200	Domestic Random Group

1. Reasons for non-merger deletion:bankruptcy, liquidation, etc. (coded 2, 3, 5, and 10 in COMPUSTAT)
2. For foreign-acquired targets, only 18 targets are involved in a multiple bidding situation. The remaining 17 targets are not included for a varietey of reasons. For example, 7 of those targets have multiple acquirers, which are combination of U.S. and foregin acquirers.

(8) Domestic Control : Domestic-acquired targets, which are to be compared with foreign-acquired targets, are selected based on the criteria specified in Section II-1 : industry, method of payment, time, industrial relatedness, and exchange.[12)]

Using these criteria, 100 foreign-acquired targets ("foreign group") and 159 domestic-acquired targets ("domestic control group") have been identified for the analysis. The foreign-acquired targets are then classified by bidder' s country of origin to see if there is any country effect : United Kingdom (U.K.) 45, Canada 12, Europe (excluding U.K.) 30, and Asia & Oceonia 13.[13)] In addition, 200 domestic-acquired targets are chosen randomly ("domestic random group") to illustrate the differential wealth effects without appropriate control. While most studies observe and analyze the gains generated by the domestic random group, this study is unique in that it considers the gains generated by the domestic control group. Exhibit 1 details the screening process used to obtain the final sample of targets.

III-2. Event Study Methodology

The event study methodology provides the framework for estimating the premiums paid by the acquirers to the target firms in foreign and domestic acquisitions. The capital asset pricing model (CAPM) is used in calculating the premiums paid to the target firm. The study generates deviations between actual and expected rates of return. These abnormal returns are cumulated and analyzed separately for each target group. The premiums are observed by considering the cumulative abnormal returns (CARs) of the target firms.

This analysis considers abnormal returns around the date of the announcement of the takeovers. The day prior to the first public announcement date of the takeover in the Wall Street Journal (*WSJ*) is used as the announcement date. In fact, it is the date

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12) All necessary information including bidder's home country is identified in the *Wall Street Journal Index, Mergers and Acquisitions* [24], and *Predicasts F & S Index* [28].

13) "Europe" includes W. Germany (9), Switzerland (7), France (5), Netherlands (5), Sweden (2), Belgium (1), and Italy (1). "Asia & Oceonia" includes Japan (8), Australia (4), and New Zealand (1). In some categories several countries are grouped together to maintain at least 10 targets for statistical significance.

when either party indicated publicly that a merger or takeover was being considered (see Michel, Shaked, and Lee [25]). In the 71-trading day interval surrounding the announcement date (from 40 days before to 30 days after), the abnormal returns for portfolios of acquired firms are attributed to the announcement of the proposed acquisitions. The average portfolio abnormal returns for a specific target group on a given day are then analyzed to determine whether the excess return are statistically significant.

The abnormal returns (ARs) for each company are calculated by subtracting the expected returns from the actual returns for each day under investigation. Then, daily abnormal returns for each company are summed over the period of investigation to obtain cumulative abnormal returns (CARs). Average abnormal returns ($\overline{AR}$s) for each day are calculated for the portfolios of the target firms in foreign and domestic takeovers. Finally, the average cumulative abnormal returns ($\overline{CAR}$s) for each target group are obtained by summing the average abnormal returns over the period of investigation.

III-3. Measures of Corporate Performance

The firm's performance is adjusted relative to its industry ; this is done because Morck, Shleifer, and Vishny [26] note an industry effect in the past performance of hostile targets. It is apparent that management cannot control the industry-wide movement. This study forms a benchmark to control for the industry component of performance. For each industry (as defined by the two-digit SIC code), 30 firms without takeover involvement are selected in alphabetical order from the COMPUSTAT database.[14] Since the performance is measured for four years prior to the target's announcement, and the earliest announcement year is 1975, the benchmark performance covers the time interval 1971-1989.

