

Government Effectiveness, Institutional Distance, and Equity Ownership in Cross-Border Acquisitions by Emerging Economies: A Comparative Analysis

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ABSTRACT

Our study enhances comprehension regarding the motivations behind cross-border acquisitions (CBMA) by Emerging Market Multinationals (EMNEs). This research explores the impact of both formal and informal institutional distance on equity ownership in emerging markets. Additionally, we posit that these direct correlations are more pronounced for EMNEs compared to Multinational Enterprises (MNEs). To validate these hypotheses, we compare the CBMA of firms based in developing countries with those in developed countries. Motivated by the need to better understand a prominent group of foreign acquirers, we examine acquisitions initiated by EMNEs over a 12-year period. We observe that acquirers from developing countries tend to hold greater equity share in targets located in more economically advanced nations, sharing cultural proximity. Our study's empirical findings highlight the differential impact of economic distance on the equity share sought by acquirers based in emerging markets, contingent upon the level of government efficiency. Specifically, we note that this relationship shifts from a linear correlation in instances of low government efficiency to a curvilinear association in situations of high government efficiency. While the cultural distance seems to have a greater adverse effect on the degree of ownership taken in acquisitions for EMNEs compared to Emerging Market Multinationals (DMNEs). It lends support to the position that the context of institutions, and institutional theory, matter.

Keywords Cross-border acquisitions, Emerging market multinationals, Equity participation, Institutional distance, government effectiveness.

INTRODUCTION

In the last two decades, both the frequency and intensity of mergers and acquisitions (M&A) transactions have increased, resulting in increased research on the antecedents, moderating factors and consequences of these decisions (Shimizu et al. 2004; Halebian et al. 2009; Liou, Chao, et Yang 2016). Industry consolidation, privatization, and liberalization of the global economy have all contributed to the growth of cross-border acquisitions (Shimizu et al., 2004). However, most existing studies have focussed on cross-border acquisitions of companies located in developed economies. The announcement of cross-border M&A activities by multinationals from emerging economies has recently been seen a rapid increase in line with the fast-paced development of the global economy. While the acquisition policy, particularly in emerging markets, holds significant importance, it is crucial to gain a better understanding of how emerging markets encourage this form of internationalization. Additionally, it is important to examine whether the acquisition

policies of companies located in emerging countries differ from those of companies in developed countries.

Aside from the inherent implementation and integration difficulties, CBMA poses further quandaries as institutional distance reduces the comparability of disparate operational landscape (Kostova 1999; Xu and Shenkar 2002; Shimizu et al. 2004). Institutional distances between the acquirer's home country and that of the target company complicate the acquisition process, thereby reducing the likelihood of successful integration (Kostova 1999). Consequently, institutional factors may exert distinct influences on the internationalization environment of emerging firms (Peng, Wang, and Jiang 2008; Peng et al. 2009).

Several recent studies have explored the impact of institutional distance on the degree of equity ownership in cross-border acquisitions (Malhotra, Sivakumar, et Zhu 2011a; Morschett, Schramm-Klein, et Swoboda 2010; Liou, Chao, et Yang 2016; Gaffney, Karst, et Clampit 2016; Gaur, Malhotra, and Zhu 2022). The level of equity share in acquisitions exerts a profound impact on various aspects of corporate strategy, including corporate governance, the ability to transfer tacit assets, and risk exposure (Chari and Chang 2009; Das and Teng 2000). This becomes particularly pertinent when analyzing EMNCs, as the propensity to innovate, risk-taking, proactive, and competitiveness relative to their developed country counterparts, drives them to acquire strategic assets or advantages such as technology or branding via internationalization (Chen 2011; Hope, Thomas, and Vyas 2011; Luo and Tung 2007; Madhok and Keyhani 2012). For the purpose of this study, we argue that EMNCs will pursue higher degree of equity ownership in acquisitions of target located in economically developed countries with cultural proximity. We further identify the association between the institutional distance and ownership level in order to mitigate the institutional uncertainty and the potential moderating effect of Government effectiveness level (GE) on the distance-ownership nexus. Generally, institutional differences between countries heighten the complexity of the acquisition process and render acquirers more risk-averse. Prior EMNC internationalization studies have often focussed on the assumption that EMNCs differ from DMNCs with respect to economic scale, development path, and institutional background. As such, it is vital to scrutinize the role of institutional distance in ownership participation depending on MNC classification and ascertain whether this divergence is justified.

LITERATURE REVIEW

The number and value of cross-border acquisitions have increased, and they make up around 38% of all acquisitions, the highest share since 2008 (Thomson Reuters, 2016). In contrast to traditional internationalization theories, this increase in acquisitions from emerging markets reflects the growing significance of internationalization, which is characterized by a relatively more aggressive approach (Aybar and Ficici 2009; Gubbi et al. 2010; Hope, Thomas, and Vyas 2011; Luo and Tung 2007). Furthermore, 2017 saw a notable rebound in developing economies, propelled by a noteworthy rise in cross-border Chinese acquisitions and the strong economic growth of exporters of natural resources (UNCTAD 2017).

In contrast to the specific factors that developed multinationals rely on, EMNCs differ significantly from developed market multinationals because of their latecomer status and particular benefits from their country of origin, such as preferential access to labor, capital, or government policies at lower costs (Rugman 2010). Emerging companies, as they are low-cost enterprises, continuously learning and improving their skills and knowledge to create distinctive advantages that help them stay competitive in the global market (Kedia, Gaffney, and Clampit 2012). Furthermore, EMNCs frequently expand internationally in order to obtain vital resources required to successfully compete in both domestic and foreign markets and get beyond institutional and trade barriers in their home markets (Luo and Tung 2007). EMNCs attempt to surmount their competitive disadvantages by means of bold, proactive, and high-risk acquisitions in order to attain firm expansion and a competitive stance in the worldwide marketplace. Additionally, they are driven to internationalize in order to overcome competitive disadvantages around the globe, acquire key assets like technology and R&D, and promote and boost social and economic growth in their home nations (Gaffney,

Kedia, and Clampit 2013). In developing and transitional nations, mergers and acquisitions (M&A) have grown significantly, with cross-border mergers and acquisitions (CBMA) value rising at an astounding rate of 23.47%. The industrialized countries had a particularly noticeable trend, with a growth rate of 25.12%, whilst the developing and transitional countries recorded growth rates of 24.91% and 81.04%, respectively. Given that developed market asset valuations remain lower, the financial crisis has accelerated the internalization of emerging market enterprises. Nevertheless, considering the state of the world economy right now, this recovery pattern is not particularly encouraging. The implementation of systematic economic policies, an explicit monetary system, and an efficient financial market are essential to sustaining this recovery (Reddy 2015).

