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THE SHORT- AND LONG-TERM VALUE GAINS TO ACQUIRERS OF EMERGING MARKET TARGETS IN MERGERS AND ACQUISITION DEALS[1]

Emmanuel Okofo-Dartey
Corresponding Author: University of South Africa, South Africa
Email: emmanuelokofodartey@yahoo.com

Lungile Ntsalaze
University of South Africa, South Africa
Email: ntsalaze@unisa.ac.za

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Abstract

This study investigates whether the acquisition of targets from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their profitability and growth opportunities. The study uses firm-level data of 93 listed acquirers of targets from the emerging markets sourced from the Bloomberg Terminal from 2003 to 2018. It employs the difference generalized method of moments (GMM) for analysis. This dynamic panel estimation method takes care of endogeneity problems, omitted variables, and error measurements. The study reveals that, broadly, the acquirers' profitability levels improve in the short-term after merger and acquisition (M&A) deals. This improvement in the acquirers' profitability levels occurs in the 1st, 4th and 5th year periods within the short-term after their M&A transactions are completed. Regarding growth opportunities, acquirers of targets from the emerging markets experience both negative and positive returns on their short-term growth opportunities. However, they experience significant positive returns on their growth opportunities in the long-term. Our paper complements and contributes to the body of knowledge on international market entry and have implication for potential acquirers interested in investment opportunities in the emerging markets.

Keywords: Short-term, Long-term, Acquirers, Targets, Profitability, Growth Opportunities

JEL Classification: C33, G3, G34, L25

1. Introduction

Mergers and acquisitions (M&As) contribute significantly to the efficient allocation of resources in an economy. It is among the most critical investment decisions that firms make (Bhabra and Huang, 2013). For years, however, target firms in M&A activities globally have come from developing economies, while developed market firms have traditionally served as acquirers. For instance, in 2014, as observed by Clifford Chance (2015), cross-border M&A transactions in the

[1] This study is based on the doctoral dissertation entitled “Drivers of Mergers and Acquisitions and Firm Value Growth in Emerging Markets” of the author.

emerging economies saw an increase of more than 25%. Several of the firms initiating these deals were large multinational firms from Europe.

Several reasons are highlighted in the literature as the motivating factors that encourage companies from the other parts of the world to pursue target firms from the emerging markets in acquisition transactions. These factors, among others, include the following; first, the emerging markets provide acquirer firms the opportunity to benefit from the vast untapped-market opportunities in these markets. Second, the emerging markets offer acquirers direct access to natural resources and other raw materials and cheap labor. Third, foreign firms are provided with the needed opportunity to realize higher returns by investing in emerging markets. These acquirer firms propose that they can implement better corporate governance practices and institutional reforms in legal and accounting standards to help improve the value of target firms. There are also few strong contracting institutions in the emerging markets, making it challenging to write enforceable contracts. This provides avenues for developed market acquirers to overcome the weak institutional environments and improve the target firms' value (Chari *et al.* 2010). The fourth reason motivating firms from the other parts of the world to pursue targets from the emerging markets is globalization. Through global integration in information technology, transportation, and communication, people become interconnected with different countries. To achieve these growth expectations, acquirer firms from developed markets continue to identify areas they can obtain lower production costs and opportunities for growth, which the emerging markets often provide (Mentz and Schiereck, 2008). The fifth is the ability of acquirers to bargain effectively in the emerging markets. For instance, acquirers in developed markets may not have strong bargaining power regarding domestic acquisitions than the target firm acquired from the emerging markets. Usually, the improved international acquisitions by acquirers from the developed markets tend to be due to direct policies from the governments of countries of these acquirers designed to facilitate cross-border M&As. This eventually makes acquiring firms realize positive abnormal returns (Fuller *et al.* 2002; Chari *et al.* 2004).

Despite the above factors that encourage acquirers to pursue targets from the emerging markets, several obstacles, including political instability, poor infrastructure, lack of local knowledge, exchange rate fluctuations, and cultural barriers, sometimes limit these acquirers' efforts to expand the emerging markets.

Evidence suggests that firms engage in mergers and acquisitions to gain value gains for the acquiring company (Aybar and Ficici, 2009; Chari *et al.* 2010; Moeller and Schlingemann 2005; Goddard *et al.* 2012). An important question that appears to have been largely overlooked is whether the acquisition of target firms from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their profitability and growth opportunities. This is particularly striking because a primary concern for firms from both developed and emerging countries is acquisitions' impact on their value growth. That is, the value generated from their acquisition deals is what is most important to investors regardless of whether the acquirer is located in an emerging or a developed economy.

Therefore, this paper sets out to investigate whether the acquisition of target firms from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their profitability and growth opportunities. Some previous studies have examined wealth effects of the acquisition of targets in developed and some part of the emerging markets on of acquirer firms and report of a positive or no stock price effects for acquirers and positive effects for targets after examining the impact of M&As on both acquirers and targets (Bris *et al*. 2008; Chari *et al.* 2010; Kuipers *et al.* 2009; Morck and Yeung, 1992). This study considers the post-M&A impact of the acquisition of target firms from selected emerging markets globally. The study expects the acquisition of targets from diverse geographical areas in the emerging markets to have a different impact on acquirers. The emerging and developed markets differ from one another in terms of their economic and legal environments in addition to technology and skill. Further, the emerging markets are a significant economic region of the world, which, according to Atsmon *et al.* (2012), by 2025, the annual consumption in emerging markets will be around $30 trillion. These markets represent the most significant growth opportunity in the history of capitalism (Atsmon *et al.* 2012).

The rest of the paper is organized into four sections explained as follows. The next section reviews the relevant literature on the objective to be investigated. Section 3 explains the methodology adopted to achieve the study's objective while Section 4 presents, interprets, and discusses the results. The last section provides a summary, conclusion, and the policy implications of the study.

