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REPORT OF THE EXPERT MEETING ON MERGERS AND ACQUISITIONS: POLICIES AIMED AT MAXIMIZING THE POSITIVE AND MINIMIZING THE POSSIBLE NEGATIVE IMPACT OF INTERNATIONAL INVESTMENT

Held at the Palais des Nations, Geneva,
from 19 to 21 October 2000

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I. OUTCOME OF THE EXPERT MEETING

1. The Expert Meeting on Mergers and Acquisitions: Policies Aimed at Maximizing the Positive and Minimizing the Possible Negative Impact of International Investment discussed a range of issues for consideration by the Commission on Investment, Technology and Related Financial Issues.

Trends, motivations and performance of M&As

2. Cross-border M&As have increased significantly in developed countries and are now also becoming important in developing countries and transition economies. They involve a broad spectrum of sectors and companies, large firms as well as SMEs, in developed and developing countries. Cross-border M&As are likely to continue to grow. A global market for firms is emerging.

3. Factors motivating M&As include the search for efficiency and synergies, access to markets, market power and strategic assets (including, among other things, a labour force with certain types of skills, specific technology or brands). But, above all, M&As are driven by the desire to move quickly, under pressures from markets to grow and enhance competitiveness. Changes in the global environment (liberalization in trade, finance and investment, as well as technological changes) have created a situation that facilitates cross-border M&As. It is the interaction between these two sets of forces - motivating factors at the firm level and macro-economic changes - that helps to explain the recent wave in cross-border M&As and is likely to sustain their growth in the future.

4. Despite a high perceived rate of failures in terms of increased shareholders' value and financial returns, M&As can bring other benefits for a company, such as an improved long-term strategic position important for its survival. Factors that contribute to the success of M&As include a proper integration of the human resources and mutual economic benefits for the firms involved.

Impact on host-country development

5. The following possible positive effects were mentioned: immediate capital inflows; immediate or follow-up new investment and resulting job creation; job conservation as acquired ailing firms are rescued or acquired firms are able to grow; immediate transfer of technology, especially information technology, and of managerial and other skills, leading to improved competitiveness; transfer of marketing skills; improvement of corporate governance; access to, and integration with, global markets and increased exports; restructuring of firms and industries; longer-term industry development perspective; greater efficiency and productivity and improved quality of services; and increased tax and privatization revenues.

6. The following possible challenges were identified: immediate reduction of employment; increase of concentration; less competition; no addition to the capital stock at the time of entry; possible low pricing of sold assets due, for example, to a lack of expertise; shrinking of domestic stock markets; crowding out of local enterprises, especially SMEs; loss

of indigenous brands; cost of arbitration; and increase in the foreign control of a host country's economy, of special concern in sectors considered of strategic importance for the country.

7. The economic policy framework and the country's level of development are key. Other factors affecting the impact are: whether a short or long-term perspective is taken to evaluate effects; the normal or exceptional circumstances (such as privatization programmes or financial crises) in which cross-border M&As take place; motivation of the investor (e.g. market seeking vs. efficiency seeking); the situation of the acquired enterprise; and the availability of alternatives as regards modes of entry of investment.

Policy considerations

General issues

8. As increased investment is not an end in itself, some countries have found that the positive impact depends, among other things, on having the right economic policies, the right level of government activity, the regulatory framework and a competition policy.

9. Some Governments do not have specific policies concerning cross-border M&As.

10. Policy responses for cross-border M&As among SMEs and among large firms may be different. Some Governments encourage cross-border M&As among SMEs to facilitate their access to foreign finance and improve their competitiveness.

11. In privatization, some countries have maintained "golden shares" and have sought commitments from strategic foreign investors on further investment. When such commitments are made, there is often a trade-off between the up-front price of assets to be sold and these commitments.

12. Some countries have restructured their public sector as an alternative to privatization.

13. Some Governments have in place measures to deal with the problem of lay-offs, such as the training and retraining of workers laid off. Some countries have found it useful, because (among other things) of these employment effects, to emphasize a balanced development of the domestic and foreign enterprise sector.