The factors encouraging the international expansion of EMNCs have changed significantly in recent years. Acquiring crucial assets, like as resources and market information, is becoming more and more important, and knowledge-driven projects are receiving more attention. Emerging businesses are aggressively seeking strategic assets to strengthen their competitive edge, according to UNCTAD (2017). Kedia, Gaffney, and Clampit (2012) argue that market and resource exploration—particularly in emerging economies—is the primary driver of EMNCs’ internationalization. Yet EMNCs in rich countries have also modified their investing methods. Through the adoption of this strategy, these companies are in a position to gain access to new brands, technologies, R&D, managerial, and operational skills, all of which help them enhance their market share. According to Belussi, Rudello, and Savarese (2016), EMNCs are focusing on specific markets inside industries with lower-level technology in order to achieve their overarching goal of becoming more dominant in developed markets.

One interesting aspect about EMNCs is that their acquisitions have been less successful than those of MNCs (Aybar and Ficici 2009). Conversely, institutional distance lengthens the time necessary to complete acquisitions and reduces multinational companies’ ability to conclude M&A deals (Dikova, Sahib, and Van Witteloostuijn 2010). Nonetheless, EMNCs are more likely to offer a higher bid to purchase assets in industrialized countries when they are motivated by a sense of patriotism (Hope, Thomas, and Vyas 2011). Gubbi et al. (2010) discovered that when targets are based in developed markets, cross-border acquisitions really create value for Indian companies. Internationalization behavior in general and the CBMA context in particular are significantly predicted by institutional distance (Kostova 1996). In general, the process of successfully integrating M&As is frequently complicated by differences between the institutional frameworks of the home and host countries. The presumption that EMNCs differ from DMNCs has been the main focus of EMNC internationalization research (Luo and Tung 2007). Consequently, it is imperative to scrutinize the role of institutional distance in ownership participation dependent on MNC classification and ascertain the justification for this difference.

Ownership participation is a key factor in cross-border acquisitions and has garnered significant attention in the finance literature that show that different strategies can result in varying shares held in M&A deals (Chari and Chang 2009; Chen and Hennart 2004; Malhotra, Sivakumar, and Zhu 2011). The level of ownership can affect how resources are allocated and decisions are made, among other aspects of company strategy (Chari and Chang 2009; Das and Teng 2000). Furthermore, Chen (2011) found that companies seeking to acquire complementary capabilities are more inclined to purchase greater equity shares in the acquisition, highlighting the significance of synergies in M&A transactions. It is noteworthy that in order to preserve their intellectual property, companies operating in nations with weak intellectual property rules may also purchase larger equity shares (Chen, Huang, and Chen 2009). Examining the effects of institutional distance—such as differences in law, culture, and economy—on the equity share of foreign acquisitions is therefore crucial.

Previous research has attempted to understand the various dimensions of institutional distance (Ghemawat 2001; Kostova 1996; North 1990) or institutional differences that exist between countries (Berry, Guillén,

and Zhou 2010; Dikova, Sahib, and Van Witteloostuijn 2010; Kostova 1996). Institutional distance refers to the difference in institutional environments across countries which can affect firms' strategies and performance (Dikova, Sahib, & Van Witteloostuijn 2010; Xu & Shenkar 2002). To characterize institutional dimensions, some scholars have proposed classifications, such as the CAGE model of Ghemawat (2001), which encompasses cultural, administrative, geographic, and economic factors. Alternatively, the six dimensions of Dow and Karunaratna (2006) focus on political, economic, legal, social, technological, and environmental factors, while the nine dimensions of Berry, Guillén, and Zhou (2010) include regulatory, normative, cognitive, social, economic, political, historical, geographic, and environmental factors. By examining the concept of institutional distance, scholars can gain valuable insights into the impact of institutional differences on cross-border operations and inform the strategic decision-making of firms looking to expand into new markets.

As to the results reported by Hoskisson et al. (2013), the institutional environment is a critical factor that affects cross-border M&A deals between companies located in different emerging countries as well as between firms from developed and emerging countries. As observed by Dutta, Malhotra, and Zhu (2016), formal (regulatory) and informal (normative) institutional distance significantly impact the investment decision-making of multinational companies, affecting aspects such equity participation and company performance. The degree of equity shares in cross-border acquisitions initiated by DMNCs typically decreases by institutional distance (Pan & Tse 2000); however, this is not always the case for EMNCs, as pointed out by Aybar and Ficici (2009). The CAGE model of Ghemawat (2001) highlights country-specific differences that can influence foreign acquisitions.

Cultural distance, in particular, is one of the most common measures of informal institutional distance (Du and Boateng 2015), and it can have a negative impact on MNC behavior, as observed by Barkema, Bell, and Pennings (1996). It appears that firms located in countries with relatively higher quality institutions are more likely to choose full acquisition, while those located in countries with lower quality institutions tend to choose partial acquisition (Davis, Desai, and Francis 2000). According to these findings, cross-border acquisitions remain a crucial source of internationalization for EMNCs seeking to expand their market reach and competitive advantage.

In the context of cross-border M&A in emerging markets, cultural and economic distance are critical factors that must be taken into consideration. In such markets, EMNCs often prefer to acquire firms in economically developed countries with strong intellectual property protection, as noted by Elango and Pattnaik (2011). To better understand the impact of distance on these deals, it is important to operationalize distance in a more precise and specific manner. This can be achieved by focusing on two key dimensions of distance rather than treating them all as part of a single multidimensional measure, such as "psychic or institutional distance" (Zaheer, Schomaker, et al. Nahum 2012). While Kogut and Singh (1988) reduce psychic distance to only cultural distance, this perspective may be too narrow since psychic distance encompasses a broader concept (Dow & Karunaratna 2006). The notion of psychic distance, as suggested by Kogut and Singh (1988), only considers cultural distance, which is a narrow perspective given that psychic distance encompasses a broader concept (Dow & Karunaratna 2006). Thus, taking a key dimensions' approach allows for the selection of precise dimensions that differentiate countries, leading to a more comprehensive understanding of the cross-border M&A activity (Zaheer, Schomaker, and Nachum 2012).

The concept of economic distance has long been associated with lower levels of internationalization behavior and reduced outcomes for companies, this may not be the case for EMNCs Gaffney, Karst, and Clampit (2016). These firms are driven by institutional deficiencies in their home markets to seek internationalization opportunities that provide a more secure and safe environment, in line with the insights of Luo & Tung (2007). In their quest to improve their competitiveness, EMNCs increasingly pursue cross-border acquisitions in economically distant countries, thereby leveraging the benefits of greater global

integration. To maximize their control and facilitate asset transfers, these companies often seek a higher equity share during the acquisition process, as emphasized by Gaffney, Karst, and Clampit (2016). Such an approach enables them to capture the knowledge and capabilities of the acquired firms, and thus enhance their own strategic and operational capabilities.