2. Literature review and hypotheses development

2.1. Theoretical review

The following theories are applied to investigate whether the acquisition of target firms from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their profitability and growth opportunities.

2.1.1. Market entry hypothesis

The market entry hypothesis adequately explains the acquisition transactions in the emerging market (Zhu *et al.* 2011). This hypothesis put forth that acquirers who engage in cross-border acquisitions use it to enter emerging markets. The differences between emerging and developed markets, like language, the culture, and the legal and political systems, make it impossible for foreign companies to undertake greenfield investments (Zaheer, 1995). Hence, whereas domestic acquirers from the emerging markets usually take over firms that perform poorly and are mismanaged, developed market acquirers become interested in firms that are performing well and are also firmly established in emerging markets (Zhu *et al.* 2011).

2.1.2. Hubris hypothesis

According to Roll (1986), an acquiring firm's management could evaluate a target firm's value incorrectly as an incentive for merger activity when that management is desirous of pursuing an agenda of "empire building''. Hubris hypothesis, therefore, refers to an interest in M&A transaction that can pay more than the actual value of a target's assets because of excessive confidence about the possibility of synergistic value to be derived from the acquisition or the extreme confidence of the management in its capability and competence to manage the target firm better (DePamphilis, 2008). According to Malmendier and Tate (2008), over-confident managers may result in value-destroying acquisitions. If managers' level of confidence increases due to previous acquisitions successes, it could be a reason for the decreasing trend in returns to acquirers. However, Aktas *et al.* (2007) demonstrate that other factors could also account for decreases in acquirers' returns. It may be due to a diminishing pool of suitable targets, learning effects, and costs associated with integrating targets. Therefore, managers tend to overestimate their ability to grab buying opportunities and become too hopeful because of their pride or self-confidence.

2.1.3. Free cash flow theory

Jensen (1986) defines free cash flow as the surplus of cash in the firm after all projects with a positive net present value have been financed. Martynova and Renneboog (2008) state that the availability of excess cash reserves in firms makes managers become bolder and encourages them to potentially undertake value-destroying investments at the expense of those that create value. As a result, managers of firms that have a substantial amount of liquidity will be motivated to use this excess cash flow to make many irrational expenses or undertake activities of M&As, some of them, however, prove to be unprofitable economically. Being aware that substantial cash flows exist, this theory argues that managers are potentially likely to utilize them to undertake M&A operations that are generally considered unfruitful and are likely to affect the value of shareholders adversely. Lin *et al.* (2013) suggest that buyers who have substantial cash flow usually undertake value-destroying deals, which becomes evident through the decrease in firms' performance and earnings to shareholders.

2.2. Empirical review

Despite disagreement about whether M&As create value or not, Malmendier and Tate (2008); Petmezas (2009); and Rau and Vermaelen (1998) maintain that M&As remain a leading global business expansion strategy. However, they present challenges to managers because most acquisitions do not create meaningful shareholder value (nearly 70%), yet building a world-class company through organic growth is almost impossible (Harding and Rovit, 2004).

Perceiving M&As from the perspective of management, several M&A deals become successful whereas others also fail right from the onset before the M&A transactions are finalized (El Zuhairy *et al.* 2015). This situation arises because of the inability of some managers to realize that merging their companies with others goes beyond simply taking possession of capital, premises, equipment, and other assets. To actually make a merger work involves effectively merging or combining human resources, management styles, corporate structure, managing expectations of managers as well as aligning policies.

Scholars identified two major firm growth pathways; thus, the internal and external growth strategies (Dickerson *et al.* 1997). Each of them has several advantages and disadvantages. The internal growth expansion route tends to be slower because firms usually grow using the resources they generate, which may come with their costs. The external expansion growth strategy of which M&A is an example, however, appears to be a more rapid means by which firms can realize growth (Gaughan, 2005) and further reduce costs and gain synergies (LaMattina, 2011). Internal growth limits firms from taking advantage of unexploited market opportunities in contrast to M&As, which is a quicker growth strategy that enables firms to diversify to related markets and to leverage their current capabilities (Bhagat *et al.* 2011; Gaughan, 2005).

Many studies have reported that almost 70 percent to 80 percent of all M&As fail (Bretherton, 2003). Some contend that 53 percent of M&A transactions affect firms' value adversely and do not achieve any financial gains (Shimizu *et al.* 2004). However, literature that discusses the short-term impacts of M&As reveals that they create value, although the target firms realize a more significant percentage of this value. Acquirers from high-tech industries that purchase target firms in industries that are related to experience value destruction. Mantecon (2009) also suggests that shareholders of acquiring firms lost a total of $187 billion in three days around the M&A announcement date, through an investigation of cross-border M&As involving 75 countries. Similarly, Chen and Young's (2010) study of 39 M&As transactions by state-owned firms in China from 2000 to 2008 provides no different outcome than what the previous scholars' results suggest.

Despite the numerous theoretical and empirical reviews pointing to mixed results of both positive and negative impact for acquirers in M&As, several of the prior studies reviewed have concentrated mainly on targets from the developed markets with limited attention focusing on few emerging markets such as China, India, and Brazil. As a result, there is still sparse empirical literature on the impact of the acquisition of targets from the broader emerging markets to these targets' acquirers. Therefore, this makes a case for an investigation into whether the acquisition of target firms from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their profitability and growth opportunities. Based on the preceding discussion therefore, this study hypothesizes that:

H_1: Profitability levels of acquirers of target firms from the emerging market improve in the short-term period after M&A transactions.

H_2: Growth opportunities of acquirers of targets from the emerging markets improve in the short-term after their M&A transactions.

