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Implications of Cross-Border Mergers and Acquisitions by TNCs in Developing Countries: A Beginner's Guide

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International mergers and acquisitions have become the preferred mode of overseas investment by multinational companies, accounting for the bulk of FDI in the developed world and for increasing shares in the developing world. However, many government s express concern about this mode of MNC entry, preferring 'greenfield' investments to the takeover of national firms. This paper provides an overview of the main economic costs and benefits that may be involved and argues that M&As do have costs but these may be over-stated.

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1. INTRODUCTION

International mergers and acquisitions (M&As), particularly those with giant transnational companies (TNCs) spending vast sums of money to take over firms in other countries, are one of the most visible aspects of globalisation. Such M&As are now the most important form of FDI, far outstripping investment in new facilities ('greenfield' investments) in terms of value (see various issues of UNCTAD, *World Investment Report*).[1] While most such M&As take place within the industrial world, they are also increasing in importance in the developing world (largely in the form of acquisitions since mergers with local firms are relatively uncommon). Cross-border M&As can have important implications for host countries. They tend to lead to substantial restructuring of existing facilities. They can lead to a repositioning of the acquired enterprise in global and local markets and to consolidating international networks of production, innovation and marketing (Maucher, 1998). They may involve significant layoffs and technological change. They may also lead to 'asset stripping', where the physical and other assets of the acquired firm are separately sold off and the enterprise wound up as a productive operation.

Cross-border M&As are often regarded with suspicion and trepidation by developing countries. Many industrial countries also dislike the idea of national enterprises or property being taken over by foreign companies. However, developing countries feel more vulnerable because of the inherent asymmetry: their firms are not generally in a position to take over firms in the industrial countries from which most TNCs come and are more concerned with promoting the development of domestic entrepreneurship. Yet, there is a very strong revealed preference on the part of TNCs to enter countries by the M&A route, and restricting this route may well mean keeping out valuable FDI. This paper provides a 'beginner's guide' to these issues in cross-border M&As in developing countries.

For a start, it is important to note that the same forces drive both FDI and M&As: rapid technical change, shrinking economic distance, intensifying competition and policy liberalization. M&As are, however, more than just one of many modes of channelling direct investment: the form affects the content significantly. M&As may capture and create new synergies between national and foreign firms and, as such, may be an important means of restructuring national economies in line with emerging technological forces. Unlike FDI through greenfield ventures, they involve local enterprises directly in this restructuring and integration process. However, as with globalisation generally, the impact of M&As can be double-edged and uneven. Capital markets are not a perfect means of allocating resources and restructuring activities. TNCs do not operate with full information, and wrong decisions on M&As can lead to high economic and social costs in host economies. The private interests of TNCs may diverge from the social interests of host economies: take-overs may lead to asset stripping, downgrading of local capabilities or the transfer abroad of scarce assets.

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[1] While the data on M&As (which are lumpy and spread over different years) are difficult to compare directly with annual FDI inflow, UNCTAD estimates that around 80 percent of direct investment in the developed countries consists of cross-border M&As. In the developing world, cross-border M&As reached a peak in 1998 at about $70 billion, 40 percent of total FDI inflows. The highest share (nearly 90 percent of FDI) was in Latin America, with Africa (including North Africa) at 31 percent and Asia at about 19 percent. Calculated from Figure IV.8c of UNCTAD, *World Investment Report 2000.*

In fact, there appears to be a general presumption that in 'normal' circumstances (when there is no economic crisis or transition, and ignoring privatisation), FDI in the form of greenfield ventures is preferable to M&As. The former entails building a new plant, the latter involves only the transfer of an existing plant or firm from local to foreign hands. This suggests, at least at first sight, that greenfield FDI adds to the host country's productive system, while M&As do not; on the contrary they 'denationalise' existing national assets and add to foreign exchange burdens without adding to productive capacity.

This popular perception has some validity, but it can also be misleading. A sound economic analysis of the effects of the two modes of entry must be based on a sound understanding of the global context and realistic counterfactuals. While there do remain differences between the two modes, these are not as large or evident as often thought by host governments. This paper provides a preliminary review of the analytical issues involved.