14. Some countries seek to establish corporate governance rules.

15. In the case of privatization and sales under exceptional circumstances, some countries have found that the price of assets is important but not the only consideration. In the case of sudden sales under such circumstances (including involving cross-border M&As), e.g. in an economic crisis, some countries have found it difficult to determine the right prices. A clear long- term developmental perspective was found helpful in this respect.

Competition policy

16. In the light of the rise of cross-border M&As, a number of countries pay increasing attention to the importance of competition laws and cooperation between competition authorities. They have found that policies aimed at maintaining the contestability of markets and the dissemination of the culture of competition complements the adoption and implementation of competition laws. They also found that special attention to the relevant market definitions, market performance and market structure is warranted.

17. Some countries integrate competition policy with other public interests and concerns and ensure policy co-ordination between competition authorities and regulatory bodies of specific industries, especially in industries that are monopolies.

18. Apart from national merger reviews, international co-operation might be useful, especially at the regional level. For example, as merger control is costly, cooperation at the regional level has been found useful by some. An exchange of information between countries affected by M&As has also been found useful by some countries. Another form of cooperation involves joint review mechanisms. Standardization of time limits was also mentioned.

19. When reviewing cross-border M&As, countries in a position to do so could make information relevant to developing countries available to them.

20. Some countries rely on donor partners for technical assistance to develop their laws and regulatory frameworks in this area.

Issues for further research

21. A number of issues were identified that could be considered for further research. In particular, research would be desirable concerning investment subsequent to entry, policy implications for development at the international level, and the impact of various types of cross-border M&As on market structure and key areas of economic development. Inputs from the World Association of Investment Promotion Agencies (WAIPA) and other competent organizations could be useful here.

II. CHAIRPERSON'S SUMMARY

22. The Expert Meeting on Mergers and Acquisitions was attended by more than 100 participants from 50 member States, UN agencies, and other intergovernmental and non-governmental organizations. Experts exchanged views on the following issues: trends, motivations, strategies and performance of cross-border mergers and acquisitions (M&As); and the impact of cross-border M&As on host country development and policy implications.

23. The question of cross-border mergers and acquisitions was being discussed for the first time in UNCTAD, and the purpose of the Meeting was to deepen the understanding of the subject on the part of business and governmental actors, especially as mergers and acquisitions are a rather new phenomenon in many countries and are assuming increasing importance.

A. Trends, motivations, strategies and performance of cross-border M&As

Motivations

24. Experts from the business sector dealing with cross-border M&As stressed that the main driving motivations behind cross-border M&As relate to the need to grow on global markets and to act quickly. Under competitive pressures, speed is a determining factor: between buying or building, buying is generally preferred, as it allows rapid market penetration. As one speaker observed: "Speed is our friend, time is our enemy". The number of M&As increased by 43 per cent a year during the period 1995-1999, and this trend is expected to continue in the future.

25. Cross-border M&As will become a crucial element in the growth strategy of firms, whether they are large or small and medium-sized enterprises (SMEs). For large TNCs, a key motivation for cross-border M&As in all countries is market consolidation. Global TNC growth cannot be sustained without M&As, especially in such sectors as telecommunications, energy and electricity. Motivations for M&As cited by the representative of a major TNC include: entering new business lines and innovation; strengthening presence in markets with long-term potential; and shortening the time required to secure a market position. The main reasons for cross-border M&As involving SMEs are related to gaining access to foreign markets and global production networks, reducing costs, improving management practices, restructuring and enhancing competitiveness. In the case of a company from a developing country acquiring another company in a developed country, the main motivation is the acquisition of a global brand name and access to the global market place.

26. Motivations of enterprises vary according to sectors. In some sectors M&As allow firms to reach a critical size which will allow them to compete and grow. In others, M&As allow firms to be vertically integrated, thus bringing more value added and new technologies. Enterprises could also use M&As to acquire skills and creative assets in local economies, without having to expatriate personnel out of their national environment.

27. In Japan, there has traditionally been a preference for greenfield investments, both for inward and outward FDI. Today the attitude towards M&As within the public and private sector has changed. The late 1990s also saw a rapid increase in the inflow of cross-border M&As. The main reasons are that M&As provide a faster route to acquiring firm-specific competitive assets and skills abroad. The benefits of inward cross-border M&As include the inflow of management techniques.