3. Data and methodology

The study uses the firm-level dataset of acquirers of targets from the emerging markets obtained from the Bloomberg terminal from 2003 to 2018. The main reason for the selection of the period is the availability of data. Several countries in the emerging markets during this period experienced a substantial rise in M&A activities because of the implementation of various

regulatory and structural reforms. The dataset consists of annual financial information such as Return on Assets, Cash and equivalents, Networking Capital, Price-to-Book ratio, financial leverage, Tobin's Q, Natural log of Total Assets, and records of M&A deals of acquirers of emerging market targets from Spain, United States of America, Luxemburg, Singapore, Switzerland, Sweden, Germany, Holland, Portugal, Greece, Italy, Mexica, United Kingdom, Chile, Colombia, China, Finland, Kazakhstan, Japan, Philippines, Hong Kong, Austria, Australia, France, India, South Africa, Brazil, and Denmark. The country selection is also motivated by the availability of data. The records of M&A deals cover the date of the announcement, the industry of both the acquiring and target firms, the type of merger, public firms, and mode of payment (cash, equity, or both). For an acquiring firm to be included in the sample, it must be listed firm. Similar to Liu *et al.* (2017), the study included only non-overlapping deals. That is, we excluded acquirers that made multiple acquisitions within a year or consecutive years. Our final sample, therefore, is made up of 93 acquirer firms.

3.1. Description of the variables

3.1.1. Mergers and acquisitions and growth in returns on assets of acquirers

The growth rate in return on assets (GROAs) was used as one of the dependent variables to measure improvement in acquirers' value growth in terms of profitability. Return on assets is an indicator of how profitable a firm is or how efficient management uses its assets to generate earnings. The market for corporate control theory suggests that firms underperforming in an efficient market would either have to increase their profitability levels by acquiring more assets or are potentially likely to become targets, thereby transferring their resources to another more capable management team. This means that underperforming firms are more likely to become targets to financially strong and healthy ones. The impact of firms' growth through M&As on firms' profit levels is an essential factor for acquirers to consider (Kouser *et al.* 2012). Bertrand and Betschinger (2012), after analyzing Russian acquirers' find that, on average, acquisitions reduce the profitability (proxied by ROAs) levels of firms. GROAs is calculated as the difference between ROAs of firm *i* at time *t* and t_{-1} divided by ROAs of firm *i* at time t_{-1} and multiplied by 100. Therefore, this study predicts that the profitability levels of acquirers of target firms from the emerging market will improve in the short-term period after M&A transactions.

3.1.2. Mergers and acquisitions and acquirers' growth opportunities

The growth rate in Tobin's Q (*GTOBQ*) was also used as another dependent variable to measure improvement in acquirers' performance or growth opportunities. Prior studies have made use of Tobin's Q to assess firms' value growth and performance of M&As (Adams and Mehran, 2008; Kammler and Alves, 2010). Firms with low Tobin's Q usually have low growth opportunities expectations, and therefore their counterparts outperform them, which makes them likely targets. *GTOBQ* is calculated as the difference between Tobin's Q of firm *i* at time *t* and t_{-1} divided by Tobin's Q of firm *i* at time t_{-1} and multiplied by 100. Therefore, this study expects that the growth opportunities of acquirers of targets from the emerging markets will improve in the short-term after M&A transactions.

3.1.3. Networking capital and acquirers' gains in M&As

Networking capital is the difference between an acquirer's current assets and current liabilities. Martynova and Renneboog (2008) submit that the availability of excess cash reserves in firms makes managers become bolder and encourages them to potentially undertake investments such as M&As that are value-destroying at the expense of those that create real value. Thus, managers of firms with substantial cash holdings may be encouraged to employ the financial resources available to them to undertake investments such as acquisitions or make irrational and profitable expenses economically. The financial theory also suggests that companies having extra liquidity in the form of excess working capital would potentially engage in investments whose net present

value is negative. Therefore, the study expects a positive relationship between the acquirers' networking capital and their profitability and growth opportunities after their M&A deals.

3.1.4. Total assets (a proxy for firms' sizes) and acquirers' gains in M&As

Total assets are used to measure firm size. The present study uses the natural logarithm of the acquirers' total assets to measure their sizes. Previous studies have used the log transformation of firms' value of total assets as a proxy to measure firms' sizes (Carow *et al.* 2004). The agency theory suggests that acquirer firms' main motivation for mergers and acquisitions is because of self-interest. For instance, a manager may desire to increase firm size rather than maximize shareholders' value since benefits are connected to its size. For instance, as resources under the manager's control increase, his power and control also increase. The study expects a positive relationship between the acquirers' sizes and their profitability and growth opportunities after their M&A deals.

3.1.5. Cash and cash equivalents

The ratio of cash and equivalents over total assets control for idle resources. Some basic indicators assist in distinguishing between M&A deals that create value from those that do not. These indicators may include high pre-acquisition cash balances which serve as a motivation for acquisition deals that aren't well planned which eventually results in poor post-merger performances. According to Tortoriello *et al.* (2016), acquirer firms that have high levels of cash and cash equivalents before deal executions compared to their assets underperform their counterparts by 8.6% over one year and 10.1% over three years. Harford (1999) finds that firms with high cash are more likely to become acquirers than other firms, showing that the market response to an unexpected acquisition announcement is significantly decreasing in the acquirer's excess cash level, but he does not investigate post-acquisition returns. This study, therefore, expects a positive relationship between the acquirers' cash and cash equivalents and their profitability and growth opportunities after their M&A deals.

3.1.6. Financial leverage (FINLEV) and acquirers' gains in M&As

Research on M&A has found that firms with unused debt capacity tend to engage in M&A more frequently than firms with high levels of debt. Leverage is linked to M&As because these growth strategies are expensive and sometimes are externally financed because they may require additional resources beyond what is generated from normal operations (Harrison *et al.* 2014). Harrison *et al.* (2014) examined the relationship between leverage for acquirers, targets, and post-acquisition performance and found that leverage harms acquirers' post-acquisition performance. The negative performance is clustered in acquiring firms, which are already highly geared. They concluded that M&As have a significant and persistent impact on the capital structure, causing a continuous increase in average debt-to-assets of acquirers in post-acquisition periods of up to five years. Financial leverage of firm i at time t−1, which is calculated as total debt/shareholder's equity. Therefore, the study predicts a positive relationship between the acquirers' financial leverage and their profitability and growth opportunities after their M&A deals.