Three measures are used to evaluate the pre-takeover performance of the target

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14) This is common practice in empirice emprical works, and researchers have concluded that the assignment of two-digit SIC codes to firms for industry classification is meaningful (see Lee [17]). The product line accounting for the largest percent of sales will determine the Primary SIC code in the COMPUSTAT database.

firms. The first two measures are based on the growth of income and free cash flow, as suggested by Morck, Shleifer, and Vishny [27] and Lehn and Poulsen [19], respectively. Income is defined as Net income+Interest expense+Deferred taxes. Free cash flow is calculated as Operating Income before Depreciation-Interest Expense-Total Income Taxes-Preferred Dividend-Common Dividend. The growth measure is defined as log (P(Y-1))-log (P(Y-4)), where Y is the year of the first announcement date and P is income or free cash flow (see Morck, Shleifer, and Vishny [27]). Industry-adjusted growth is then computed by subtracting the growth measure of the benchmark from that of the target firm.

The measure of the target firm's industry-adjusted stock return uses equally weighted monthly returns as benchmark returns for each industry. Industry-adjusted returns for each target firm are computed by subtracting the benchmark return from the target's return during the same calendar month and then accumulating the results for the three year period ending one year prior to the announcement (see Martin and McConnell [22]).

Positive values of industry-adjusted measures indicate that the target firm is performing well within its industry, while negative values indicate poor performance. Another performance-related measure, the standard deviation of the daily stock returns, is calculated for one-year period, ending one year prior to the announcement (See Lee [18]). In addition, the strength of the foreign acquirer's home currency relative to the dollar is measured as a "proportionate difference". That is, the buyer's average exchange rate (expressed in units of foreign currency per dollar) for the period 1974-1989 is subtracted from the currency's exchange rate at the announcement year; this difference is then divided by the average exchange rate (See Harris and Ravenscraft [9]).[15], [16] Positive values indicate a stronger bidder's home currency and a weaker dollar, and negative values indicate the reverse.

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15) The sample period 1974~1989 for the average exchange rate is chosen to avoid any complication from the floating exchange rate which began on March 19, 1973.

16) If the announcement date is after June, the exchange rate at the announcement year is used ; otherwise, the exchange rate of the year before the announcement is used, as suggested by Harris and Ravenscraft [9]. The annual exchange rate is obtained from International Financial Statistics [11].

IV. EMPIRICAL RESULTS

IV-1. Time-Series Analysis

The time series of cumulative abnormal returns (CARs) of the portfolios of 100 foreign-acquired targets (foreign group) and 159 domestic-acquired targets (domestic control group) provides the basis for determining the wealth effect of the foreign acquisition on the target firms. Exhibit 2 presents the average abnormal returns ($\overline{\text{AR}}$s) and average cumulative abnormal returns ($\overline{\text{CAR}}$s) for the period +5 days surrounding the announcement date. The $\overline{\text{AR}}$s and $\overline{\text{CAR}}$s are presented for the groups of foreign, domestic control, and domestic random, and classified by the bidder's home country among foreign-acquired targets. The t-statistic shows that the abnormal returns for the subsamples are statistically significant surrounding the announcement date.

The plot of the target firm CARs in Exhibit 3, along with the results in Exhibit 2, clearly suggests that the targets of foreign acquirers do not have higher wealth gains than those of targets of domestic U.S. firms. On the announcement day, the average ARs and CARs of the foreign group (12.46% and 18.04%) are not statistically different from those of the domestic control group (10.98% and 19.23%). The same results hold when the subsamples of cash bids for the two groups are compared.[17] As expected, the wealth effects of the foreign group differ from those of the domestic random group, which is chosen without appropriate control. While the difference of the CARs between the foreign and domestic random groups is marginally significant on day+1 (t-statistic=1.69; p-value=0.093), it approaches 8% and becomes statistically significant at the 5% level by day+7. The results demonstrate the importance of appropriate control for determining the wealth effects of foreign acquisitions.

The analysis is also performed at the industry level. Only four industries (SIC 28, 35,

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17) This study identifies 53 foreign-acquired targets and 71 domestic-acquired targets whose method of payment is cash. The CARs on the announcement day for the former are 17.05% and for the latter are 20.37%.