2. ANALYTICAL BACKGROUND

There are essentially five ways in which a TNC can serve a foreign market:

1. *No direct investment*: serve the market by exports or licensing local firms.
2. Invest directly by a *greenfield* venture.
3. Invest directly by *acquiring* a local firm.
4. Invest directly by *merging* with a local firm.
5. Enter into a *strategic alliance* with a local firm.

The choice between FDI and externalised means of serving markets (i.e. between 1 and the others) has been extensively analysed in the international investment literature. Once the decision to invest directly has been taken, however, the choice of mode and its economic effects on countries has received less attention (Dunning, 1999). The management literature has examined its ramifications from the company viewpoint, but the economic implications for host countries, particularly developing countries, remain unexplored.

While a free choice between modes 2 to 6 is feasible in developed economies with liberal entry rules, strong private enterprises and well-functioning capital markets, this is not true of many developing and transition economies. Here the practical choices are more limited. For instance, M&As are not a realistic alternative to greenfield investment in the least developed countries (e.g. in Sub-Saharan Africa) where there is little to acquire in the private sector. However, there is considerable scope even here for the acquisition of state-owned enterprises as governments liberalise and privatise.[2] In developing countries with larger industrial sectors and better-developed capital markets, the acquisition of private enterprises *is* a realistic alternative to greenfield entry (though, unlike in industrial countries, it may be confined to low to medium technology activities). Mergers, however, are less feasible because of the large gaps between local and foreign firms in size, technology and management (though advanced newly industrializing economies (NIEs) like the Republic of Korea have firms with the size and capabilities that make them attractive for mergers). The same goes, more

[2] Foreign exchange raised through privatisation (from both FDI and portfolio flows) represented about 44% of total revenue generated by privatisation in developing countries during 1990-97 (up from only 8% in 1980). In Sub-Saharan Africa the foreign exchange contribution to privatisation revenue was 59% in the 1990-97 period. In the last year for which data are available, foreign exchange represented 83% of privatisation revenue in SSA compared with only 43% in developing countries. Some *80-90%* of this foreign exchange was in the form of FDI. Source: World Bank.

forcefully, for strategic alliances: few are likely in the developing world, though some exist in the most advanced NIEs.

In most transition economies, at least early in liberalization, the acquisition of state-owned enterprises is the most practical (sometimes the only permitted) way to enter the market. Thereafter greenfield entry becomes more likely, though mergers and strategic alliances are largely in the future for most countries. Thus, the focus on greenfield versus M&As makes considerable empirical sense in developing and transition economies.

The management literature has investigated four aspects of the choice: *investing firm characteristics, target country characteristics, industry characteristics and investment characteristics*. The most common framework is transaction costs analysis, investors choosing the mode that minimises the costs of entry. Some important findings (drawing on Harzing, 1999, and others) are as follows (some subtleties and qualifications in the argument are ignored below in the interests of brevity):

☛ Firms with lower R&D intensity are more likely to buy technological capabilities abroad by acquisition, those with strong technological advantages are likely to set up greenfield ventures.

☛ More diverse investing firms are likely to enter new markets by acquisitions.

☛ In the recent (post 1980) period, firms with greater international experience have higher levels of acquisition than do others.

☛ Larger TNCs are traditionally more prone to acquire than small ones. However, in recent years smaller firms have become more prone to acquire as transaction costs of M&As have declined.

☛ The greater the cultural and economic distance between the home and host countries, the less the probability of acquisition. Most M&As concentrate in developed home and host countries with similar cultural and business practices.

☛ Advertising intensity leads to more acquisitions if brands are valuable and cannot be easily transferred across countries. This propensity is strengthened where local firms have established distribution systems and extensive knowledge of the local market.

☛ Greenfield investments offer the investor greater control and more ability to mould affiliate structures, systems and culture than acquisitions. Acquired firms have established structures, procedures and behaviour patterns that may be difficult to change.