3.1.7. Market-to-book ratio

Merger activity comes in waves, and returns to acquiring firms depend, among others, on the acquirer's book-to-market ratio (Rau and Vermaelen, 1998). The acquirers' market-to-book ratio proxies for management quality and investment opportunities. Prior studies suggest that, in most merger cases, the pre-merger acquirers have lower book-to-market ratios than their targets (Pablo, 2009). Acquirers that have high market valuation as indicated by their market-to-book ratio become successful in deal negotiations. Managers of these acquirer firms are considered to possess superior managerial capabilities than their peers whose market-to-book ratios are low.

Following the preceding discussion therefore, the study predicts a positive relationship between the acquirers' market-to-book ratio and their post-M&A profitability and growth opportunities.

3.2. Econometric model development

The study employed a panel data analysis to investigate whether the acquisition of target firms from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their profitability and growth opportunities. The growth rate in returns on assets (GROAs) was used as one of the dependent variables to measure improvement in acquirers' value growth in terms of profitability. Return on assets is an indicator of how profitable a firm is or how efficient management uses its assets to generate earnings. The growth rate in Tobin's Q was also used as another dependent variable to measure improvement in acquirers' performance or growth opportunities. Prior studies have made use of Tobin's Q to assess firms' value growth and performance of M&As (Adams and Mehran, 2008; Kammler and Alves, 2010). The study also incorporates other firm-specific variables as control variables to take care of other factors that may influence the acquirers to undertake M&As and impact the acquirers' value growth after their M&A transactions. These control variables include the size of the acquirers (total assets), the networking of the acquirers, cash and cash equivalents (a proxy for idle resources), market-to-book (a proxy for acquirer value or management quality and investment opportunities) and financial leverage. Similar to Ohman and Yazdanfar (2018) and Park and Jang (2011), dynamic models below, based on generalized methods of moment (GMM) were developed to investigate whether the acquisition of target firms from the emerging markets impacts the short-term and long-term value gains of acquirers of these targets in terms of their profitability and growth opportunities.

$$GROA_{i,t} = \beta_1 ROA_{i,t-1} + \beta_2 TAS_{i,t} + \beta_3 CASHQ_{i,t} + \beta_4 FINLEV_{i,t} + \beta_5 NETWC_{i,t} + \beta_6 TOBIN_{i,t} + \beta_7 MKBK_{i,t} + \beta_8 Y_2 M\&A_{i,t} + \beta_9 Y_1 M\&A_{i,t} + \beta_{10} Y_1 M\&A_{i,t} + \beta_{11} Y_2 M\&A_{i,t} + \beta_{12} Y_3 M\&A_{i,t} + \beta_{13} Y_4 M\&A_{i,t} + \beta_{14} Y_5 M\&A_{i,t} + \beta_{15} Y_6 M\&A_{it} + \beta_{16} Y_7 M\&A_{i,t} + \beta_{17} Y_8 M\&A_{i,t} + \beta_{18} Y_9 M\&A_{i,t} + \beta_{19} Y_{10} M\&A_{it} + \varepsilon_{i,t} \quad (1)$$

$$GTOBIN_{i,t} = \beta_0 TOBIN_{i,t-1} + \beta_2 TAS_{i,t} + \beta_3 CASHQ_{i,t} + \beta_4 FINLEV_{i,t} + \beta_5 NETWC_{i,t} + \beta_6 TOBIN_{i,t} + \beta_7 MKBK_{i,t} + \beta_8 Y_2 M\&A_{i,t} + \beta_9 Y_1 M\&A_{i,t} + \beta_{10} Y_1 M\&A_{i,t} + \beta_{11} Y_2 M\&A_{i,t} + \beta_{12} Y_3 M\&A_{i,t} + \beta_{13} Y_4 M\&A_{i,t} + \beta_{14} Y_5 M\&A_{i,t} + \beta_{15} Y_6 M\&A_{it} + \beta_{16} Y_7 M\&A_{i,t} + \beta_{17} Y_8 M\&A_{i,t} + \beta_{18} Y_9 M\&A_{i,t} + \beta_{19} Y_{10} M\&A_{it} + \varepsilon_{i,t} \quad (2)$$

where; '*it'* denotes acquirer '*i*' at time '*t'*. Models 1 and 2 were used to estimate the value growth of the acquirers' growth in terms of their profitability (which is proxied by their ROAs) and opportunity growth or performance (which proxied by Tobin's Q). The study incorporated year dummies in the models to capture whether emerging market targets' acquisition impacted the acquirers' profitability and growth opportunities in the short-term or long-term. Year dummies $\beta_8 Y_2 M\&A_{i,t}$, *and* $\beta_9 Y_1 M\&A_{i,t}$ capture the level of the acquirers' profitability and growth opportunities two years before the M&A deals. $\beta_{10} Y_1 M\&A_{i,t}$, $\beta_{11} Y_2 M\&A_{i,t}$, $\beta_{12} Y_3 M\&A_{i,t}$, $\beta_{13} Y_4 M\&A_{i,t}$ *and* $\beta_{14} Y_5 M\&A_{i,t}$ capture the impact of acquisition transactions on the acquirers' profitability and opportunities for growth in the short-term (1 to 5 years) period post-M&A deals while $\beta_{15} Y_1 M\&A_{i,t}$, $\beta_{16} Y_2 M\&A_{i,t}$, $\beta_{17} Y_3 M\&A_{i,t}$, $\beta_{18} Y_4 M\&A_{i,t}$ *and* $\beta_{19} Y_5 M\&A_{i,t}$ assess the long-term (6 to 10) impact of the acquisition transactions of the acquirers. Like Beccalli and Frantz (2009), the year of the deal itself is left out of the analysis as it can be considered as a transition period, which is usually strongly affected by the accounting practices regarding M&As. Lastly, the following firm-specific variables *TAS*, *NETWC, CASHQ, FINLEV* and *MKBK* representing the natural logarithm of total assets (a proxy for acquirer size), the networking of the acquirers, cash and cash equivalents (a proxy for idle resources), financial leverage and market-to-book (a proxy for management quality and investment opportunities) were included as control variables while β_0 - β_{19} are the coefficients to be estimated, respectively, and $\varepsilon_{i,t}$ is the error term.