28. The factors driving M&As – cross-border and domestic – in developing countries are similar to those in developed countries, and they include the globalization of consumer markets, increased competition at the global level, rising costs of R&D and transfer of technology, changes in the financial markets and the development of modern ownership structures, and privatization. Cross-border M&As in developing countries have become important and bring advantages as well as challenges. Once TNCs have entered markets through M&As, new greenfield projects have often followed. It is noted, however, that M&As have resulted in the downsizing of domestic capital markets, as the shares of the acquired companies are delisted from local stock markets to be listed on the stock markets of parent companies.

Performance

29. There is no precise and agreed yardstick to measure the success or failure of M&As. Nevertheless, despite an apparently high rate of failure, as measured in terms of shareholder value, firms often enter into M&As because the market place expects them to grow through mergers and for strategic reasons. Synergy is a critical factor in the success of an M&A, as it allows firms to build reputation, to buy power and to enhance revenue. Behind the merging firms are people, and therefore the synergy between the firms' cultures should persist. One speaker pointed out that successful M&As combine four elements: there must be a long-term strategic fit – opportunistic M&As do not work; there should be a minimum overlap between companies in terms of product or personnel, as this facilitates integration; the culture of the two companies should not clash; and it must make economic sense to both buyer and target companies (a win-win situation).

30. Another expert added that the conditions for success concern the experience of the companies involved, the additional investments required to upgrade the technological capacity of acquired companies, and the motivation in terms of training and integrating employees. Size and growth should not be ends by themselves. Transfer of technology and human development are continuous processes, and, in this respect, there is no difference between cross-border M&As and greenfield FDI.

Policy issues

31. It was mentioned that rules and regulations need to be adapted to the new globalized context and should not be a deterrent to cross-border M&As. For example, it was pointed out that some regulations in the United States make it difficult for US companies to go public in other countries.

32. A precise and secure legal framework appears to be a prerequisite for successful M&As. Some experts mentioned that it is more important to regulate the behaviour of

enterprises than to put a limit on foreign ownership of capital. Views diverged concerning national sovereignty, as experts from developed countries asserted that, with the exception of activities related to national defense or activities that could endanger public health, restrictions on foreign ownership are not justified.

33. Governments need to harmonize their rules and regulations. The various tax regimes applying to stock options were mentioned as an example.

34. There was general agreement that competition policy becomes more important as a result of the increase in M&A activity. Factors discussed include how to define the relevant market and how to improve merger control without creating additional regulatory barriers at high cost.

35. There is a need to distinguish between mega-mergers and “normal” acquisitions. These two different types of M&As may call for different policy responses. There is also a need to pay more attention to how cross-border M&As affect SMEs. Areas which may deserve special attention are financing, access to markets and competition.

Outlook.

36. Panelists from the business sector agreed that there will be an increase and acceleration in M&As in the new economy. There will be a wave of mergers, demergers and then mergers again as companies adapt to the new environment. Before, companies used to think in terms of a five-year time period from planning to action. Now plan and action are becoming one: “plaction”. The implication is that cross-border M&As will become more important in the future, and developing countries need to have in place appropriate policies to deal with them. There should be a synergy between the interests of companies and host countries.

B. Impact of cross-border M&As on host country development and policy options

37. Several experts from developing countries presented their countries’ experiences regarding the impact of cross-border M&As.

38. Experts recognized that cross-border mergers and acquisitions are not simply a transfer of ownership, but could have a positive impact on the host economy, notably on:

- Local industrial structure, through transfer of managerial skills and new technologies (e.g. cross-border M&As are a way to circumvent stringent intellectual property right regimes), addition to productive capacity resulting from additional sequential investment, the possibility of integrating quickly into global production networks and to access global markets, improved productivity and profitability of acquired firms, and inducing the adoption of a long-term vision and strategy by the Government;
- Available resources, through increases in government revenues, additional investments and increases in exports;

- Market organization, through the formation of lobbies to negotiate with creditors and suppression of local anti-competitive groupings.