In addition to institutional factors, cultural proximity has been identified as a key determinant in cross-border acquisitions (Malhotra, Sivakumar, & Zhu 2011a). Culture, as the most important aspect, is widely discussed generally in terms of access to foreign markets, and particularly, in the context of cross-border acquisitions (Portugal Ferreira et al. 2014; Kogut & Singh 1988). Several researchers have argued that cultural distance between the home and host countries can significantly affect the success of international acquisitions and post-acquisition integration (Malhotra, Sivakumar, and Zhu 2011a, 2011b; Shimizu et al. 2004). However, previous studies on the impact of cultural distance have yielded mixed results, similar to those on geographic distance (Harzing 2003). Many studies suggest that a greater cultural distance between acquiring and target firms increases the likelihood of partial acquisition (Ahern, Daminelli, and Fracassi 2015; Collins et al. 2009; Malhotra 2012; Malhotra and Gaur 2014), reduces the number of foreign acquisitions (Ahern, Daminelli, & Fracassi 2015) and leads to fewer operations (Malhotra, Sivakumar, and Zhu 2011a) which may be attributed to the information asymmetry (Li and Xie, 2013). However, some studies show that developed countries (OECD countries) with cultural and geographic proximity tend to attract a greater number of cross-border acquisitions (Glambosky, Gleason, and Murdock 2015). Using US capital flows to 110 host countries, Bailey and Li (2015) find that cultural distance exerts a negative impact on FDI flows to more distant countries. Nevertheless, this negative influence can be mitigated by the demand factors such as the market power of the host country, which further underscores the critical role of demand-side factors in shaping cross-border investment patterns.

Previous research on cross-border acquisitions initiated by EMNCs has yielded inconsistent results regarding the relationship between cultural distance and capital participation. Malhotra, Sivakumar, and Zhu (2011a, 2011b) pointed out that the impact of cultural distance on capital participation is moderated by the host country's market potential. Malhotra, Sivakumar, and Zhu (2011b) reported a curvilinear relationship between cultural distance and capital participation with a "U-shaped" pattern. Yang (2015) found a positive relationship between institutional (cultural) distance and ownership participation. He also noted that acquirers are less likely to enhance their ownership stakes if countries' regulatory environment (host and home country) are similar. Meanwhile, Liou, Chao, and Yang (2016) and Liou, Chao, and Ellstrand (2017) have found that EMNCs are less likely to acquire full ownership in countries with greater cultural distance. However, these findings contradict the results of Elango and Pattnaik (2011) and Ferreira et al. (2017). Elango and Pattnaik (2011) found that Indian companies tend to acquire full control of companies located in culturally distant countries to create value. Similarly, Ferreira et al. (2017) found that foreign companies opt for full participation despite greater cultural and financial distance between the home country and Brazil. Studies on cross-border mergers and acquisitions (CBMA) in the Chinese market reveal that cultural proximity has a significant positive impact on Chinese capital flows to Western countries and the Asia-Pacific region (Amighini, Rabellotti, & Sanfilippo 2013; Buckley et al. 2007; Quer, Claver, & Rienda 2012). Moreover, the cultural distance creates an informational asymmetry that could result in a partial acquisition (Xie 2014). However, greater cultural difference between the acquiring and target countries increases the level of uncertainty during the process of CBMA, which negatively affects the degree of control (Kang and Jiang 2012). Nevertheless, the results of studies in this area have been inconsistent, with some indicating that acquiring firms tend to gain greater control over targets located in culturally distant countries (Ferreira et al. 2017; Elango & Pattnaik 2011), while others reveal that companies prefer to have greater control over targets in culturally proximity countries (Collins et al. 2009; Ahern et al. 2015; Liou et al. 2016; Liou et al. 2017).

Emerging multinational firms have been accelerating their global expansion (Luo and Tung 2007; Luo and

Rui 2009). However, their behavior may differ from that of developed multinational firms (Aybar and Ficici 2009; Dikova, Sahib, and Van Witteloostuijn 2010; Gaffney, Karst, & Clampit 2016; Gubbi et al. 2010; Hope, Thomas, and Vyas 2011). Indeed, firms from emerging countries are particularly affected by institutional distance during cross-border mergers and acquisitions (CBMA) compared to their counterparts from developed countries (Gaffney, Karst, and Clampit 2016).

Furthermore, the level of government effectiveness in the host country is a crucial factor that affects the acquisition process. Despite the importance of this institutional variable, it has been ignored in resource theory studies (Deng and Yang 2015). Government effectiveness is an integral part of institutional systems that represents the institutional governance and reflects the perception of the quality of public services, policy development and implementation in the host country (Kaufmann, Kraay, and Mastruzzi 2011). For foreign investors to undertake cross-border acquisition activities, host governments must develop and implement sound economic and regulatory policies. Without such policies, economic development will be limited and less attractive to foreign investors (Peng, Wang, and Jiang 2008). Resource dependency theory studies aim to reinforce the power of acquirer firms in order to reduce competition. By removing an important competitor, emerging firms are widely monitored by the host government (Peng, Wang, and Jiang 2008). In fact, the theory's power is influenced by competition laws, which are more likely to be applied in host country with high level of government effectiveness.

In this study, we propose that emerging market multinational corporations (EMNCs) tend to pursue a higher degree of equity ownership in acquisitions of target companies located in economically developed countries with cultural proximity. We also examine the potential moderating effect of government effectiveness level (GE) and the MNC classification on the distance-ownership relationship. In this regard, we provide the following hypothesis:

Hyp 1: *Greater economic distance between acquiring and target countries will increase EMNC equity share in cross border acquisitions.*

Hyp 2: *Greater cultural distance between the acquiring and target countries will decrease EMNC equity share in cross border acquisitions*

Hyp3.a: *Compared to acquirers from developed countries, emerging acquirers are more adversely affected by cultural distance in terms of their ability to participate in the foreign target's capital.*

Hyp3.b: *Compared to acquirers from developed countries, emerging acquirers experience a stronger positive impact of economic distance on their ability to participate in the foreign target's capital.*

Hyp 4: *Efficiency of the target government is expected to have a positive moderating effect on the relationship between economic distance and target capital participation in cross-border acquisitions by firms from emerging countries*

METHOD

To test the hypotheses of our study, we examined two samples of cross-border M&A deals announced between 2004 and 2016, sourced from the Thomson One Banker Merger and Acquisition database and Thomson Eikon. The first sample comprises cross-border acquisitions made by companies from emerging countries during this period. The majority (over 50%) of these transactions were completed by companies based in Brazil, Russia, India, China, and South Africa (the BRICS countries), which are the largest and most influential nations in the emerging market, as designated by the United Nations Conference on Trade and Development (UNCTAD). Our initial sample included 186 acquisitions by Emerging Markets Countries after excluding deals with missing data, and was used to test assumptions 1 and 2. To investigate the impact

of institutional distance on ownership, we use a final sample consisting of 365 acquisitions by developed country firms and 220 acquisitions by emerging country firms that occurred between 2004 and 2018. To account for the classification of multinational enterprises, we include a country variable for the acquirer firm, taking a value of 0 for emerging countries and 1 for developed countries. We exclude leverage buyouts, spin-offs, recapitalizations, self-tender offers, exchange offers, repurchases, acquisitions of remaining interest, and privatizations from the sample. Only deals with a value of at least USD1 million and where the acquirer owns more than 50% of the target shares after the merger are included.