The study used GMM in first difference to estimate models (1) and (2) above. This GMM estimation technique takes away the firm-specific effects and removes the correlation between the lagged dependent variable $y_{i,-1,}$ the individual firm effects ηi and the other right-hand-side variables. Specifically, it stated as:

$$\Delta Y_{it} = \gamma \Delta Y_{it-1} + \beta^{I} \Delta X_{it} + \Delta \varepsilon_{it} \quad (3)$$

The study preferred the GMM in first differences to the Ordinary Least Squares (OLS) estimation technique because the lagged dependent variable also forms part of the independent variables in models (1) and (2). OLS regressions of such equations produce inconsistent and biased estimates because the independent variables are not independent of the error term.

GMM in first differences was also considered superior to other alternative approaches of estimating models (1) and (2) like the least squares dummy variables (LADV) and fixed effects. Although the fixed effects estimator eliminates the firm-specific effects ηi by using the "within transformation", it does not eliminate bias. GMM takes care of this problem by using the lagged dependent variable ($y_{i,-s}\, for\ s \geq 2$) in level as instruments.

Arellano and Bond (1991) proposed two estimators: the one-step estimator and the two-step estimator (henceforth termed GMM1 and GMM2, respectively). GMM2 is the optimal estimator. GMM1 turns out to be optimal when the residuals are homoscedastic. If there is heteroscedasticity, GMM1 of instrumental variables continues to be consistent; however, carrying the estimation in two steps increases efficiency. The one-step, GMM1, can be found by using

$$A_{1N} = \left(\frac{1}{N}\sum_{i=1}^{N} Z_i^{*\prime}\, HZ_i^{*}\right) - 1 \quad (4)$$

where; H is a T – 2 square matrix with twos in the main diagonals, minus ones in the first sub diagonals, and zeros otherwise. The two-step, GMM2, is found by letting

$$A_N = \left(\frac{1}{N}\sum_{i}^{N} Z_i^{*\prime}\, \Delta\hat{\varepsilon}_i \Delta\hat{\varepsilon}_i' Z_i^{*}\right) - 1 \quad (5)$$

where; $\Delta\hat{\varepsilon}$ = $\Delta\hat{\varepsilon_i}$…,$\Delta\hat{\varepsilon_{iT}}$ are the residuals from a consistent GMM1 of Δy_i.

4. Results and discussion

The study investigated whether the acquisition of target firms from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their profitability and growth opportunities. Two variables comprising return on assets (ROAs) and Tobin's Q were used as surrogates of the acquirers' performance in profitability and growth opportunities. The study also considered a range of firm-specific variables that could motivate acquirers to undertake M&A deals and also have an impact on their value growth. Table 1 presents the descriptive statistics of the variables.

Table 1. Descriptive statistics

Variables	Obs.	Mean	Std. Dev.	Max	Min
$ROAs_{it}$	1048	11.548	78.642	1405.554	-125.645
$FINLEV_{it}$	1044	1.224	1.297	14.231	-0.991
$LTAS_{it}$	1049	10.054	2.382	17.586	0.180
$CASH_{it}$	1049	7.081	2.328	13.602	-1.404
TOBIN'S Q_{it}	1034	0.360	0.404	3.688	-0.752
$MKBK_{it}$	1038	0.730	1.178	11.105	-3.020
$NETWC_{it}$	535	5.983	2.504	14.946	-0.726

Notes: Column 1 refers to the two main independent variables of ROA_{it} (a proxy for profitability) and TOBIN'S Q_{it} (a proxy for growth opportunity) and the control variables used in the study. These control variables are $FINLEV_{it}$, $LTAS_{it}$, $CASH_{it}$, $MKBK_{it}$ and $NETWC_{it}$, representing the financial leverage, cash and cash equivalence, market-to-book ratio and networking capital.

The results presented in Table 1 reveal a mean value of 11.548 for ROAs with minimum and maximum values ranging from -125.645 to 1405.554, respectively, and high variability regarding the standard deviation. The average value of Tobin's Q showing the acquirers' growth opportunities is 0.360. It has a minimum score of -0.752% and a maximum 3.688% score, suggesting a low possibility of value growth for acquirers of emerging market acquirers after their M&A deals. The acquirer's average size was 10.054, whereas the maximum and the minimum sizes of the acquirers were 17.586 and 0.180. Regarding the acquirer's financial leverage levels, the average was 1.224%, with a maximum and minimum values of 14.231% and -0.991%. This suggests that some acquirers had relatively high levels of debt.

Regarding the acquirers' market-to-book ratio showing management quality and the acquirers' market value, the results show an average ratio of 0.730, suggesting that most of the acquirers were managing their firms well. Concerning the cash and equivalents, Table 1 shows that, the average is 7.081 while the maximum and minimum values range from 2.328 to 13.602. The acquirers' networking capital also reveals an average value of 5.983 and a maximum and minimum values of 14.946 and -0.726. This indicates the availability of several of these acquirers' liquid resources for investment activities such as mergers and acquisitions.

Table 2 presents the correlation analysis describing the level of relationships among the variables.