39. In a few countries, especially those of Central and Eastern Europe, privatization has been the main form of cross-border M&As. In general, at the firm level, they have led to improved productivity, profitability and better services to consumers. Some experts noted that privatization deals often include additional future investment commitments by foreign investors. One expert mentioned a survey conducted on the impact of foreign acquisitions through privatizations in countries with economies in transition. This survey indicated that additional investment and restructuring, as well as expansion of capacities, have followed acquisitions in the majority of cases. The expert added that FDI policy should focus on the creation of new productive capacities, regardless of the mode of entry. Foreign acquisitions through mass privatizations can help in the restructuring of existing firms.

40. On the negative side, experts raised a number of concerns. Cross-border M&As do not in principle add to existing capital stock, but represent only a change in ownership. It was also noted that technology transfer has taken place more frequently in the case of greenfield FDI than in the case of cross-border M&As, at least in Latin America. Cross-border M&As can also weaken the domestic production base if well run local firms are taken over with the intention of eliminating competitors and if there is loss of jobs because of restructuring. In some countries, there has also been a loss of indigenous brands, loss of jobs and industrial concentration as local competitors, in particular SMEs, are driven out of the markets, as a result, for example, of predatory pricing practices by TNCs. Anti-competitive behaviour by foreign firms can be a serious concern, especially in the absence of a strong regulatory framework for competition in host countries. In addition, in some industries (e.g. water supply), there are few international players operating, and this leads to more concentration after privatization.

41. Furthermore, in the case of privatizations, resources obtained by Governments can be misused. It has been noted that two types of measures could be taken in order to mitigate the negative effects of privatizations:

- A government policy to determine clearly the beneficiaries or the use of the revenue accruing from privatizations (as in the case of the capitalization programme in Bolivia);
- A commitment to bring additional investments as part of a privatization bid by a foreign enterprise (as in the case of Peru).

42. The representative of an international trade union organization expressed concern that, beyond their economic impact, cross-border M&As also have a social dimension. The interests of stakeholders, besides shareholders and including workers, suppliers, consumers and Governments, should be taken into account. The consequences of globalization are felt by workers through loss of jobs, downward pressure on wages, and worsening of working conditions. Competition policy is too narrow in scope, because it addresses the concerns of competitors only. Policy responses should be based on a better understanding of the impact of trade and investment liberalization on the workforce and local communities, and it should

strengthen corporate governance, take into account the interests of local stakeholders, build local capacities and companies, and empower workers and unions.

43. Some experts commented on the effect of outward cross-border M&As on developed countries. For these countries there could be costs in terms of loss of employment and loss of competitiveness, if high-technology firms are transferring their facilities to other countries.

44. A question was raised as to whether domestic M&As should be encouraged rather than cross-border M&As, most particularly in sensitive sectors such as banking and other financial industries.

45. Measures to address the negative impact of cross-border M&As were discussed. It was recognized that Governments need to invest in education and improve the investment regime, as well as corporate governance rules. Concerns need to be taken up within a broader framework: regulatory bodies need to be set up first. Strategic considerations in allowing M&As require regulation of behaviour instead of restrictions on ownership share structures. In the case of least developed countries, the challenge of dealing with cross-border M&As is compounded by the need to improve or to put in place the general regulatory framework. A number of these countries do not have a competition law or any regulatory body to oversee industry regulation. There is a lack of well trained technical staff or lawyers, and financial services are often inadequate. There is an obvious need for technical assistance in these countries.

46. On employment effects, some experts noted that, in some cases, layoffs are inevitable if the target company was run inefficiently. It was also noted that M&As can lead to increased employment in the long run. The need for policies to deal with massive layoffs was stressed. Some experts pointed out that political economy cannot ignore short-term unemployment problems, even if these are acceptable under economic theory. There is obviously a need to retrain unemployed workers, especially where there is a huge skill gap, to help them move from one industry to another. Mention was made of the possibility of setting up a special fund for this purpose, with contributions from foreign investors.