Exhibit 2

ABNORMAL RETURNs (ARs) AND CUMULATIVE ABNORMAL RETURNs(CARs)
Portfolios of the Target Firma:Foreign, Domestic Control, Domestic Random Groups

Days	Avg. CARs	Avg. ARs	T-statistic	Significance
		1. Foreign Group		
-5	0.0233	0.0032	0.8035	
-4	0.0272	0.0038	0.7845	
-3	0.0343	0.0071	2.0653*	
-2	0.0492	0.0148	3.6829**	
-1	0.0558	0.0066	1.7915	
0	0.1804	0.1246	5.9259**	
1	0.2206	0.0403	2.9491**	
2	0.2217	0.0010	0.4023	
3	0.2245	0.0028	0.7286	
4	0.2238	-0.0006	-0.2434	
5	0.2279	0.0041	1.7514	
		2. Domestic Control Group		
-5	0.0405	0.0065	2.0330*	
-4	0.0429	0.0025	0.8715	
-3	0.0514	0.0084	2.0238*	
-2	0.0670	0.0157	4.5196**	
-1	0.0825	0.0155	3.8776**	
0	0.1923	0.1098	7.3226**	
1	0.2270	0.0347	4.0939**	
2	0.2273	0.0003	0.1670	
3	0.2275	0.0002	0.0905	
4	0.2285	0.0015	0.5070	
5	0.2333	0.0048	2.6402**	
		3. Domestic Random Group		
-5	0.0145	0.0035	1.5034	
-4	0.0190	0.0045	2.0243*	
-3	0.0238	0.0048	2.1846*	
-2	0.0323	0.0085	3.5089**	
-1	0.0445	0.0121	3.9633**	
0	0.1264	0.0819	7.8119**	
1	0.1528	0.0264	3.7702**	
2	0.1499	-0.0029	-1.7414	
3	0.1518	0.0019	1.1102	
4	0.1490	-0.0028	-1.6319	
5	0.1496	0.0005	0.4137	

* significant at 0.05 level (Exhibit 2-1)   ** significant at 0.01 level

Exhibit 2

ABNORMAL RETURNs (ARs) AND CUMULATIVE ABNORMAL RETURNs(CARs)
Foreign Group Classified by Country

Days	Avg. CARs	Avg. ARs	T-statistic	Significance
		1. United Kingdom(U.K.)		
-5	0.0256	0.0018	0.3780	
-4	0.0270	0.0013	0.3467	
-3	0.0391	0.0121	2.1177*	
-2	0.0661	0.0270	4.7640**	
-1	0.0791	0.0129	2.5912*	
0	0.1898	0.1107	5.6184**	
1	0.2519	0.0622	2.4292*	
2	0.2553	0.0033	0.9570	
3	0.2543	-0.0010	-0.1807	
4	0.2517	-0.0026	-0.6015	
5	0.2556	0.0039	1.0718	
		2. Canada		
-5	-0.0386	-0.0084	-1.6213	
-4	-0.0444	-0.0058	-0.8077	
-3	-0.0403	0.0041	0.4841	
-2	-0.0421	-0.0017	-0.3238	
-1	-0.0328	0.0092	1.0970	
0	0.2952	0.3280	2.6544*	
1	0.3015	0.0063	0.6496	
2	0.3004	0.0003	0.1670	
3	0.3251	0.0247	1.1076	
4	0.3306	0.0055	0.8311	
5	0.3395	0.0089	1.7581	
		3. Europe(excluding U.K.)		
-5	0.0446	0.0051	0.4795	
-4	0.0553	0.0107	0.7700	
-3	0.0585	0.0031	0.4717	
-2	0.0581	-0.0004	-0.0514	
-1	0.0539	-0.0042	-0.4972	
0	0.1400	0.0861	2.9689**	
1	0.1396	-0.0004	00.0375	
2	0.1392	-0.0004	-0.0629	
3	0.1400	0.0007	0.2117	
4	0.1417	0.0017	0.3859	
5	0.1439	0.0022	0.5849	

* significant at 0.05 level (Exhibit 2-2)   ** significant at 0.01 level

Exhibit 2

ABNORMAL RETURNs (ARs) AND CUMULATIVE ABNORMAL RETURNs(CARs)
#### Foreign Group Classified by Country