Dependent variables: Ownership participation, or equity participation, refers to the percentage of equity acquired by the acquirer in a cross-border M&A deal. Thomson Eikon provides a continuous scale for this measure, with values ranging from 0.1% to 100%. To exclude M&A transactions that involve portfolio investments, we set the threshold value at 10%. In line with previous studies by Chari and Chang (2009), Chen and Hennart (2004), Malhotra, Sivakumar, and Zhu (2011b), Gaffney, Karst, and Clampit (2016), Liou, Chao, and Yang (2016), and Liou, Chao, and Ellstrand (2017), we examine the range of ownership degrees, which provides a more nuanced measure compared to a binary variable indicating partial or total acquisition. The use of a continuous variable allows for a more precise analysis of the possible changes in the ownership structure (Chen and Hennart, 2004; Malhotra, Sivakumar, and Zhu, 2011b).

Independent variables:

- **Cultural distance (*Dist*):** Cultural distance has been extensively researched in academia and is commonly used to measure and analyze cross-border behavior and informal institutional distance (Liou, Chao, and Yang 2016). To measure informal institutional distance, we use four cultural dimensions – power distance, uncertainty avoidance, individualism, and masculinity/femininity – as identified by Hofstede (1980). We obtain the index data from Hofstede’s official website and construct a measure of the cultural difference between the home and host countries using the mahalanobis distance (Berry, Guillén, and Zhou 2010). A low score on this measure indicates cultural proximity, while a high score indicates that the two countries are culturally distant.
- **Economic distance (*Dist*):** Economic distance is measured by the difference in economic development and macroeconomic characteristics between the home and target countries. To measure economic distance, we use three indicators related to economic differences predominant in studies of international trade: income (measured by GDP per capita), inflation (measured by GDP deflator), and trade intensity (measured by exports and imports of goods and services), as proposed by Berry, Guillén, and Zhou (2010). These indicators affect firm survival, performance, and mode of entry into foreign markets (Zaheer and Zaheer 1997) and are also correlated with consumer preferences and purchasing power, the degree of openness of the economy to exogenous influences, and macroeconomic stability. We measure the distance using the mahalanobis distance as a dyadic distance between the home and host countries. This measure is scale-invariant and takes into account the variance-covariance matrix. Specifically, we use the economic distance proposed and calculated by Berry et al. (2010). The distance of mahalanobis is calculated as follows:

$$d(x, y) = \sqrt{(x - y) \text{Cov}(D)' (x - y)'}$$

Where $\text{Cov}(D)$ is the covariance matrix. If the elements of x and y are independent, the covariance matrix would be an identity matrix, making the Mahalanobis distance equal to the Euclidean distance. Unlike the circular shape of a Euclidean distance ball (in two dimensions), the Mahalanobis distance ball is elliptical in shape.

- **Government Effectiveness (*GE*):** is a dimension of governance used to assess the quality of public services and administrations, as well as the level of independence of the public service from political

pressures in the host country. This indicator is one of the six dimensions of governance defined in the Worldwide Governance Indicators (WGI) developed by Kaufmann, Kraay, and Mastruzzi (2009). It is scored on a scale of 0 (lowest) to 100 (highest).

Control variables: We controlled several relevant factors to clarify the real influence of the two dimensions of institutional distance on the target’s capital participation. Consistent with prior research (Buckley et al., 2007), we include natural resources (LnNat-resources) as a control variable, which is measured as the natural logarithm of the ratio of mineral and metal exports to total goods exported to the host country. We also control for the search for strategic assets (LnStrategic-assets) by using the natural logarithm of the number of patent filings by residents at the host country level. The search for strategic assets and natural resources in the target country has been found to have a positive relationship with the number of cross-border mergers and acquisitions by companies from emerging markets (Deng and Yang, 2015). Additionally, we incorporate total international reserves (*LnReserves*) to capture the effect of the local market on foreign investment activities. Total international reserves are measured as the natural logarithm of the total US dollar value of foreign reserves held by each acquiring country, including monetary gold, special drawing rights, IMF member reserves held by the IMF, and holdings of foreign exchange under the control of monetary authorities. All of these indicators are obtained from the World Bank database. Finally, we also control for geographic proximity (*Same border*) between the acquirer and target firm countries by including a dummy variable that equals 1 if countries share the same border and 0 otherwise. The geographic dummies are sourced from the Central Intelligence Agency CIA World Factbook.

Moreover, to account for potential industry and year-specific effects, the model includes fixed effects for both using two sets of dummy variables (PIndustry_i; PYear_j). Thus, the final model takes the following form:

$$Ownership_i = \beta_0 + \beta_1 * Cult_Dist_i + \beta_2 * Eco_Dist_i + \beta_3 * Same_border_i + \beta_4 LnReserves_i + \beta_5 * LnNat_resources_i + \beta_6 * LnStrategic_assets_i + \epsilon_i$$

Table 1. Definitions of variables			
Variables	Definition	References	Data Source
Dependent variable			
Ownership	Equity participation, or the percentage of ownership held by the acquiring firm after a cross-border acquisition.	Liou, Chao, et Yang (2016)	SDC Platinum
Independent variable			
DistCult	Informal institutional distance is measured through 4 cultural dimensions, namely power distance, control of uncertainty, individualism and the masculine-feminine dimension using the mahalanobis method.	Berry et al (2010).	Greet Hostfede Index (GIS)
DistEco	Economic distance is calculated based on three indicators relating to economic differences: income (measured by GDP per capita), inflation (measured by the GDP deflator) and trade intensity (measured by exports and imports of goods and services).	Berry et al (2010).	World Bank
Moderating variable			

