THE INFLUENCE OF ACQUIRER CSR ON INVESTOR REACTION IN CROSS-BORDER ACQUISITIONS BY EMERGING MARKET ACQUIRERS

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ABSTRACT

We analyze the influence of acquirer CSR performance on acquirer announcement returns for a sample of 545 transactions, in which acquirers from emerging countries purchased targets from developed markets. Drawing on stakeholder theory, we argue that emerging market acquirers with higher CSR performance experience more favorable investor reactions upon acquisition announcement. We furthermore posit that this CSR performance-investor reaction relationship is more pronounced in acquisitions characterized by larger institutional or cultural distances between the acquirer and target's countries.

Keywords:

corporate social responsibility, cross-border acquisitions, emerging market acquirers

INTRODUCTION

When companies from emerging markets try to acquire targets in developed countries, they are regularly met by considerably skepticism from various stakeholders in the developed countries such as politicians, employees, and the media (Tingley et al., 2015). The latter's concerns typically revolve around negative perceptions and stereotypes regarding inferior ethical, governance, and regulatory standards of emerging countries (Zhou & Guillén, 2015). This often leads to a "liability of foreignness" (Aybar & Ficici, 2009) for emerging market acquirers impeding a prospective acquisition. One remedy in such a situation could be the ability of a company to signal "trustworthiness" (Barney & Hansen, 1994). Prior research has identified CSR as a way to prove such trustworthiness since a company with high CSR performance has demonstrated conduct that goes beyond a mere adherence to minimal regulatory and legal requirements (Boubakri et al., 2016).

But above phenomenon is also interesting from the perspective of M&A research. Most prior studies on cross-border M&A have focused on acquirers from developed countries (cf., Bhagat, Malhotra, & Zhu, 2011). In contrast, despite their growing economic and societal importance little research has been conducted on emerging market acquirers, especially those targeting companies from developed markets (c.f., Tao et al., 2017). Furthermore, most M&A studies have found a negative investor reaction for an acquirer when announcing an acquisition (cf. e.g., Datta, Pinches, & Narayanan, 1992; Haleblian et al., 2009; King, Dalton, Daily, & Covin, 2004). This highlights the importance for M&A research to further explore the phenomenon of emerging countries acquirers as well as to try to identify firm characteristics leading to a more favorable investor reaction for acquirers. We address both these gaps by analyzing the influence of an emerging market acquirer's CSR performance on the reaction of its investors when announcing the acquisition of a target from a developed market.

Drawing on stakeholder theory (Waddock & Graves, 1997; Roberts & Dowling, 2002), we argue that having a track record of strong CSR performance is indicative of the willingness and ability to cater to multiple factions, which enables emerging market acquirers to gain the trust of both with their own investors and in the developed market. Consequently, their investors expect acquirers with strong CSR performance to being able to overcome the liability of foreignness and thus assess the focal acquisition more favorably. When exploring the boundary conditions of this acquirer CSR performance-investor response relationship, we furthermore posit that CSR become more influential in acquisitions the larger the institutional and cultural distances between the acquirer and target's countries are.

To test those hypotheses, we analyze a sample of 545 cross-border acquisitions from 2000 to 2014, in which a public acquirer from an emerging market purchased a developed market target. While we find significant average positive announcement returns for the emerging market acquirers, we are unable to empirically observe above hypothesized relationships regarding the influence of CSR performance.

Our study contributes to the literature in several ways. First, we add to stakeholder theory in the context of CSR (Waddock & Graves, 1997; Roberts & Dowling, 2002) by providing a rationale how strong historical CSR performance functions as a signal of trustworthiness for a company when interacting with various factions. Second, we contribute an interesting extension to the bootstrapping hypothesis from research on spillover effects in M&A (cf., Goergen & Renneboog, 2008; Martynova & Renneboog, 2008; Bhagat et al., 2011) by arguing that acquirers with strong prior CSR performance receive a more favorable investor reaction as opposed to those authors expecting acquirers with weaker governance standards to receive a more positive investor reaction when targeting companies in markets with higher standards. Third, our lack of observing a clear empirical influence of CSR performance could also be interpreted as support of the extant

literature on CSR, which has largely yielded ambiguous findings on the relationship of CSR and various aspects of firm performance (cf. Malik, 2015).

The remainder of this study is organized as follows. In the next section, we review the relevant literature on cross-border M&A and CSR before developing our hypotheses. Subsequently, we present our empirical research design and results before finishing with a discussion of our findings.