☛ For the same reason, greenfield investments will tend to have greater intra-company trade than M&As, which would have established local supply and demand links.

☛ Acquisitions are encouraged by capital markets imperfections that lead to the undervaluation of company assets (Gonzalez *et al*. 1997). By a similar reasoning, they are also encouraged by economic crises that lead to sharp falls in asset prices generally.

☛ Horizontal acquisitions are driven by the search for new markets, products and brands rather than cost cutting (Capron, 1999). Such acquisitions often lead to 'asset rationalisation' which can damage the acquired firm's capabilities; however, where there is a transfer of competence, there is a synergistic benefit to both parties.

☛ In the immediate post-acquisition period, there is substantial one-way (acquirer to acquired) technology transfer, often imposed. Over time, however, there is a more reciprocal process of technology transfer and sharing of tacit knowledge (Bressman *et al*. 1999).

In sum, from the investor perspective, M&As in general offer *advantages* over greenfield investments of rapid entry and access to existing proprietary assets (technology,

skills, organisation, information, supplier networks, brands, contacts etc.). Where capital markets are imperfect or in crisis, M&As also offer access to undervalued capital assets. In *developing countries* specifically, however, the advantage of M&As is rarely access to proprietary technology or skills (with exceptions in some NIEs). The advantage is more rapid entry, local market knowledge, established distribution systems and contacts with the government, suppliers or customers. Acquisitions (*via* the privatisation route) may also be the only way to enter some services and infrastructure activities; in countries where other investment opportunities are lacking, this may be the predominant form of FDI.

The general *disadvantages* of M&As lie in the cultural and organisational inertia inherent in any established concern that raises the cost of integrating the acquired firm into corporate systems and bringing its technologies and skills to international levels. Where the cost of changing ingrained habits, routines and skills is likely to be high, TNCs will prefer greenfield entry. Such problems are likely to larger in developing economies that have not been exposed to international competition and are far behind 'best practice' management and technological levels. In addition, local contacts with suppliers and customers may be worth very little in an economy that is liberalising and so has to drastically restructure its markets. The acquisition of private firms in developing countries also faces the difficulty that it may be costly and cumbersome to value companies where asset markets and corporate governance are weak or rudimentary.

The assessment of the costs and benefits of the two modes will, of course, vary with corporate attitudes, information and global strategies. That is why different investors will opt for different modes of entry, or set very different prices and conditions on potential M&As, under the same conditions.

3. ASSESSING M&AS VERSUS GREENFIELD FDI

3.1 INTRODUCTION

This section compares the possible costs and benefits to host economies of the two modes of entry under various headings. This can be done only be posing *realistic counterfactuals*: what would have happened if the investment had not taken place (in that particular form).

A realistic counterfactual must go beyond the individual investment to take account of the *economic context* in which investment takes place. This depends on the particular situation of each country as well as on the general context of trade, technology and competition in the developing world. As noted, the latter is changing. Trade liberalization, intensifying competition, accelerating technical change and increasingly integrated global production systems all mean that firms have to rapidly upgrade, restructure and become internationally competitive. This is true of all economies, regardless of the macroeconomic situation. However, macroeconomic disturbances make the process much more difficult. Financial crises (as in East and Southeast Asia in 1997-1999), debt and fiscal problems (in parts of Africa) or high rates of inflation exacerbate pressures on firms, often making sheer survival difficult.

Inward FDI provides a potent tool for upgrading competitiveness (UNCTAD, 1999). In economies where domestic technological capabilities and skills are weak and raising them to international levels is difficult, it is probably the most powerful available tool. Even in economies where capabilities are strong, the pace of technical change and the growth of international production systems often make TNC participation invaluable. M&As as a

mode of inward FDI is one important way to restructure and upgrade competitive capabilities (Maucher, 1998). Its contribution has therefore to be assessed relative to a situation where domestic firms (that do not get acquired or merged) have to face globalisation on their own. In addition, they have to face competition from the foreign investor which now, by assumption, mounts a greenfield venture in the same market.