GE	Government Effectiveness captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government’s commitment to such policies. It is scored on a scale of 0 (lowest) to 100 (highest).		World Governance Indicators
Control variables			
LnActif.Strateg	The search for strategic assets is measured by the natural logarithm of the number of patents filed by residents in the target country.	Buckley et al (2007)	World Bank
LnRess.Natur	Natural resource seeking is measured by the natural logarithm of the ratio of mineral and metal exports to exported goods in the target country.	Buckley et al (2007)	World Bank
LnReserves	The natural logarithm of the total US dollar value of each acquiring country’s foreign exchange reserves.	Luo et Wang (2012)	World Bank
Contig	Binary variable which takes the value of 1 if the countries share the same border, 0 otherwise.	Ragozzino (2009)	CIA Factbook

RESULTS

Table 2 provides a summary of descriptive statistics for the variables used in our analysis. The table is presented in two panels: one for a sample of 186 deals performed by emerging market countries (Panel 1), and the other for a sample of 585 deals performed by acquirers from developed (365 deals) and emerging countries (220 deals). On average, the ownership in the sample is more than 80%. The cultural distance has an average value of 8.07, indicating that the cultural distance between emerging countries has become narrower over time. The economic distance has an average value of 13.87, which suggests that maintaining economic stability reduces the economic distance between countries. We also observe that firms from emerging markets tend to acquire targets based in countries with a common border, with an average value of 0.13.

Table 2: Descriptive statistics					
Variable	Observation	Average	Standard deviation	Min	Max
Panel A: sample of acquirers from emerging countries					
Ownership	186	80.22	28.79	10%	100%
Eco.Distance	186	13.87	10.91	0.95	68.12
Cult.Distance	186	8.07	5.58	2.18	30.85
Same border	186	0.13	0.34	0	1
LnReserves	186	12.39	1.55	8.23	15.17
lnNat resources	186	1.44	0.89	-2.10	3.98
lnStrategic assets	186	8.39	2.86	1.95	13.19
GE	186	81.67	19.25	22.11	100
Panel B: sample of acquirers from developed and emerging countries					
Ownership	585	84.56	26.69	10%	100%
Eco.Distance	585	7.99	11.26	0.44	109.21
Cult.Distance	585	7.99	5.47	1.13	36.16

Same border	585	0.16	0.36	0	1
Ln Reserves	585	11.95	1.71	5.32	15.18
lnNat resources	585	1.37	0.86	-2.10	4.13
lnStrategic assets	585	9.29	2.76	1.94	13.19
GE	585	84.71	15.81	20.19	100

The variables corresponding to the search for strategic assets and natural resources have average values of 8.39 and 1.44, respectively. This suggests that firms from emerging markets tend to acquire targets based in knowledge-based economies and countries with more natural resources. Finally, the average value of the total international reserves is 12.39, indicating the importance of having a solid financial environment in the domestic economy for foreign investment activities.

The correlation matrix is shown in **Table 3**. While the variables in the correlation matrix are not highly correlated, we assessed the potential for multicollinearity by computing the variance inflation factor (VIF) scores for each variable. Our analysis revealed that the maximum VIF score across all variables and regressions was 3.97, which is well below the threshold of 10. Therefore, we can conclude that multicollinearity is not a concern in this study.

Table 3: Pearson correlation matrix

	1	2	3	4	5	6	7	8
Panel A: sample of acquirers from emerging countries								
1. Ownership	1.0000							
2. Eco. Dist	-0.1645**	1.000						
3. Cult. Dist	-0.1814**	0.0540	1.000					
4. Same_border	0.1110	0.2590***	0.0626	1.000				
5. LnReserves	-0.0045	-0.1838**	-0.1189	-0.0038	1.000			
6. lnNat_resources	0.0035	0.1050	-0.1517**	-0.1235	0.0125	1.0000		
7. lnStrategic_assets	0.2279***	-0.3938***	-0.1856**	-0.3371***	0.1145	-0.1051	1.000	
8. GE	0.2425***	-0.1167	-0.0494	-0.1114	0.1276*	-0.0808	0.2817***	1.0000
Panel B: sample of acquirers from developed and emerging countries								
1. Ownership	1.0000							
2. Eco. Dist	-0.2617***	1.000						
3. Cult. Dist	-0.1510***	0.1455***	1.000					
4. Same_border	0.0669	0.1775***	-0.0626	1.000				
5. LnReserves	0.0300	-0.1667***	0.0773*	-0.1260***	1.000			
6. lnNat_resources	-0.0461	0.0311	-0.1949***	-0.1428***	0.0319	1.0000		
7. lnStrategic_assets	0.2970***	-0.4661***	-0.3713***	-0.0761*	0.0116	-0.2289***	1.000	
8. GE	0.2649***	-0.3602***	-0.0945**	0.0228	0.0553	-0.1281***	0.3093***	1.0000

*, **, ***, present the level of significance of, respectively, 10%, 5%, and 1%.

The study conducted regressions of institutional distance versus ownership, and the results are presented in **Table 4**. The findings indicate that the coefficients of Eco.Dist are significantly negative, suggesting that formal institutional distance (economic distance) has a significant negative effect on ownership participation. This finding contradicts **Hyp1**. In the case of informal institutional distance, the regression coefficients of Cult.Dist are negative as expected, but not statistically significant. However, the impact of geographical proximity (same_border) on the degree of takeover is positive and significant. This suggests that acquirers from emerging countries are more likely to acquire full ownership of targets in countries that are geographically closer. This is because smaller geographic distance reduces the problems of informational asymmetry, increasing the likelihood of total ownership of the target's shares (Buch and DeLong 2004). State-owned firms also tend to have total (partial) control of targets in geographically close (distant) countries, respectively (Karolyi and Liao 2017). The study also found that the effects of strategic assets (LnActif.Strateg) and natural resources are positively related to the degree of participation in the target's capital. In Model (3), the estimate suggests that a 1-unit increase in the strategic asset (e.g., number of patents) of the target country is associated with an increase of 1.0189 units ($\exp(0.0187)$) in share ownership. The search for strategic resources is one of the main motives for M&A transactions, as they provide firms with a competitive advantage by linking target's resources to the needs of the acquiring company. Moreover, countries rich in strategic resources attract cross-border acquisitions of emerging companies (Haleblian et al. 2009; Nicholson and Salaber 2013). Finally, the study notes that natural resource research has a positive impact on the percentage of shares held, but the result is not statistically significant.