Table 2. Correlation analysis

	ROAs	FINLEV	LTAS	CASH	TOBIN	MKBK	NETWC	VIF
ROAs	-1.00							1.114
FINLEV	-0.003	1.00						5.147
LTAS	0.004	-0.391	1.00					1.297
CASH	-0.147	-0.351	0.925	1.00				2.512
TOBIN	0.168	0.441	-0.322	-0.312	1.00			3.166
MKBK	-0.014	0.831	-0.367	-0.317	0.728	1.00		7.870
NETWC	-0.016	0.231	0.656	0.596	-0.062	0.146	1.00	2.475

From the results in Table 2, it can be observed that the relationship between ROAs and Tobin's Q is positive but not strong (r=0.168). The acquirers LTAS also has a positive relationship with their ROAs (r=0.004). However, the FINLEV, CASH, MKBK, and NETWC all have negative relationships with ROAs. The results reveal that the Tobin's Q has a positive relationship with the FINLEV but is negatively related to LTAS and CASH. Further, the results from Table 2 indicate that the other variables' correlation results are not strong, implying no presence of multicollinearity. Even though the results show CASH and LTAS as well as MKBK and FINLEV to be highly correlated at (r= 0.925) and (r=0.831) respectively, a robustness check by the variance inflation factor (VIF) however confirms results of all the variables to be less than 10 as suggested by Salmeron *et al.* (2018) which indicates no presence of multicollinearity. This suggests that the variables used for the estimation do not pose multicollinearity problems. As GMM is a normality-free approach, stability tests and serial correlation tests weren't issues to be concerned about as they are taken care of already.

4.1. Regression results

Table 3 provides results of whether the acquisition of target firms from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their profitability. Based on hypothesis 1, Model 1 was developed for the estimation. Model 1 estimates the impact of the acquisition of target firms from the emerging markets on the profitability levels

(proxied by ROAs) of these targets' acquirers. A GMM in the first difference estimation technique was used for the analysis.

Table 3. Impact of M&A transactions on acquirers' profitability

Variable ***ROAs***	**Coefficient**	**SHORT-TERM** (1-5 years Post-M&A transaction)	**Coefficient**	**LONG-TERM** (6-10 years Post-M&A transaction)	**Coefficient**
$ROAs_{t-1}$	1.168*** (0.168)	Year 1	4.335***	Year 6	6.405***
$LTAS_{it}$	3.703*** (1.164)	Year 2	1.255	Year 7	0.192
TOBIN'S Q_{it}	15.667*** (1.850)	Year 3	1.028	Year 8	-2.313
$FINLEV_{it}$	0.035 (0.201)	Year 4	2.419***	Year 9	1.749
$CASH_{it}$	1.142*** (0.366)	Year 5	3.117***	Year 10	0.291
$NETWC_{it}$	0.955*** (0.183)				
$MKBK_{it}$	3.815*** (0.560)				
DIAGNOSTICS					
Observations	1049				
Instruments	53				
AR 2	0.1724				
Hansen J-Statistics Prob.	0.1272				

Notes: Table 3 shows dynamic panel analysis results using difference GMM methods to investigate whether the acquisition of targets from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their profitability levels. Standard errors are provided in parenthesis below the coefficients of estimates *, ** and *** represent 10%, 5%, and 1% significance, respectively.

Source: Author's estimation based on data collected

In Model 1, the coefficient for the lagged ROAs (a proxy for profitability) is positive and statistically significant at 1%, suggesting that the previous year's profit levels of the acquirers are essential in explaining the acquirers' current profit positions.

The study predicted in hypothesis (H_1) that the profitability levels of acquirers of target firms from the emerging market improve in the short-term after M&A transactions. Consistent with the above hypothesis, the profitability levels of acquirers of targets from the emerging market largely improve in the short-term after M&A transactions, even though the improvement in the acquirers' profitability levels does not occur in all the years within the short-term period. This study shows that the acquirers' profitability levels immediately improve in the 1st year after the M&A transactions. However, it does not continue in the 2nd and 3rd years. This may be due to the post-M&A integration process, which is suggested to be slow and time-consuming after M&A deal is completed (Miczka and Grosler, 2004). The acquirers' profitability levels subsequently start to improve again in the 4th and 5th years, still within the short-term periods. Cultural integration and synergistic gains that result in value creation after acquisition transactions are generally completed in the first three years after mergers and acquisitions, but actual synergy and value creation may take a long time to be achieved (Miczka and Grosler, 2004). This positive impact of the acquirers' M&A deals on their profitability levels in the short-term even extends to the 1st year of the acquirers' long-term period and then ceases. This means that the acquirers do not

experience any value gains in terms of improvements in their profitability levels in the long-term after M&A transactions.

On the effects of the control variables on the acquirers' profitability levels, the acquirers' total assets' coefficient is positive and statistically significant at 1%. This suggests that an increase in the acquirers' sizes may improve their profitability levels, all other things being equal. As the acquirers expand in sizes through their acquisitions of targets from the emerging markets, it encourages them to invest more in different areas to increase their profit levels in line with what the financial theory suggests. This finding corroborates Lee's (2009) views that firm size positively impacts their profitability levels.

The acquirers' coefficient of Tobin's Q denoting their growth opportunities is positive and statistically significant at 1%. This means that the improvement in the acquirers' performances could increase their profitability levels, all other things being equal. This is contrary to the previous assertion by Mateev and Anastasov (2010) that there is a negative relationship between ROAs (a proxy for profitability) and firm growth.