3.2 FINANCE

Both greenfield and M&A investments add to financial resources in the host country (to the extent that neither is financed by raising local resources). Greenfield FDI manifests itself in new productive facilities while an M&A transfers the ownership of existing assets into foreign hands. The transfer places investible resources in the hands of the former owners (in cash or disposable shares) so the net financial effect is the same, if the size of the investment is identical. Both result in dividend outflows in due course. In the narrow sense, then, there is no difference between the two modes.

In times of financial crisis, however, M&As can provide the additional benefit of saving domestic firms that are in a severe liquidity crisis (but otherwise viable), and contributing foreign exchange inflows for the economy as a whole. This has shown to be the case in East and Southeast Asia during the recent financial crisis (UNCTAD, 2000, forthcoming). To quote,

> "M&As became an important source of finance at the time of the crisis, thereby contributing to the speedy recovery of the economies. True, under normal circumstances it is possible for an acquirer to raise capital in the local financial markets without bringing in new capital from outside. But in the crisis-hit countries which experience a credit crunch and depressed domestic financial markets, cross-border M&As necessarily entail fresh capital inflows from the outside." (p. 16)

At the same time, the fact that many firms were sold at depressed ('*fire sale*') prices suggests that M&As entail a net cost to the host economy compared to similar greenfield investments. This would be the case if the acquired firms could have survived without the external cash injection, not if they would have gone under. In the latter case, given that greenfield investment was probably not a realistic alternative at that time, M&As may represent a large net gain. If, on the other hand, acquisitions were driven by short-term financial considerations, and acquired assets sold off as soon as markets recovered, the M&As may represent a net cost to the host economy. Clearly it may have been better if the host economy could have obtained other sources of liquidity for local firms and so prevented 'fire sales', even if M&As were allowed later – at better and more stable prices. However, this option may not have been open in the depths of the financial crises, and M&As may have provided very valuable injections of finance.

Another risk of M&As applies to non-crisis conditions when the acquired company is broken up and different components are sold at a price higher than the cost of the acquisition ('*asset stripping*'). This may be a sign of capital market imperfections because the market fails to value assets at their true value. However, it may also be a sign, in efficient capital markets, that firms are themselves managing their assets badly. In this case asset stripping may serve a useful economic function: the ill-managed firm may be divided into parts and the viable one may be placed under better management.

Under the heading of 'finance' we can also consider the effects of M&As and greenfield FDI on the *crowding in* and *crowding out* of domestic firms. While a merger or acquisition by definition is the transfer of assets from local to foreign owners (and so lower levels of domestic ownership in the economy), its effects on other local firms may be more beneficial than of greenfield entry. This is because an established local firm will tend to have strong domestic supply linkages than a new foreign entrant. In a liberal trade setting, the former may reduce domestic linkages (with or without foreign take-over) but to the extent that local suppliers are efficient (and over time have learned from buyers) domestic linkages are likely to persist. When local linkages are inefficient and the economy is exposed to foreign competition, there is likely to be a similar reaction between greenfield and M&A affiliates.

The fact that a greenfield investment starts with low local linkages does not, however, necessarily mean crowding out – it just means less local stimulus to potential suppliers. Over the longer term, there is little reason to expect any difference in impact between both modes.

Crowding out can also occur if a foreign firm has privileged access to local factors (capital and skills) relative to local competitors. This is certainly possible, but it can occur with both modes of entry.

3.3 TECHNOLOGY

Technology transfer: To the extent that a foreign investor enters a country to undertake productive activity over the long-term, there is no reason to expect different effects in terms of technology transfer by mode of entry. The TNC is presumably committed to operating efficiently in either case and will do whatever is needed to ensure this. However, a greenfield investment necessarily involves the setting up of a new facility and so new equipment embodying new technologies (though some TNCs may bring in used equipment where this is appropriate to local conditions). Using these new machines and technologies in turn involves the creation of new skills and information. A merger or acquisition involves taking over an existing stock of equipment with an accompanying body of skills, routines and work habits. In some cases, this may mean that M&As involve less efficient technologies to start with, but not always – for instance when existing technologies are better adapted to the local environment or have a strong learning base that allows equipment to operate more efficiently.