BACKGROUND AND HYPOTHESES

In Study 2, we outlined that most researchers report negative reactions to the acquirers' stock prices upon acquisition announcements (cf. e.g., Datta, Pinches, & Narayanan, 1992; Haleblian et al., 2009; King, Dalton, Daily, & Covin, 2004), which leads research to a particular interest in settings as well as firm characteristics with a more favorable investor assessment.

With respect to settings, cross-border M&A have long been such a potentially promising constellation. While most research has not observed substantial performance differences between cross-border and domestic M&A, these studies predominantly focused on acquirers from developed countries pursuing cross-border acquisitions (cf., Bhagat, Malhotra, & Zhu, 2011). Little research, however, has been conducted on emerging market acquirers (c.f., Tao et al., 2017). This distinction is important since prior research has also found evidence that acquirers from countries with low corporate governance standards are met with a more favorable investor reaction when targeting companies from countries with higher corporate governance standards due to the anticipation of bootstrapping spillovers (Martynova & Renneboog, 2008).

With respect to firm characteristics, little research has hitherto studied the influence of CSR performance on acquisition performance. Deng et al. (2013) find that acquirers with a higher CSR score exhibit a higher likelihood of merger completion, higher combined merger announcement returns, and a stronger long-term financial performance. Aktas et al. (2011) observe a positive relationship between CSR scores of target companies and acquirer's announcement returns. Gomes and Marsat (2018) as well as Qiao and Wu (2019) find that target CSR is positively associated with bid premiums.

To the best of our knowledge, however, no study so far has examined the influence of CSR performance in a cross-border M&A setting involving acquirers from emerging countries targeting companies from developed markets. This is surprising since prior research has identified CSR

performance as a firm characteristic influencing a broad range of other company actions and outcomes (cf. e.g., Aguinis & Glavas, 2012; Malik, 2015). Examples include company performance and investor perception (e.g., Cochran & Wood, 1984; Margolis & Walsh, 2003; Orlitzky, Schmidt, & Rynes, 2003; Waddock & Graves, 1997), access to financing (Cheng, Ioannou, & Serafeim, 2014), cost of equity as well as analyst coverage and dedication of institutional investors (Dhaliwal, Li, Tsang, & Yang, 2011), company reputation (Brammer & Pavelin, 2006; Fombrun & Shanley, 1990), quality of employees (Turban & Greening, 1997), higher brand equity and level of consumer satisfaction (Lev, Petrovits, & Radhakrishnan, 2010).

The link between CSR performance and investor response in cross-border M&A

Conducting cross-border M&A is complex and challenging – especially for acquirers from developing countries (Li, Wang & Kuo, 2019). Most research supports the notion that companies from developed markets both have a longer history of and adherence to higher governance and CSR standards (cf. Husted, 2015; Liang & Renneboog, 2017). For instance, Ioannou and Serafeim (2012) report that financial, social welfare, and labor right protection systems are on average better in developed markets than in their emerging counterparts. In addition, some further concerns may also arise from generally negative stereotypes in developed markets about inferior developing country governance and regulatory standards (Zhou & Guillén, 2015). In their pursuit of acquiring developed market targets, acquirers from emerging countries hence frequently face a "liability of foreignness" (Aybar & Ficici, 2009) that includes being perceived as being not trustworthy. Consequently, these acquirers often encounter resistance from key stakeholders (e.g., public, politicians, and regulators) in the target countries that could derail or prevent an acquisition as well as impede subsequent post-merger integration along the way.

A strong CSR performance is one way to signal such "trustworthiness", a characteristic already identified in prior research as source of a potential competitive advantage by Barney and Hansen (1994). By achieving high CSR performance, a company has demonstrated conduct that goes beyond a mere adherence to minimal regulatory and legal requirements (Boubakri et al., 2016). Thus, emerging market acquirers may be able to demonstrate a willingness and ability to comply with target countries' norms and expected conduct and hence ultimately gaining legitimacy with target countries' critical stakeholders (Li et al., 2019).

Furthermore, this trustworthiness also extends directly to the acquirer's own shareholders. Being typically a major pursuit requiring considerable management attention, cross-border acquisitions may create concerns among the emerging market shareholders as well as other incumbent stakeholders that existing long-term relationships will be jeopardized in favor of the new endeavor (Deng et al., 2013). The stakeholder theory perspective on CSR (Waddock & Graves, 1997; Roberts & Dowling, 2002) explains that companies with high CSR performance have a proven history of being able to take into consideration and manage such multiple and conflicting demands and interests. Consequently, investors of acquirers with high CSR performance are less concerned of being neglected in favor of new factions and thus view an announced cross-border acquisition more favorably.