47. On the question of technology transfer, it was pointed out that technological spillovers will not take place in the case of M&As undertaken in order to eliminate a competitor. These spillovers tend to be more important in the case of greenfield FDI than in the case of M&As. At the same time, it was also recognized that linkages with local firms might be stronger in the case of M&As, as there is access to an established set of linkages.

48. The effects of cross-border M&As that take place under special circumstances, such as economic/financial crisis or privatization programmes, raised particular concerns. Thus, during a financial crisis, unless new finance can be obtained, there are few options left to firms having liquidity problems and their Governments but to sell at “fire sale” prices. Otherwise, the firms will face bankruptcy. It is important for Governments to have a clear set of priorities when intervening in cases of M&As in situations of distress and to consider all alternatives available. Technical capacities have to be strengthened, for example in classifying and valuing well-performing and non-performing assets in a distressed bank. Also important is the timing of the selling process, in order to avoid selling many companies in the same industry at the same time, so that bidders do not pick and choose the best deals and

drive the prices of others down. The need to set clear priorities also applies in the case of privatizations. The involvement of strategic foreign investors has been motivated in most cases by the need to obtain foreign capital, restructure the company, increase competitiveness and improve the services to consumers. The price of assets in privatization is important but is not the main priority in most cases. More important is the quality and reliability of the buyer and offer. It is important to introduce a competitive bidding process open to as many bidders as possible that meet certain basic requirements. Governments need to develop expertise and experience in negotiating techniques to match the strength of TNCs.

49. Apart from the economic impact of cross-border M&As, there is a shared concern among developing countries about the erosion of the national enterprise sector and consequently of the economic sovereignty of the host country. It was generally felt that precautionary devices could be put in place to avoid sensitive areas of the economy falling exclusively into foreign hands. The question was raised as to whether there should be restrictions on foreign ownership in the banking sector, for example. There is also the question of relocation of the decision-making centre of the acquired company to a foreign country. There is often a trade-off between the need for domestic companies to protect themselves against undesirable foreign acquisitions of ownership and control, and the need to allow markets for ownership and control to function efficiently.

50. The role of competition policy was given special emphasis. There was general recognition that the effects of cross-border M&As on competition deserve special attention by policy makers. Governments need to have national competition laws in place to deal with these effects and to disseminate a culture of competition. Such a culture is now embedded in many countries, e.g. in Latin American countries. At the same time, competition policy needs to be better integrated with other policies. Control of cross-border M&As goes beyond traditional competition policy concepts and needs to take into account the contestability of markets. Policy-induced market distortions can be as important as private anti-competitive behaviour.

51. It was also felt that it is becoming increasingly difficult for local authorities to assess the effects of global deals on local markets. This raises the question as to the extent to which domestic regulation can address these effects. A related challenge is how to determine the relevant market in products and industries characterized by constant innovation. Some experts noted that there is often a tension in competition policy analysis between the effects of M&As on the present market structure and the process of innovation and “constructive destruction” that is occurring in certain high-technology product markets. Thus, competition policy should not be so rigid as to prevent the creative process of cross-border M&As. In this respect, some experts mentioned that the real issue for developing countries is to focus not so much on competition but rather on the regulation of individual industries to allow them to reach appropriate concentration levels to function efficiently. Regulation should be based on sound national development strategies. Policy priorities may involve modernization, technological upgrading, etc. (for example, regulation in the telecommunications sector based on these priorities may contradict competition policy principles).

52. Some comments were made on the need to address the challenges posed by cross-border M&As at the level of implementation of competition policy. Several measures were suggested. For example, strengthening cooperation among competition authorities of

countries concerned by some cases of M&As in order to exchange information and foster consultations; joint investigations or work sharing arrangements in cases where the enforcement efforts of one agency could be used to help M&A review in other jurisdictions. Standardization of review periods and other procedures could also facilitate reviews when several jurisdictions are involved. Another suggestion related to the creation of informal observatory mechanisms at the regional level to study cross-border M&As and improve present methodologies. These mechanisms could reduce the cost of monitoring by national authorities.

53. Experts also requested UNCTAD to undertake research on the impact of M&As, notably on the contribution of cross-border M&As among SMEs in enhancing their productive capacity in increasingly globalized markets.