Technology upgrading: In terms of upgrading technologies over time, the result can again go either way. An acquired firm may need considerable technological upgrading to bring it to competitive levels, and so may experience relatively rapid change compared to a new facility that is already near technical frontiers. On the other hand, the acquired firm may exhibit organisational inertia because of inherited habits and routines, making it difficult for the TNC to upgrade technologies. The technological move up the value chain is not expected to differ greatly by mode of entry. This move depends on market orientation, local skills and capabilities and corporate strategies (*WIR, 1999*). Whether the TNC acquires a firm or sets up a new one should not make any difference to the outcome. The evidence for Asia and Latin America shows that M&As can indeed lead to considerable technological upgrading. If the acquired firm had built up good research capabilities, this may be used by TNCs to boost R&D.

Technology generation: M&As may lead to the preservation and enhancement of technological capabilities in firms under competitive pressure. This can be a particularly valuable contribution in economies opening up to international competition; and offers a better outcome than greenfield entry that may lead local firms to going out of business and losing

their capabilities altogether. However, M&As may lead to the downgrading of technological (R&D) activity and status in acquired firms. If the acquired firm does not possess technological assets regarded as valuable by the parent company, or the role assigned to it in the global production system is lower than the role it had earlier, M&As can be deleterious to technology. This has been observed in Latin America and Eastern Europe, where affiliates reduce R&D or undertake simpler tasks than they did before, though there are many cases where the opposite has happened, with local research capabilities upgraded and brought to international levels. The real issue is, however, whether the mode of entry makes a difference to the TNC's decision on local technological activity. Given local skills, factor prices and institutions, would an investor who downgrades an acquired firm's R&D have undertaken greater R&D in a greenfield site? There is no strong *a priori* reason to expect this.

It is also possible that an acquisition of a local technological leader allows the foreign firm to strip a local firm of its proprietary technological assets. This is one major reason why many developed countries seek to prevent the take-over of 'national champions' and so preserve locally strong sources of innovation and linkages with research institutions. The case is particularly strong in strategic defence technologies. This risk is certainly present and has to be safeguarded against, though in the context of this paper it applies only to a few advanced NIEs and transition countries.

However, in normal circumstances a TNC acquiring a technologically strong firm will tend to preserve its R&D base and links with local technological sources. While particular technologies and products will certainly be exploited by the TNC system for export or other markets, it would be irrational to kill the goose that lays the research eggs. The more sensible strategy, which most TNCs adopt, is to strengthen local technological effort and linkages (this is Dunning's 'asset seeking' FDI). We should also remember that 'asset seeking' FDI in the United States has been used by NIEs like Mexico, Republic of Korea and Taiwan Province of China to boost their domestic technological base, without damage to the host economy.

Technology diffusion: The outcome in terms of diffusing new technology and knowledge locally depends on the strength and economic efficiency of linkages established by acquired firms. If these are positive, TNCs will retain and strengthen them – in this case M&As will lead to better diffusion than greenfield sites in the short term. If they are inefficient, M&As will lead to less diffusion than before, but there should be then no difference from a greenfield investment.

In sum, the differences in technological terms between the two entry modes will hinge upon the strength and efficiency of technological capabilities built up by the acquired firm as evaluated in a globally competitive context.

3.4 EMPLOYMENT AND SKILLS

Employment quantity: At first sight, a greenfield investment raises employment while an M&A does not; in fact, many M&As in industrial countries result in significant reductions in employment in the acquired firm.[3] However, the picture becomes more complex if other factors and counterfactuals are considered. If the investment is aimed at the domestic market – which is by definition limited– the greenfield investment will (once it enters the market)

[3] We only consider direct employment effects here. Indirect ones depend upon linkages, considered elsewhere.

necessarily reduce the activity of competing firms and so lead to a loss of employment in the latter. At the same time, if the entry raises efficiency and competition in the market, it may create additional employment. If the investment is aimed at (virtually unlimited) export markets, the greenfield venture is likely to add to employment in the short term. The long-term effect of both modes is likely to be similar.