Days	Avg. CARs	Avg. ARs	T-statistic	Significance
		4. Asia & Ocenia		
-5	0.0236	0.0147	1.7682	
-4	0.0291	0.0055	0.4031	
-3	0.0311	0.0020	0.4133	
-2	0.0539	0.0228	1.5875	
-1	0.0613	0.0074	0.9125	
0	0.1349	0.0736	1.7512	
1	0.2245	0.0896	1.9731@	
2	0.2229	-0.0017	-0.2729	
3	0.2232	0.0003	0.0562	
4	0.2182	-0.0050	-0.7655	
5	0.2230	0.0048	0.5487	

@ significant at 0.10 level   (Exhibit 2-3)

Exhibit 3
CARs TO THE PORTFOLIOs OF THE TARGET FIRMs
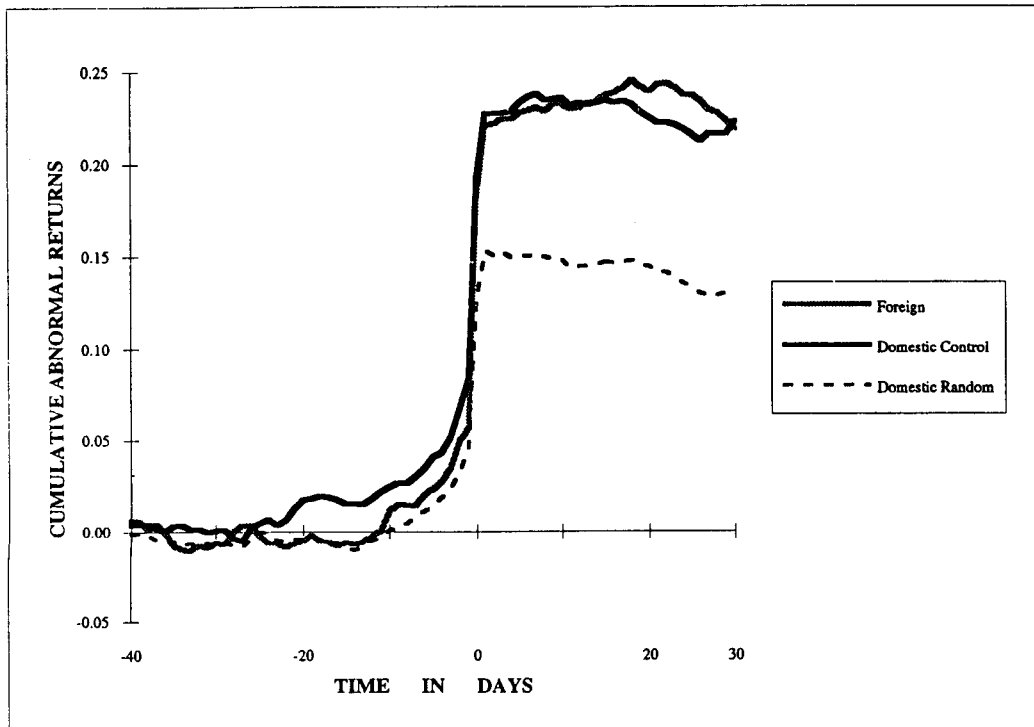
36, and 38) are identified as having at least a marginally sizable number of foreign-acquired targets. This suggests that the foreign acquisitions are concentrated in high-technology or R&D-intensive industries (Cebenoyan, Papaioannou, and Travlos [3] and Harris and Ravenscraft [9]).[18] It is important to note that none of the pairs of industries acquired by the foreign and domestic acquirers (e.g. chemical targets acquired by U.S.-based targets vs. chemical targets acquired by foreign acquirers) is statistically different in wealth effects. Regarding the announcement day results, while the CARs of the foreign-acquired targets are higher than those of domestic-acquired targets by 15.88% for SIC38 (to the contrary, they are lower : by 10.64% for SIC28), because of the high standard deviation, the difference is not statistically significant.[19] Thus, this study does not support Cebenoyan, Papaioannou, and Travlos' [3] argument that differential wealth gains between the foreign and domestic takeovers are directly related to the intensity of foreign acquisitions in the respective US. industries. The conflicts in the results may be due to miscontrol of the domestic-acquired targets and different aggregation of the industries.[20]