	Economic distance (1)	Culture distance (2)	Institutional distance (3)
Eco.Dist	-0.0038** (-2.07)		-0.0039** (-2.12)
Cult.Dist		-0.0074 (-1.59)	-0.0075 (-1.62)
LnReserves	-0.015 (-1.21)	-0.014 (-1.04)	-0.018 (-1.39)
lnNat_resources	0.029 (1.22)	0.0168 (0.73)	0.0213 (0.92)
lnStrategic_assets	0.0218*** (2.81)	0.0235*** (3.10)	0.0187** (2.38)
Same_border	0.219*** (3.93)	0.195*** (3.27)	0.216*** (3.92)
GE	0.0032*** (2.69)	0.003** (2.52)	0.0032*** (2.70)
Constant	0.536*** (2.79)	0.532** (2.58)	0.667*** (3.19)
Obs	186	186	186
R²	0.1537	0.1556	0.1733
Prob>F	0.0000	0.0001	0.0000

The numbers in brackets are the associated t-statistics. *, **, *** indicate significance at the 10%, 5%, and 1% levels, respectively.

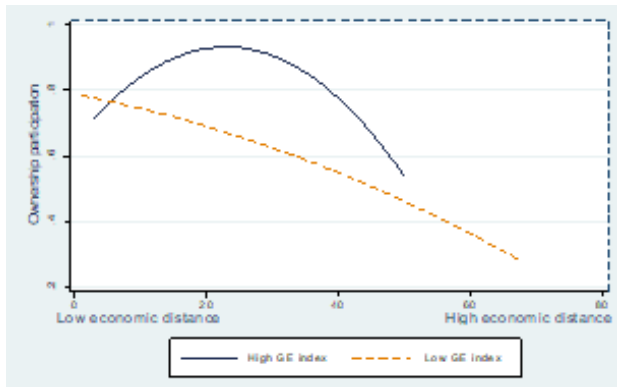
In this study, we examine whether the impact of institutional distance on ownership depends on the level of government effectiveness in the target country. To test for moderating effects, we also estimate two sub-samples based on the average government efficiency index (high or low). To better understand the impact of our predictor variables on the degree of capital participation, we control for fixed effects of the year using a set of dummy variables, as well as the target country’s government effectiveness level. The estimated results are presented in **Table 5**. Model (1) serves as the reference model and includes only the control variables for targets based in countries with high levels of government efficiency. The coefficients of (ln Natural resources) and (ln Strategic assets) are significantly positive, indicating that for emerging acquirers, higher levels of good governance in the host country help to strengthen the relationship between the degree of ownership and the abundance of natural resources and strategic assets in that country. These findings are consistent with the results of Models (2) and (3). The coefficients of “Same border” remain consistently positive and significant across all regressions, suggesting that the degree of participation in the target’s capital increases when the acquiring and host countries share a common border. These results are in line with the findings of Grinblatt et Keloharju (2001), who showed that acquirers are more likely to hold shares in companies located in geographically close countries that share the same language. However, proximity in terms of geographic distance also often implies shared cultural aspects, which can reduce the cost of acquiring information.

Table 5: moderating effects of Government effectiveness (GE).

	<i>High government effectiveness level</i>					<i>low GE</i>
	Control variable (1)	Culture distance (2)	Economic distance (3)	Economic distance (4)	All variables (5)	All variables (6)
Constant	0.4198 (1.49)	0.6788** (2.30)	0.4234 (1.39)	0.4757 (1.47)	0.8642*** (2.92)	1.337*** (3.77)
Same_border	0.2154*** (2.86)	0.1937*** (2.67)	0.2155*** (2.85)	0.2543** (2.55)	0.2448*** (3.11)	0.217** (2.44)
LnReserves	-0.0086 (-0.41)	-0.0159 (-0.76)	-0.0088 (-0.40)	-0.0085 (-0.40)	-0.0169 (-0.86)	-0.0473* (-1.64)
lnNat_resources	0.0867*** (2.62)	0.0734** (2.33)	0.0869** (2.54)	0.0679** (2.05)	0.0293 (1.00)	0.005 (0.13)
lnStrategic_assets	0.0241*** (2.70)	0.017* (1.94)	0.024*** (2.66)	0.0076 (0.64)	-0.0150 (-1.46)	0.0035 (0.15)
Cult.Dist		-0.0118*** (-2.34)			-0.0184*** (-3.37)	0.0004 (0.04)
Eco.Dist			-0.0001 (-0.03)	0.0194 (1.58)	0.0365*** (2.89)	-0.0093*** (-3.44)
Eco.Dist ²				-0.0004* (-1.92)	-0.0008*** (-3.35)	
Year FE	Yes	Yes	Yes	Yes	Yes	No

Obs	133	133	133	133	133	53
R ²	0.2435	0.3009	0.2435	0.2778	0.3940	0.2230
Prob>F	0.0010	0.0000	0.0003	0.0000	0.0000	0.0000

The numbers in brackets are the associated t-statistics. *, **, *** indicate significance at the 10%, 5%, and 1% levels, respectively.



Fig(1): ownership, economic distance and GE index

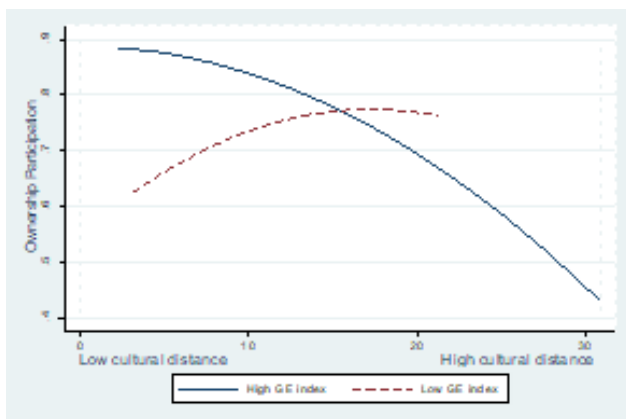


Fig (2): ownership, cultural distance and GE index

In Model (2) to (4), we investigated the effects of institutional distances on ownership, where Model 2 examines the impact of cultural distance, which shows a significant negative effect on ownership as cultural differences increase. This finding is consistent with previous research by Liou, Chao, and Yang (2016) and Liou, Chao, et Ellstrand (2017) and suggests that cultural differences lead to increased information asymmetry and risk for the acquirer. Model (3) presents the results of the effect of economic distance on the capital participation of the target with a high level of government efficiency. We note that the economic distance has a negative and non-significant impact on the capital participation ($\beta = -0.0001$), which is contrary to that expected. To further examine our findings, we tested a curvilinear relationship between economic distance and equity participation. **Fig (1)** depict the resulting relationship of the effect of economic distance on the degree of capital participation by the level of effectiveness of the target government. **Fig (1)** show a curvilinear relationship at a high level of government efficiency. The degree of participation is first positively associated with economic distance, then negatively beyond a certain level of government efficiency. It would seem that the impact of economic distance on the ownership only appears from a certain level of efficiency of the target government. The model (4) introduces the squared economic distance. This changes the sign of the economic distance coefficient from negative to non-significant positive with the squared economic distance coefficient negative. This reveals the existence of an inverted U relationship between economic distance and ownership participation. This finding provides a partial