In summary, we argue that by creating a sense of trustworthiness both with target stakeholders as well as the companies' own shareholders, emerging market acquirers with better CSR performance are met with a more favorable investor response from their own shareholders. Our *Hypothesis 1* hence reads:

Hypothesis 1: Emerging market acquirers with higher CSR performance are, on average, associated with a more positive investor response by their shareholders.

In the previous section we outlined why a company from an emerging market faces a "liability of foreignness" (Aybar & Ficici, 2009) when pursuing a target from a developed country and how an acquirer's CSR provides a remedy for such foreignness, leading to a more positive assessment of the announced acquisition by its investors. Two key sources of this foreignness are differences in the institutional (cf., Xie, Reddy & Liang, 2017) and cultural environment (cf., Beugelsdijk et al., 2018). The former comprises the regulatory and political environment, the latter is shaped by the population's attitudes regarding aspects such as power distance, uncertainty avoidance, individualism, masculinity, long-term orientation, and indulgence (Hofstede, 2001). The liability of foreignness for an acquirer increases the more dissimilar the countries in the focal acquisition are. Thus, we expect acquirer CSR performance to be more influential in acquisitions characterized by larger institutional or cultural distances. Hence, *Hypotheses 2* and *3* state:

Hypothesis 2: The CSR performance-investor response relationship is more pronounced for larger institutional differences between the acquirer and target's countries of origin.

Hypothesis 3: The CSR performance-investor response relationship is more pronounced for larger cultural differences between the acquirer and target's countries of origin.

METHODS

Sample and data collection

Our final sample for subsequent hypotheses testing consists of 545 acquisitions with a minimum deal value of 5 million USD announced between the beginning of 2000 and end of 2014, in which a public acquirer from an emerging market purchased a developed market target. We furthermore only included transactions with CSR data for the acquirer being available from Thomson Reuter's Asset4 database. We obtained M&A data from Thomson ONE, market returns and company financial data from Datastream, and data on CSR from Asset4.

Measures

Dependent variable

Acquirer CAR. To assess market reaction to an M&A announcement, we follow prior research's dominant approach of using event study methodology (cf. Haleblian et al., 2009; Hayward, 2002; Laamanen et al., 2014; McNamara, Haleblian, & Dykes, 2008). We calculate cumulative abnormal returns (CAR) over a three-day window [-1; +1] around the date of an acquisition's announcement.

Explanatory variables

Acquirer CSR. Asset4 annually processes 900 data points to calculate 250 key performance indicators for each company covered. These key performance indicators are further organized into 18 categories within the four pillars (1) environmental performance score, (2) social performance score, (3) corporate governance score, and (4) economic performance score. We follow Cheng et al. (2014) in creating an equally weighted composite index of the first three pillars (i.e., environmental, social, and corporate governance) to capture an acquirer's CSR performance. Since

Asset4 scores are already lagged by one year due to being based on prior's year data, we use the acquirer company scores from the year of the focal acquisition when constructing *Acquirer CSR*.

Institutional differences. To create a measure for institutional differences between the acquirer and target's host countries, we draw on the "Institutions" indicator from the Global Competitiveness Report provided by the World Economic Forum (WEF). This indicator assesses the quality of a country's both public and private institutional environment on a scale of 1 to 7 with respect to property rights, public ethics and corruption, undue influence, government efficiency, security, corporate ethics, and corporate accountability. We calculate *Institutional differences* as the difference between the target country score and the acquirer country score.

Cultural differences. Following broad research convention, we base our measure for *Cultural differences* on Hofstede's (2001) cultural composite index factoring in power distance, uncertainty avoidance, individualism, masculinity, long-term orientation, and indulgence. We calculate the difference between the target country score and the acquirer country score for each of above six factors and then use the arithmetic mean over these six factors as *Cultural differences.*

Control variables

In our hypotheses testing, we include multiple standard control variables identified by prior research as being influential on acquisition announcement returns. Specifically, we control for (1) *Acquirer leverage* as total debt to total assets*,* (2) *Diversifying acquisition* as a dummy variable equaling 1 if the primary SIC division of target and acquirer differ*,* (3) *Public target* as a dummy variable equaling 1 if the target is a publicly listed company*,* (4) *Deal size* measured as acquisition value in USD billion*,* (5) *Method of payment* as a dummy variable equaling 1 if the acquisition is paid with cash only.