The reduction of employment in an acquired firm may not be a net loss if the local firm was in competitive difficulties and would have gone bankrupt in the absence of the acquisition. M&A entry then represents a net employment gain (even if the number of employees is smaller than before). In crisis-stricken or transition economies, this 'employment preservation' effect is common, and often quite strong (UNCTAD, 2000, forthcoming; Hunya and Kalotay, 2000).

It is not clear, however, that it makes economic sense to tackle the employment issue *at the firm level*. If the economy is growing and labour markets are efficient, the firing of particular employees (who can find alternative employment according to their skills) is not merely irrelevant but desirable for flexibility and dynamism. If the economy is near full employment levels, a greenfield investment simply bids labour away from other firms and may raise wages for the relevant skills. Even if an economy suffers from unemployment and the government wishes to use FDI for employment generation, is not clear that it should prefer greenfield to M&A as a mode of entry. The problem of the counterfactual has already been noted, but there is a more general issue. Problems in employment creation may lie in inflexible labour markets, inappropriate skills, weak competitiveness, wrong trade and competition policies and so on. In these conditions, tackling the symptoms rather than the causes is an inefficient policy solution.

Employment quality: Employment quality refers to wages, employment conditions, gender issues and the like. TNCs generally offer high quality employment, unless they are in low technology export-oriented activities outside the purview of normal labour laws. A greenfield venture is likely in the short run to offer better quality if the inertia associated with acquisition leads the TNC to preserve old work norms in an acquisition. However, this effect is likely to erode if the acquired firm introduces new management practices and technology, and is integrated into the corporate network and culture of the parent. It is possible that the raising of employment quality in a formerly local firm has greater demonstration effects on other local firms than a greenfield affiliate.

Skills: TNCs generally invest more in training than comparable local firms, and tend to bring in more modern training practices and materials. They also bring in expatriates with specialised skills, and tend to strike strong linkages with training institutions and schools. As with employment quality, the difference between the two modes is likely to lie in the short-term inertia associated with the acquisition of a local firm. In the long-term there is no reason to expect any difference in impact.

There is a risk that an M&A results in skilled employees being transferred abroad by the parent. This may be an undesirable brain drain from the host economy (though it may lead to higher welfare and skill creation for the employees concerned and also to the host economy when they return). We should also note that where the host economy has such desirable skills at low cost, TNCs can attract workers abroad by other means. A greenfield venture can bid workers away from other firms and send them abroad, or foreign firms may hire workers without having to invest locally at all. For instance, the substantial movement (often temporary) of software specialists from India to the United States is not mainly by

means of FDI, and certainly not due to acquisitions of local firms. The risk of a net loss of skills by M&As is thus negligible.

3.5 EXPORT COMPETITIVENESS

FDI can be a powerful instrument for developing host countries to exploit their existing comparative advantages and build new advantages, as long as the countries are able to create new skills and capabilities and attract TNCs into higher value activities (*WIR 1999*). In the case of most new export-oriented activities including those located in EPZs, greenfield entry is the only feasible mode since there are no local firms to take over. In the case of existing activities that are oriented to domestic markets and can be restructured to become export-oriented, greenfield and M&A do provide alternatives. It is not clear, however, which mode is more desirable for the host country. The outcome could go either way, depending on the value of capabilities, skills and routines in existing local firms and the cost involved in bringing them to best practice levels. In the long-term, once more, there is little reason to expect any difference by mode of entry.

In countries opening up to globalisation and international competition, M&As can, as noted for technology generation, be an effective means of preserving and upgrading existing capabilities. This has been the case, for instance, with the automotive component industry in Mexico, Brazil and more recently Thailand, where a large number of national firms have been taken over and restructured; the likely counterfactual was bankruptcy. Greenfield entry in this case would also be a way of building competitive facilities, but would imply a greater destruction of local capabilities.