In sum, the above results confirm that the net benefits to the foreign acquirers of U.S. targets are not significant enough to justify a large premium to the targets. Furthermore, it is interesting to note that prior to the announcement date, the CARs associated with the domestic control group are slightly higher than those with the foreign group (see Exhibit 3). For example, 16 days prior to the takeover announcement, the difference of the CARs between the two is 2.6%, while the CARs of foreign groups start exceeding those of domestic control group 13 days after the announcement. Although the difference is not statistically significant in either period, this catch-up may well indicate that more information about the foreign acquisitions is revealed to the U.S. investors after the announcement. These results warrant a closer look at whether the foreign bidder is well informed about the target's value.

18) The sample sizes for SIC 28, 35, 36, and 38 are 9, 13, 10, and 9, respectively.

19) The CARs for the other two industries (SIC 35 and 36) are found to be almost identical.

20) Cebenoyan, Papaioannou, and Travlos [3] combine several two-digit SICs and divide them into three separate groups : the technology industrial sector, the seconary industrial sector, and the service sector. Due to the limited sample size, this level of aggregation is justified for significant results.

IV-2. Pre-Takeover Performance

In order to determine whether the foreign acquirer is informationally deficient in its acquisition of U.S. firms (as compared to its U.S. counterparts), we evaluate the past performance of the targets in foreign and domestic acquisitions. The results in Exhibit 4 show that foreign acquirers buy firms that are performing at least as well as their industry peer group and the domestic-acquired targets.[21] Indeed, based on the measures used, they buy even better performing companies than the U.S. bidders, but the point estimate difference is not statistically significant. In addition, the volatility of the target's value (VOLSTOCK) in a foreign takeover is about the same as that in a domestic takeover ($t=0.42$; $p=0.67$). These findings are consistent with Harris and Ravenscraft's [9] argument that foreign acquisitions are apt to occur when the acquirer has business expertise. In sum, it is unlikely that foreign acquirers are informationally deficient and thus pay more than domestic bidders for U.S. targets.

Martin and McConnell [22] suggest that a firm with good management tends to be the target of a non-disciplinary or synergistic takeover. Thus, the comparatively good pre-merger performance of the foreign-acquired targets indirectly supports Marr, Mohta, and Spivey's [21]view that foreign takeovers occur for strategic reasons; that is, the foreign acquirer attempts to gain a market entry into the U.S. and capture the accompanying synergistic gains. They find that the foreign acquirer improves the target by using its own management expertise and fresh capital, thereby generating substantial synergistic gains. In practice, foreign acquirers frequently cite market entry as one of the primary motivations for their acquisitions of U.S. firms (See Shaked, Michel, and McClain [31]).

Kacker [15] also finds that foreign acquisitions benefit retail firms by providing managerial and operating skills; and by doing so they help to stabilize the industry. In

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21) Although not shown here, the results on the target's performance relative to its industry are not straightforward. While the CUMIAJR measure indicates that the targets in either foreign or domestic takeovers perform than the industry average, the other measures that the targets are not diffirent from the average firm in their industry. These mixed results may be due to the insufficient data available for the other two measures, INCOME and FREE CF.

Exhibit 4
Summary Statistics and A Comparison of the Performance in Foreign and Domestic Takeovers

Sample of 100 foreign acquired targets (FATs) and 159 domestic acquired targets (DATs).
The performance measures are defined in the text (Section 3.3).

| Performance Measure	Mean		MeanDiff FAT-DAT	Ho:FAT=DAT* t-value/p-value	Median		MedDiff FAT-DAT	Standard Deviation	
	FAT	DAT			FAT	DAT		FAT	DAT
(1) INCOME	0.0632	-0.1240	0.1870	t=1.50/p=0.136	0.0250	-0.1210	0.1460	0.7750	0.7790
(2) FREECF	0.0159	-0.0493	0.0650	t=0.48/p=0.631	0.0040	-0.1230	0.1270	0.9930	0.6910
(3) CUMIAJR	0.1715	0.0885	0.0830	t=1.01/p=0.315	0.1370	0.0020	0.1350	0.6550	0.6340
(4) VOLSTOCK	0.0253	0.0247	0.0006	t=0.42/p=0.672	0.0240	0.0230	0.0010	0.0100	0.0100
(5) EXCHANGE	0.0415	-	-	Ho:Exchange=0** t=2.09/p=0.040	0.0330	-	-	0.1990	-

* The hypothesis tests whether foreign acquired targets are different from domestic acquired targets under each performance measure.
** The hypothesis tests whether foreign acquirer's home currency is stronger (or weaker, if negative) than the dollar.