III. ORGANIZATIONAL MATTERS

A. Convening of the Expert Meeting

54. The Expert Meeting on Mergers and Acquisitions: Policies aimed at Maximizing the Positive and Minimizing the Possible Negative Impact of International Investment was held at the Palais des Nations, Geneva, from 19 to 21 June 2000. The Meeting was opened on 19 June 2000 by Mr. Karl Sauvant, Officer-in-Charge of the Division on Investment, Technology and Enterprise Development.

B. Election of officers
(Agenda item 1)

55. At its opening meeting, the Expert Meeting elected the following officers to serve on its Bureau:

Chairperson:	Mr. Gesner Oliveira (Brazil)
Vice-Chairperson-*cum*-Rapporteur:	Mr. Jean-Luc Le Bideau (France)

C. Adoption of the agenda
(Agenda item 2)

56. At the same meeting, the Expert Meeting adopted the provisional agenda circulated in TD/B/COM.2/EM.7/1. Accordingly, the agenda for the Meeting was as follows:

1. Election of officers
2. Adoption of the agenda
3. Mergers and acquisitions: policies aimed at maximizing the positive and minimizing the possible negative impact of international investment
4. Adoption of the outcome of the Meeting

D. Documentation
(Agenda item 3)

57. For its consideration of the substantive agenda item (item 3), the Expert Meeting had before it a note by the UNCTAD secretariat entitled “Impact of cross-border mergers and acquisitions on development and policy issues for consideration”(TD/B/COM.1/EM.7/2).

E. Adoption of the outcome of the Meeting
(Agenda item 4)

58. At its closing meeting, on 21 June 2000, the Expert Meeting adopted the outcome reproduced in section I above, and authorized the Chairperson to prepare a summary of the Meeting (see section II above).

Annex

ATTENDANCE

1. The following States members of UNCTAD, members of the Board, were represented at the session:

Algeria
Australia
Bangladesh
Bolivia
Brazil
Burundi
Canada
China
Costa Rica
Cuba
Dominican Republic
Ecuador
Ethiopia
Finland
France
Germany
Guinea
India
Iran (Islamic Republic of)
Italy
Jamaica
Japan
Jordan
Mexico
Morocco
Pakistan
Peru
Philippines
Republic of Korea
Russian Federation
Saudi Arabia
Slovenia
South Africa
Sri Lanka
Switzerland
Thailand
Trinidad and Tobago
Uganda
United Kingdom of Great Britain and Northern Ireland
United Republic of Tanzania
United States of America
Uruguay
Venezuela
Viet Nam
Zambia

2. The following intergovernmental organizations were represented at the session:

Arab Labour Organization
European Bank for Reconstruction and Development [1]
European Community
Organization for Economic Co-operation and Development
Organization of the Islamic Conference
South Centre

3. The following specialized agencies and related organization were represented at the session:

International Labour Organization
United Nations Industrial Development Organization
World Trade Organization

1 Specially invited

4. The Economic Commission for Europe and the Economic Commission for Latin America and the Caribbean were represented at the session.

5. The following non-governmental organizations were represented at the session:

General category

ActionAid
Engineers of the World
International Confederation of Free Trade Unions
International South Group Network
Public Services International
Third World Network
World Federation of United Nations Associations
World Wide Fund for Nature International

Special category

Jubilee 2000 Coalition

Special invitee

Mr. Arvind Mayaram, Chairman, Rajastan Bureau of Industrial Promotion, India, Vice-President of WAIPA

Panellists

Mr. Joseph B. Castello, Chairperson and CEO, think3, Santa Clara, California
Mr. John Kelly, Partner, Head of M and A Integration Team, KPMG, London
Mr. R.K. Krishna Kumar, Vice-Chairperson, Teta Tea Limited, Bombay
Mr. Herbert Oberhänsli, Nestle, Economic and International Relations
Mr. Reynaldo Passanezi, Deputy Director, Corporate Finance Unit, Banco Bilbao Vizcaya Argentina, (BBVA) S.A., Sao Paolo