Regarding the acquirers' financial leverage, the coefficient is also positive but statistically insignificant, suggesting that the acquirers' debt levels do not affect their profitability levels. Further, the study result found the acquirers' cash and equivalent representing coefficient for their idle resources to be positive and statistically significant at 1%. This indicates that any possible improvement in the acquirers' cash positions resulting from their acquisition of targets from the emerging markets could increase their profitability levels. The positive relationship between the acquirers' cash and equivalent their profitability could also mean that an increase in the acquirers' idle resources gives them an indication that they can invest them in activities such as M&As as a business expansion strategy for value creation in terms of improvement in profitability levels. This finding, however, runs contrary to the views of Oler (2005) that acquirers with high cash balances often suffer negative post-acquisition returns, implying that the negative news usually associated with acquirers that have high cash balances are not completely incorporated by the market in the determination of the stock price of the acquirer during the announcement but only responds to poor operating performance after deal completion.

The acquirers' coefficient of networking capital was also found to be positive and statistically significant at 1%. This means that an improvement in the acquirers' networking capital position may positively impact their profitability levels. When corporate liquidity increases, it improves firms' ability to undertake several investment activities, including acquisitions to improve their profitability positions, all other things being equal. This finding appears to corroborate what the financial management principle stipulates that high investment in the working capital elements can lead to an increase in a firm's performance in terms of cash flow and profitability (Yeboah and Yeboah, 2014).

Lastly, concerning the market-to-book ratio denoting the quality of the acquirers' management and their market valuations, the coefficient is positive and statistically significant at 1%, showing that a high market valuation of the acquirers or the quality of their management is important that could impact on the acquirers' value gains in terms of their efforts to improve on their profitability levels, all other things being equal. This is because potential acquirers highly valued in the market can attract targets with excellent prospects for growth and increased profitability. This sharply contradicts Rutkowski's (2018) view that acquirers have a lower return on assets (ROAs), representing their profitability. He suggests that, however, serial acquirers more quickly increase their assets and achieve a higher sales growth rate than the remaining companies.

In terms of the robustness and validity of the results, the probability of the AR2 results is insignificant (P-value = 0.1724) which suggests the absence of serial correlation in Model 1. Additionally, the results show that the Hansen J test is insignificant (P-value = 0.1272), implying that the instruments do not suffer from misspecification.

The next section below continues with discussion and analysis on whether acquirers of targets from the emerging markets experience value gains in terms of improvement in their growth opportunities in the short-term after their acquisition transactions. Table 4 presents results of the impact of the acquisition of targets from the emerging markets on acquirers of these targets to determine whether they experience any gains in terms of improvement in their growth

opportunities or performances in the short-term or long-term after these deals. Based on the hypothesis, Model 2 was developed for the estimation. Model 2 estimates the impact of target firms' acquisition from the emerging markets on the growth opportunities or performances (proxied by their Tobin's Q) of acquirers of the targets. A GMM in the first difference estimation technique was used for the analysis.

Table 4. Impact of M&A Transactions on Acquirers Growth Opportunities

Dependent Variable ***TOBIN'S Q***	**Coefficient**	**SHORT-TERM** (1-5 years Post-M&A transaction)	**Coefficient**	**LONG-TERM** (6-10 years Post-M&A transaction)	**Coefficient**
TOBIN'S Q_{t-1}	0.0746*** (0.0127)	Year 1	-0.0464***	Year 6	-0.0133
$LTAS_{it}$	-0.1079*** (0.0315)	Year 2	-0.0054	Year 7	0.0507*
$ROAs_{it}$	0.0609*** (0.0172)	Year 3	0.0405**	Year 8	0.0980***
$FINLEV_{it}$	-0.0099*** (0.0041)	Year 4	-0.0045	Year 9	0.0875***
$CASH_{it}$	-0.0018 (0.0093)	Year 5	0.0338	Year 10	0.0831***
$NETWC_{it}$	-2.34E-08 (2.23E-08)				
$MKBK_{it}$	0.1568*** (0.0151)				
DIAGNOSTICS					
Observations	1049				
Instruments	53				
AR 2	0.2021				
Hansen J- Statistics Prob.	0.2273				

Notes: Table 4 shows dynamic panel analysis results using difference GMM methods to investigate whether the acquisition of targets from the emerging markets impacts the short-term and long-term value gains of these targets' acquirers in terms of their growth opportunities. Standard errors are provided in parenthesis below the coefficients of estimates *, ** and *** represent 10%, 5% and 1% significance, respectively.

Source: Author's estimation based on data collected.

Table 4 shows that the lagged Tobin's Q coefficient is positive and statistically significant at 1%. This indicates that the previous year's Tobin's Q is significant in explaining the current year's Tobin's Q. and the acquirer firms' present growth opportunities very much depend on their previous growth potentials.

Hypothesis 2 predicted that growth opportunities of acquirers of targets from the emerging markets improve in the short-term after their M&A transactions. Contrary to hypothesis (H_2), the result of this study shows that acquirers of targets from the emerging markets experience mixed value gains of negative and positive impact on their growth opportunities in the short-term after M&A deals. The negative impact occurs immediately in the first year after deals are completed while the positive impact is realized in the third year period of the short term. The possible reason why the acquirers do not realize immediate value gains right after M&A deals are completed could be the slow process of integrating the two firms to make one entity. Due to the differences in culture and other independent characteristics of both the acquirer and the target before the

acquisition transaction, immediate wealth effects are not usually realized right after the acquisition transactions.

However, acquirers experience a significant positive impact on their value gains in terms of their long-term growth opportunities. This positive impact starts from 7th to 10th years in the long-term. This is because capturing post-merger opportunities always takes longer than anticipated (El Zuhairy *et al.* 2015). This may be that a merger or an acquisition involves integrating the human resources, including the corporate structure, management styles, employee expectations, and policies, which takes some time to complete for actual gains to begin to emerge. Also, other challenges which serve as hinderances must also be taken care of to ensure rapid growth. Integrating two previously separate firms is a process which is time-consuming, and the actual integration that will create the required synergy is also a difficult task to achieve (David and Singh, 1994). Apart from that, restructuring of the acquired firm takes some time. There may be some sectors of the two businesses that overlap with one another which require streamlining (Park and Jang, 2011). This finding is consistent with Mager and Mayer-Fackler (2017) and Dutta and Jog (2009), who suggest a significant and positive long-term post-acquisition performance for acquirers.