validation to our hypothesis, so that the capital participation has a positive relationship with economic distance at a point, but becomes strongly negative. This relationship is illustrated in Fig (1). Estimates in Model (5) incorporate all independent variables. Economic distance has a significant positive effect on ownership participation as predicted in hypothesis 4. This variable is significant at the $p < 0.001$ to explain the degree of equity participation when acquiring targets with high government efficiency index. Cultural distance is negatively associated with ownership participation. The relation between cultural distance and share ownership when acquiring targets based in country with higher level of government efficiency is graphed in Fig (2). Model (6) examines the relationship of economic distance when targets are located in countries with low government efficiency. Economic distance is negatively associated with ownership participation ($\beta = -0.0093$, $p < 0.001$). Fig (1) demonstrates that economic distance affects cross-border acquisition ownership participation differently by government effectiveness level. Specifically, for higher GE level economic distance increases ownership participation, but for low GE level it decreases it.

Table 6 shows the effect of acquirer’s classification on the relationship between institutional distance and ownership. Model 1 includes only the control variables. We note that the search for strategic assets and geographic proximity have a positive and significant effect at the $p < 0.001$ level on the target’s degree of participation, in order to obtain a competitive advantage. To clarify the true influence of the two dimensions of institutional distance on participation ownership, we controlled a variable associated to home country which takes the value 0 for developing countries and 1 for developed countries. The model (3) examines the effect of cultural distance on the proportion of shares held by acquirers. Similar to our initial findings in the emerging acquirers only sample, cultural distance has a significant negative effect on ownership participation in our enlarged sample. The interaction term of cultural distance and acquirer’s classification is positive (*Cult.Dist *ACQ*) which means that there is a significant difference in the impact of cultural distance on the degree of ownership according to the classification of acquirers (developed or emerging countries) through cross-border acquisitions ($\beta = 0.100$, $p < 0.001$). Model (4) tests hypothesis 3, that economic and cultural distance have differing effects on equity participation for emerging acquirers and developed acquirers. The interaction term of cultural distance and the classification of acquirers companies is positive which means that there is a significant difference in the equity held by emerging companies when acquiring culturally distant firms through cross-border acquisitions ($\beta = 0.0084$, $p < 0.01$). This supports hypothesis 3.a.

	<i>Model (1)</i>	<i>Model (2)</i>	<i>Model (3)</i>	<i>Model (4)</i>	<i>Model (5)</i>	<i>Model (6)</i>
<i>Constant</i>	0.465***	0.650***	0.508***	0.630***	0.614***	0.718***
	(5.00)	(5.87)	(4.82)	(5.42)	(5.46)	(5.64)
Same_border	0.0737***	0.0850***	0.0833***	0.0926***	0.0983***	0.0545**
	(2.84)	(3.23)	(3.3)	(3.46)	(3.77)	(1.97)
LnReserves	0.00590	0.00238	0.0092	0.00570	0.00419	0.00288
	(0.93)	(0.38)	(1.45)	(0.85)	(0.62)	(0.40)
lnNat_resources	0.0121	0.00548	0.0031	0.00128	0.00674	0.0147
	(0.84)	(0.37)	(0.21)	(0.09)	(0.47)	(0.74)
lnStrategic_assets	0.0303***	0.0208***	0.0251***	0.0193***	0.0210***	0.0136**
	(7.80)	(4.32)	(5.53)	(4.03)	(4.54)	(2.54)
Predictors						
Cult.Dist		-0.00177	-0.009***	-0.00812**		
		(-0.68)	(-2.68)	(-2.16)		
Eco.Dist		-0.00415***		-0.0033***	-0.0069**	-0.0123***

		(-4.21)		(-3.08)	(-2.44)	(-2.72)
Eco.Distance ²					3.11e-05	0.0002***
					(0.99)	(3.05)
Moderators						
Cult.Distance *ACQ			0.100***	0.00844**		
			(3.59)	(2.57)		
Eco.Distance *ACQ				3.84e-05	0.00226	0.0119*
				(0.02)	(0.46)	(1.88)
Eco.Distance ² *ACQ					6.52e-05	-0.000230
					(0.38)	(-1.16)
Obs	585	585	585	585	585	435
R²	0.099***	0.122***	0.1286***	0.142***	0.128***	0.0774***

The numbers in brackets are the associated t-statistics. *, **, *** indicate significance at the 10%, 5%, and 1% levels, respectively.

We graphed the interaction in **Fig. 3**. Regarding the interaction term for economic distance and acquirer’s classification, our hypothesis 3b is not confirmed. The coefficient associated with the interaction term is not significant.

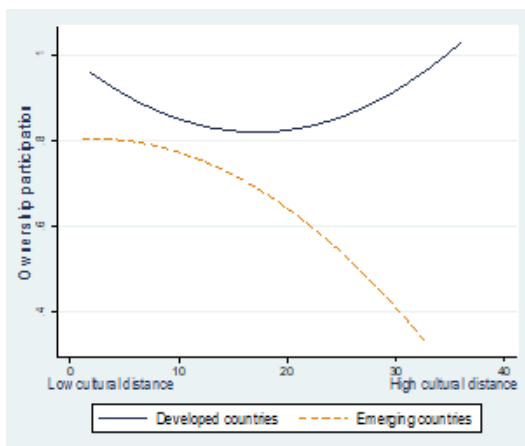


Fig (3): ownership participation, cultural distance and acquirer’s classification

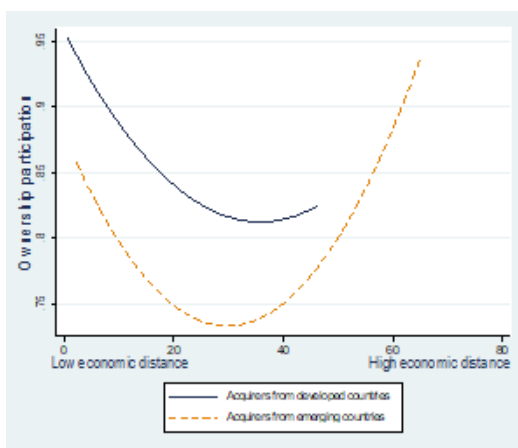


Fig (4): ownership participation, economic distance and acquirer’s classification

Due to the curvilinear relationship that we found, in only emerging acquirers sample, insignificant results regarding the interaction term of economic distance and the classification of acquirer's countries (model 5). Indeed, we focussed on a sample of targets located in countries with high government effectiveness level (model 6). We found that economic distance retains its negative sign and significance. The interaction term for economic distance and acquirer's classification is positive and statistically significant only at the 10% level. Hence, there is a significant difference between the two groups of buyers in the ownership participation when acquiring targets with high government efficiency level. We plotted the interaction graph for economic distance and acquirer's classification in Fig. 4, which demonstrates that economic distance affects cross-border acquisition equity participation differently for emerging acquirers than developed acquirers.