▒ Statistically significant

(1) Growth of Income
(2) Growth of Free Cash Flow
(3) Cumulative Industry Adjusted Stock Returns for 3 years
(4) The Standard Deviation of the One-year Daily Stock Returns
(5) The Strength of the Foreign Buyer's Home Currency Relative to the Dollar

Exhibit 5
CARs TO THE PORTFOLIOs OF THE TARGET FIRMs BY COUNTRY
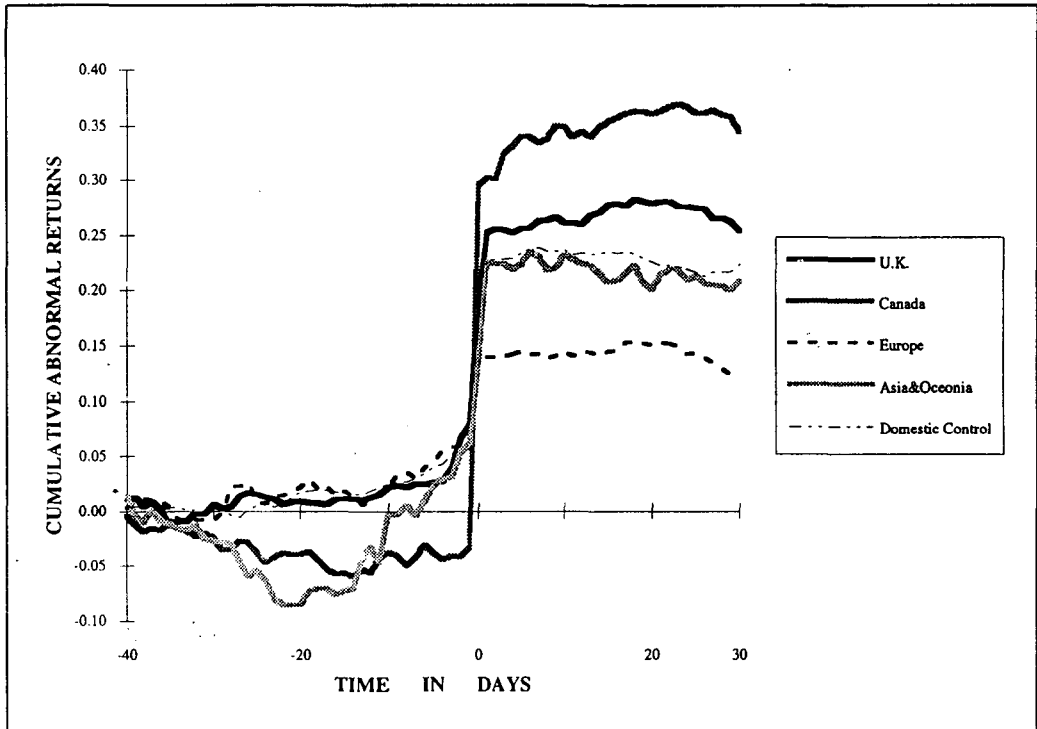
certain industries the expected synergistic gains may make it possible for foreign acquirers to afford larger premiums to target shareholders.[22] However, our study does not determine whether foreign acquisitions of U.S. firms generate more synergistic gains than comparable domestic acquisitions. At present, although the synergistic gain argument is plausible, it is untestable due to the lack of a worldwide database (including returns data for foreign firms). A thorough examination of this synergistic-gain hypothesis would require an evaluation of the abnormal returns received by shareholders of foreign acquirers.