Turning to the control variables' effects on the acquirers' growth opportunities after acquiring targets from the emerging markets, this study provides evidence of a negative but statistically significant at 1% for the acquirers' total assets (a proxy for the acquirers' sizes). The acquirers' total assets' positive sign suggests that increases in the acquirers' sizes by acquiring targets from the emerging markets do not necessarily result in improved performances or abilities to grow, all other things being equal. This is because, if the acquirers acquire targets with low growth potentials simply to increase their sizes in the form of empire-building efforts, it may negatively affect their future growth prospects. This finding, however, departs from the assertion by Adetunji and Owolabi (2016), who find a negative relationship between firm size and growth opportunities and suggest that investors do not consider firm size to affect firms' growth and market performance positively.

The return on assets (ROAs) coefficient measuring the acquirers' profitability levels was positive and statistically significant at 1%, indicating that increases in the acquirers' profitability levels may positively impact their growth opportunities. This possibly means that an increase in the acquirers' profit levels, to a large extent, has the potential to influence them to undertake investment activities such as M&As in order to improve on their overall future performances. This perfectly ties in with the view that firms expand their operations to enhance profitability, and profits can be used to grow the firm's asset base.

The study's result found the acquirers' financial leverage to be negative but significant statistically at 1%. This means that any possible increase in the financial leverage positions of acquirers of emerging market targets as a result of their acquisition of these targets may negatively affect their abilities to grow after M&A deals, all other things being equal. This may be because some of the targets may be highly geared, yet they have been acquired because of other positive characteristics they have. However, if these acquired targets are not properly integrated to complement the acquirer adequately, it may result in negative returns to these acquirers. This finding broadly confirms the views of Bouraoui and Li (2014) that leverage changes harm performance, in both the short and long run after mergers and acquisitions, indicating that acquirers' debt levels contribute to post-merger performances.

The acquirers' cash and equivalents (a proxy for the acquirers' idle resources) were found to be negative but statistically significant at 1%. This implies that any possible increase or decrease in the acquirers' cash and equivalents levels may not contribute positively to improve on their growth potentials. A significant reason for this is that the availability of excess cash reserves to firms makes managers bolder and encourages them to potentially undertake value-destroying investments at the expense of those that create value. As a result, managers of firms that have a substantial amount of cash will be motivated to use this excess cash to make several irrational investment activities such as M&As (Martynova and Renneboog, 2008).

Further, the acquirers' networking capital's coefficient was also found to be negative but statistically significant at 1%. This suggests that increases in the acquirers' networking capital positions may not necessarily improve the acquirers' growth or performances. The possible

reason could be that managers of firms with high financial resources or free cash flow, if not adequately monitored, could engage in investment activities that are detrimental to the growth of the acquirer firms as the free cash flow theory suggests.

Lastly, the market-to-book ratio (a proxy for the acquirers' market value as management quality) of the acquirers was positive and statistically significant at 1%. This indicates that the acquirers' relatively high valuation because they acquire targets from the emerging markets could help the acquirers improve on their future growth or performances, all other things being equal. The high valuation of the acquirers indicates the quality of the acquirers' managements' investment abilities, which makes them able to acquire targets that could positively help their future growth.

In terms of the results' validity and robustness, the difference GMM estimation for this study is reasonably satisfactory and robust. The test of second-order serial correlation AR (2) shows that the estimations have no problem of second-order serial correlation since the AR (2) test statistics is unable to reject the null of no second-order serial correlation (p-values = 0.2021) for Model 2. The Hansen test for over-identification indicates the null of exogenous instruments is not rejected (p-values = 0.2273) for Model I, implying that the instruments do not suffer from misspecification.

5. Conclusion and policy implications

This paper aims to investigate whether the acquisition of target firms from the emerging markets impacts the short-term and long-term value gains of acquirers of these targets in terms of their profitability and growth opportunities. Using an unbalanced panel of 93 listed acquirers of targets from the emerging markets over the period 2003-2018, the results from the difference GMM model show that, the profitability levels of acquirers of targets from the emerging markets immediately improve in the 1st year after the M&A transactions. However, it does not continue in the 2nd and 3rd years. Subsequently, however, these acquirers' profitability levels start to improve again in the 4th and 5th years, which are still within the short-term period. This is because cultural integration and synergistic gains, which result in positive returns for the acquirer firms after M&A deals, are generally completed in the first three years after acquisitions. The actual value creation or gains to acquirers of targets from the emerging markets may even take a much more extended period to achieve.

Regarding the impact of the acquisition on the acquirers' growth opportunities, we conclude that acquirers of targets from the emerging markets experience negative and positive returns on their growth opportunities in the short-term period after M&A deals. The negative effect occurs immediately in the 1st year after deals are completed, while the positive effect also occurs in the 3rd year period of the short-term. However, in the long-term, the acquirers experience a significant positive impact on their value gains in terms of their growth opportunities. The possible reason for this could be that the post-M&A integration is a time-consuming process, and the real integration required to achieve faster growth is challenging after M&A deals (Park and Jang, 2011). Besides, it also takes time to restructure the acquired firm to achieve positive gains in the short-term. Therefore, we recommend that potential acquirers of targets from the emerging and other markets do not use M&As to achieve only profitability and growth purposes. However, they should use them to create other value types, such as risk minimization through product or market diversification or cost efficiency and market power enhancement. Our paper complements and contributes to the body of knowledge on international market entry and have implication for potential acquirers interested in investment opportunities in the emerging markets. This study is limited to acquirers of targets from the emerging markets only. Thus, it cannot be generalized to acquirers of targets in other markets of the world. Future studies should analyze the short- and long-run performance of M&As for acquirers from the emerging markets.

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