DISCUSSION

The first hypothesis was to ascertain the connection between economic distance and ownership participation. The economic distance was negatively associated with the ownership participation. This finding contradicts Hyp1.

The second hypothesis was to find out if *cultural distance between the acquiring and target countries has an influence on EMNC equity share in cross border acquisitions*. there is no statistically significant relationship between *cultural distance and ownership participation*, thus rejecting the hypothesis Hyp2.

Regarding the interaction term for economic distance and acquirer's classification, our hypothesis 3b is not confirmed due to the curvilinear. The third hypothesis was to ascertain whether the classification of acquirers affects the relation between the institutional distance and ownership participation. According to the study, the interaction term of cultural distance and the classification of acquirers companies is positive which means that there is a significant difference in the equity held by emerging companies when acquiring culturally distant firms through cross-border acquisitions; thus, the hypothesis 3.a that compared to acquirers from developed countries, emerging acquirers are more adversely affected by cultural distance in terms of their ability to participate in the foreign target's capital is accepted.

Indeed, we focussed on a sample of targets located in countries with high government effectiveness level. Hence, there is a significant difference between the two groups of acquirers in the ownership participation when acquiring targets with high government efficiency level. In particular, economic distance increases the level of shareholdings purchased by acquiring firms based in emerging countries in the context of cross border M&A. This result is also confirmed by Gaffney, Karst, and Clampit (2016). While in the case of acquirers from developed countries, economic distance leads to partial acquisition of target's capital. Our results indicate that the formal (economic distance) and informal institutional distance (cultural distance) have a significant impact on the level of shareholdings purchased by acquirers from emerging countries during transnational mergers and acquisitions. These relationships are significantly different from those observed when examining acquirers from developed countries.

The fourth hypothesis of the study was to examine whether the impact of institutional distance on ownership depends on the level of government effectiveness in the target country. Prior research had suggested that M&A activity can be constrained by the level of host government effectiveness, which is an important institutional variable (Deng and Yang, 2015). The results showed a negative effect in the case of high level of government efficiency. This finding is consistent with Liou, Chao, and Yang (2016) and Liou, Chao, et Ellstrand (2017). These estimates indicate that cultural distance increases the information asymmetry and thus increases the risk faced by the acquirer. The results showed a curvilinear relationship at a high level of government efficiency. The degree of participation is first positively associated with economic distance, then negatively beyond a certain level of government efficiency. The outcomes laid out that economic

distance affects cross-border acquisition ownership participation differently by government effectiveness level. Specifically, for higher GE level economic distance increases ownership participation, but for low GE level it decreases it.

Our results indicate that economic distance can have a positive effect for firms from emerging countries, displaying behavior distinct from that of developed countries. This aligns with the internalization theory for companies from less developed nations. Furthermore, cultural distance seems to have a greater adverse effect on the degree of ownership taken in acquisitions for emerging market acquirers compared to acquirers from developed countries.

CONCLUSION

Based on previous studies (Aybar and Ficici 2009; Gubbi and al. 2010; Hope, Thomas, and Vyas 2011), our results enhance comprehension regarding the motivations behind cross-border acquisitions by companies in emerging market. It has been shown that institutional distance reduces ownership participation in international acquisitions (Pan and Tse 2000). Conversely, our results indicate that the effect of economic distance can be positive in the case of companies from emerging countries. This is consistent with Davis, Desai, and Francis (2000) who report a negative association between countries institutional quality and mergers and acquisitions investments. This underscores the significance of cross-border acquisitions as a pivotal means of international expansion for companies from emerging markets. Similarly, Gaffney, Karst, and Clampit (2016) affirm this conclusion based on their analysis of 519 acquisitions by firms headquartered in BRIC nations.

The relation between institutional distance and ownership level doesn't consistently follow a straight line but often displays a curvilinear pattern, as evidenced in both cultural distance (Malhotra, Sivakumar, and Zhu 2011b) and economic distance (Gaffney, Karst, and Clampit 2016). Our research findings suggest that the inverted U-shaped relationship, which signifies this pattern, varies notably based on the effectiveness of the host country's government. Specifically, we've noted that this relationship shifts from a linear correlation in instances of low government efficiency to a curvilinear association in situations of high government efficiency. Previous studies have reported that companies from emerging economies are willing to take risks to acquire companies that assist in rapidly enhancing their capabilities and securing strategic assets that might not be available within their local markets.

This research explores the impact of both formal and informal institutional distance on shareholding levels in emerging markets in cross border M&A. Earlier studies suggest that a higher level of control by the target company aids in the transfer of assets (Chari and Chang (2009) and Das and Teng (2000)). As outlined by Gaffney, Karst, and Clampit (2016), managers from economically distant emerging market companies can potentially boost the extent of equity participation.

Motivated by the need to better understand a prominent group of foreign acquirers, we examined acquisitions initiated by Emerging Market companies over a 12-year period. We observed that these emerging acquirers tend to hold greater equity share in targets located in more economically advanced nations, sharing cultural proximity. This higher stake aims to secure increased control over the target company and streamline the transfer of strategic assets. Notably, this relationship is more robust for acquirers from less developed countries than those from developed countries, consistent with the findings of Gaffney, Karst, and Clampit (2016) by comparing cross-border acquisition activity of firms based in BRIC countries versus the U.K.

More precisely, our study's empirical findings highlight the differential impact of economic distance on the equity share sought by acquirers based in emerging markets, contingent upon the level of government efficiency. Notably, companies from emerging markets aim for larger equity stakes when acquiring targets

in countries with higher economic development and efficient governance. Conversely, in instances of weak government efficiency, economic distance between countries leads to partial participation. Interestingly, we found that acquirers from developed countries choose partial (total) control over the target located in a country economically distant (proximity) irrespective of the level of government effectiveness. Furthermore, as suggested by EMNE specific internationalization theory, we found that these dimensions of institutional distance affected EMNEs differently than MNEs from a more developed country.

The core aspects of institutional theory remain more influential in both developed and developing markets (Peng, Wang, and Jiang 2008; Peng et al. 2009). Similar to the observations of Gaffney, Karst, and Clampit (2016), the use of specific dimensions of institutional distance provides a more nuanced examination of firm behavior within developing countries and between developed and developing countries. This underscores the critical importance of institutions and institutional theory in understanding these dynamics.

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