IV-3. Country Analysis

Since the motivations for investing in the U.S. market may differ by country of origin, this study looks at the target wealth gains by the bidder's home country. Exhibit 5 shows the plots of the CARs by country group: United Kingdom (U.K.), Canada, Europe, Asia & Oceonia, and by domestic control group. The graph explicitly illustrates the country effect in foreign acquisitions. Specifically, the targets acquired by Canadian firms reap the highest CARs, while those by European firms earn the lowest CARs. However, due to the high variation among the target firms, the difference of the CARs between the two on the announcement day (29.52%-14%=15.52% ; Exhibit 2) is not statistically significant.

The high CARs earned by U.K.-acquired targets may square with the existing evidence (Harris and Ravenscraft [9]). Panel A of Exhibit 6 shows that at the time of the acquisition the U.K.'s currency is stronger than the dollar (4.48% ; $t=2.16, p=0.036$). As Froot and Stein [7] suggest, a favorable exchange rate may impart a purchasing advantage to U.K. acquirers. Hence, U.K. firms bid more aggressively than U.S. bidders for the target firms. In fact, the strength of the foreign buyer's home currency in the sample (4.15%, $t=2.09$, $p=0.04$; Exhibit 4) comes mainly from the U.K. In addition, Choi and Lee [4] argue that foreign acquirers, particularly from the U.K., can afford to pay more than U.S. acquirers. This is because the U.K. and other countries allow an

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22) Current literature does not resolve whether or not synergistic gains exist. For definitions and arguments regarding synergistic gains, see Bradley, Desai, and Kim [1].

Exhibit 6

COUNTRY ANALYSIS OF THE PERFORMANCE

Name of countries belong to Europe and Asia (& Oceonia) are listed at footnote#13 in the text.

PANEL A. Isforeign acquirer's currency stronger than the dollar? (Ho:Exchnage=0)

EXCHANGE	Asia	@Japan	U.K.	Europe	Canada
Mean	0.0910	-0.0605	0.0448	0.0231	0.0215
t-value	1.1400	-0.6417	2.1600	0.4900	0.7700
p-value	0.2780	0.5415	*0.036	0.6260	0.4590
sample size	13	8	45	30	12

@ Shows Japan separately from Asia & Oceonia.

COUNTRY DIFFERENCE	Ho:Country A=Country B

PANEL B Does volatility of the target differ by country?

VOLSTOCK

Asia	vs.	Europe	UK	Canada	Domestic	Control	Japan
0.0318	Mean	0.0246	0.0242	0.0237		0.0247	0.0335
	t-value	1.96	2.22	1.79		2.28	
	p-value	*0.056	*0.03	*0.087		*0.024	
13	sample size	30	45	12		159	8

PANEL C Does the pre-takeover performance of the target differ by country?
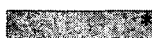
INCOME

Europe	vs.	U K	Asia	Canada	Domestic	Control
0.3036	Mean	-0.1051	-0.134	0.2025		-0.124
	t-value	-1.7	1.44	-0.33		2.26
	p-value	*0.097	0.163	0.741		*0.025
20	sample size	27	7	8		104

FREE CF

Europe	vs.	U.K.	Asia	Canada	Domestic	Control
0.3592	Mean	-0.0919	-0.5792	0.0813		-0.0493
	t-value	-1.59	2.39	-0.72		2.35
	p-value	0.118	*0.023	0.476		*0.020
23	sample size	29	9	9		113

	Asia	vs.	Canada	Domestic	Control
		t-value	-1.75		-2.18
		p-value	*0.100		*0.031

CUMIAJR

Europe	vs.	U.K.	Asia	Canada	Domestic	Control	Japan
0.2402	Mean	0.1736	-0.1524	0.3430		0.0885	-0.1699
	t-value	-0.47	-1.84	0.43		1.21	
	p-value	0.638	0.094	0.673		0.230	
30	sample size	45	13	12		159	8

Asia	vs.	U.K.	Canada	Domestic	Control
	t-value	-1.71	-1.56		-1.31
	p-value	0.093	0.133		0.193

▓▓▓▓ Statistically significant

immediate write-off of purchased goodwill against reserves. This write-off then results in higher reported earnings.