3.6 MARKET STRUCTURE AND COMPETITION

The effect of TNC entry on domestic market structures and competition is unclear. Usual measures like concentration ratios can be misleading as indicators, particularly when economies are open to import competition and TNCs congregate in scale and technology intensive activities. At the same time, the entry of large affiliates (often with giant parents merging with each other in their home countries) poses serious challenges to competition policy. While TNCs may be the leading forces in global competition and M&As may promote competition and restructuring rather than restrict it (Maucher, 1998), there needs to be effective regulation to counteract possible anti-competitive behaviour. The intense scrutiny exercised by industrial countries on their largest companies and their M&As shows how serious the risk is considered.

At first sight greenfield entry appears to promote competition by adding a new facility, while M&As do not, and may reduce it when both firms were present as competitors. The net economic effects are less apparent once contestability and technologies are taken into account. Take some examples. In a protected market, new entry may indeed promote competition (though in small markets the scale of operations may be inefficient); however, in such a market collusion may also be easier. In a market open to import competition and new local and foreign investment, the form of entry need make no difference to effective competition. Where new technologies are being introduced, it may be desirable to have fewer firms that are able to reach achieve minimum economic size and provide the skills and networks to operate competitively. M&As may not reduce competition if the acquired firm would have gone out of business.

The real issue is not so much the mode of entry as the ability of host governments to mount effective competition policy and, in the case of privatised monopolies, effective

regulation. This is now a highly skilled and demanding task. It needs, not a mechanistic application of market share rules, but an informed analysis of technology, scale, market conduct, contestability and consumer interest. With trade and investment liberalization, in fact, competition and regulation policy becomes the main tool in the area of FDI.

Corporate governance: TNCs tend observe the same standards of corporate governance in their affiliates as at home, providing the same standards of disclosure, accounting, protection of shareholder rights and so on. Most developing and transition host countries lack similar standards in their domestic firms, and an advantage of FDI may be the introduction of international standards of corporate governance.

It is likely that M&As are more beneficial in the first instance in this respect than greenfield investments. "Cross-border M&As mean the creation of new stockowners who are interested in the 'bottom lines' and dividends, as well as stock market valuations of their newly acquired businesses. Effective corporate governance and full financial disclosures are thus naturally demanded and required." (UNCTAD, 2000, forthcoming) While greenfield entry also provides good corporate governance in the affiliates, M&As offer the additional benefit that they involve (in cases where foreign ownership is partial) local shareholders *directly* in the process. The spillover, demonstration and learning effects are likely to be greater.

4. CONCLUSIONS

There do exist differences between TNC entry by greenfield and M&A in terms of the impact on host economies, most of which manifest themselves in the *short term*. The general presumption that greenfield investment is 'better' than M&A is not supported by the analysis, particularly if realistic counterfactuals are used. The outcome remains contingent on particular circumstances.

In a globalising and liberalising world with rapid technical change, M&As are integral to the process of restructuring that enterprises and economies are undergoing all over the world. The fact that they involve local enterprises directly in the process is often seen as undesirable, but this may be precisely their advantage – they allow local capabilities to be preserved and enhanced rather than dispersed or destroyed. In periods of crisis or transition, M&As may be the only way to inject foreign resources and enable economies to adjust to new circumstances. The fact that acquired firms provide an element of inertia may be an advantage to the host economy in that existing linkages, skills and business practices can be preserved to the extent that they are efficient.

The potential costs of in M&As are mainly as follows. They may downgrade local capabilities or drain them away from the host country. Efficient practices and linkages may be destroyed if they do not fit into the corporate culture or strategies of the parent TNCs. Inefficient elements of inertia may slow down the process of restructuring and technology transfer or development. Competition may be reduced in markets with low levels of contestability. Employment may be reduced. Assets may be purchased at unrealistic prices in fire sales or stripped for purely financial gain.

It is not clear how large the costs of M&As actually are and if they are symptoms of larger policy or structural problems in host economies. Many of the costs turn out to be smaller than appear at first sight or founded on mistaken analysis. Clearly, deeper and more rigorous analysis is needed before generalisations can be made with confidence.

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