Interestingly, non-U.K. European acquirers are found to pay the least for the U.S. target shareholders, and buy targets which performed the best. Moreover, as Exhibit 6 shows, Asia & Oceonia acquirers (and Japan in particular) appear to buy the most volatile and the worst performing companies.[23] Volatility of the target's value (VOLSTOCK) and cumulative industry adjusted return (CUMIAJR) of Japan-acquired targets are 3.35% and -16.99%, while those of Europe-acquired targets are 2.46% and 24.02%, respectively.

The poor performance of the targets acquired by Japan is reflected in the negative CARs prior to the announcement day (see Exhibit 5). For example, on day -23, the ARs and CARs are -8.01% and -1.59%, respectively, and are statistically significant. As the information about the acquisition is revealed to capital markets over time, the Japan-acquired targets realize positive gains. Specifically, on the announcement day they reap the benefits of the CARs (18.40%) as much as do the U.K.-acquired targets. However, the high premiums that Japanese firms paid for U.S. targets do not seem to be a result of favorable exchange rates at the time of acquisition (-6.05%, $t=-0.64$, $p=0.54$; Panel A

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23) "Asia & Oceonia" (13) consists mostly of Japan(8) (See footnote 13).

of Exhibit 6). In sum, the results show that European companies pay the lowest price for U.S. firms with good pre-takeover performance. At the same time, Japanese companies pay a considerable price for U.S. targets with management that have done poorly before the takeover.

V. SUMMARY AND CONCLUSIONS

This study presents evidence which is consistent with the main prediction of the competitive acquisition market hypothesis. That is, the wealth gains generated in foreign takeovers are not different from those in domestic takeovers. The argument that premiums to target shareholders are larger in foreign than in domestic takeovers is refuted because neither the net-benefit hypothesis nor the information-deficiency hypothesis is supported. The findings show that 1) in cases of inward foreign direct investment into the U.S., foreign firms do not realize significant net benefits from acquisitions ; and 2) the foreign acquirer is as well informed as its U.S. counterparts about the target's market.

For meaningful comparison of the wealth gains in cross-border acquisitions with those in domestic takeovers, the to-be-compared domestic targets should be controlled appropriately with respect to the characteristics of foreign-acquired targets, such as industry, method of payment, time, industrial relatedness, and exchange listings. After appropriate control, the analysis shows that as a result of foreign acquisition announcements, target shareholders do not receive higher returns than they receive from similar domestic takeover announcements.

The results indicate that foreign acquirers buy U.S. firms with relatively good management which have done well compared to industry averages and also compared to the targets acquired by U.S. acquirers. This lends some support to the synergistic-gain hypothesis that foreign takeovers occur for strategic reasons ; that is, to gain a market entry into the U.S. and capture the resultant synergistic gains. However, this study cannot determine whether foreign takeovers entail greater synergistic gains than

domestic acquisitions.

Furthermore, the results of the country analysis reveal that European acquirers purchase at the lowest cost those U.S. firms with particularly good pre-takeover performance. This may indicate that the typical agency costs involved with acquisitions in general, and foreign acquisitions in particular, are of less concern to European than to U.S. or U.K. firms. Since European firm's ownership is less diffused, or often privately structured, the self-interested managers with their own money tend to buy better performing companies at lower cost than U.S. or U.K. managers in more diffused corporate environment.

In addition, Japanese companies pay a considerable premium to acquire U.S. targets which have performed relatively poorly prior to the takeover. The fact that the financial "Keiretsu" provides Japan with its comparatively low cost of capital, may make Japan more willing to pay a higher price. However, the reason why Japanese firms buy the most volatile and worst performing firms is unclear. International barriers may explain these anomalies. The acquirers may use the acquisition as a means to overcome trade barriers. The desire to enter the U.S. market to secure a foothold before any import trade barriers are imposed may incentivize them to pay considerable premiums for the firms with less favorable attributes.

Thus, future research should be directed to evaluate the synergistic gains in foreign and domestic corporate acquisitions and to determine the division of the synergistic wealth gains between the shareholders of U.S. targets and foreign acquiring firms. Overall, the evidence of this paper supports the view that foreign takeovers occur in a competitive acquisition market.

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