RESULTS

Descriptive statistics

Table 1 (see appendix) depicts the means, standard deviations, and pairwise correlations for all variables used in our analysis. No concerningly high correlations among our explanatory and control variables emerged, which is in line with our regression diagnostics that resulted in each variance inflation factor (VIF) being below the commonly accepted threshold of 10 (Neter, Wasserman, & Kutner, 1985). We furthermore conduct event study analysis and find that the mean *Acquirer CAR* for the three-day event window (–1, +1) is 0.44 percent and significant ($p < 0.05$).

Hypotheses testing

To test our hypotheses, we employ multiple regression analysis with robust standard errors clustered at the acquirer firm level to control for acquirers conducting multiple acquisitions within our sample. We furthermore include a year trend variable to account for temporal effects. Following Aiken, West, and Reno (1991), we mean-center the independent and moderator variables prior to calculating the interaction terms to facilitate their interpretation.

Table 2 (see appendix) provides the results of our further regression analysis. All models include *Acquirer CAR* as the dependent variable. Model 1 displays the base model including only the control variables. In Model 2, we introduce our explanatory variable *Acquirer CSR,* but do not find a significant relationship and thus reject Hypothesis 1. In Models 3 and 4 we introduce the interaction terms of *Acquirer CSR* with *Institutional differences* and *Cultural differences*, respectively, but do not find significant relationships and thus reject Hypotheses 2 and 3. Model 5 displays the full model.

DISCUSSION AND CONCLUSION

This study examines the influence of acquirers' CSR performance on their announcement returns in cross-border M&A, specifically the case of acquirers from emerging markets bidding for targets from developed countries. Drawing on stakeholder theory, we explain how CSR performance helps acquirers from emerging markets to overcome their liability of foreignness (Aybar & Ficici, 2009) when targeting companies from developed countries by generating trust both with their own investors and in the target country. We furthermore explore contingency factors and argue that an acquirer's CSR performance is increasingly beneficial in achieving a positive investor reaction the more the institutional and cultural environments differ between the focal emerging and the developed countries.

Empirically, we observe significant positive announcement returns for the emerging market acquirer when announcing the acquisition of a target from a developed country. We do not, however, find empirical support for above notions that the acquirer's CSR performance influences that positive investor reaction.

Theoretical and practical contributions

Despite the few empirical findings, our study still contributes to research as well as practice. With respect to the latter, we provide encouragement for emerging market companies to pursue acquisitions in developed markets as indicated by our observation of a favorable investor reaction.

Regarding our study's contribution to research, we extend the perspective of stakeholder theory on the role of CSR (Waddock & Graves, 1997; Roberts & Dowling, 2002) by providing a rationale how strong historical CSR performance functions as a signal of trustworthiness for a company when interacting with various factions. In addition, we provide an interesting twist to the literature on the role of spillover effects in M&A (cf., Goergen & Renneboog, 2008; Martynova &

Renneboog, 2008; Bhagat et al., 2011): While these authors present a bootstrapping hypothesis that acquirers with weaker governance standards may receive a positive investor reaction by bonding themselves to countries with higher standards via acquisitions, we argue that in the case of CSR strong prior performance is beneficial for conducting an acquisition in markets with higher standards and is thus accompanied by a more favorable investor reaction. Last, our lack of observing an empirical influence of CSR performance could also support the ambiguous role of that phenomenon in prior research, which has often struggled to clearly identify an either positive or negative influence of CSR on various aspects of firm performance (cf. Malik, 2015).

Limitations of this study and avenues for future research

Our study also has several limitations. First, while we observe an on average positive investor reaction for an emerging market acquirer when announcing an acquisition in a developed market, we empirically fail to find support for any contribution of CSR to that favorable investor assessment. One reason therefor could be the still rather limited availability of data on emerging market companies with respect to CSR, leading to our sample of 545 acquisitions over 14 years. Reassessing our hypotheses at a later stage once more data becomes available could lead to significant findings. Second, due to the paucity of data we also chose to focus on the role of acquirer CSR performance without simultaneously considering the target's CSR performance. As our own Study 2 has demonstrated, however, target CSR has important theoretical as well as empirical influences. Most research on the role of CSR in M&A performance has hitherto been limited to either acquirer or target CSR (e.g., Aktas et al., 2011; Deng et al., 2013), a limitation hopefully addressed by future research. Third, we focused on the reaction of an acquirer's investors as measured by announcement returns. When developing our hypotheses, we argued that acquirers with strong CSR performance are better suited to build trust and cater to various factions in adverse

environment. This could also well translate to other outcomes of M&A such as rate and speed of deal completion or various other aspects of post-merger integration.

In conclusion, we expect CSR as well as cross-border acquisitions by emerging market acquirers to remain – and increasingly become – relevant topics, both for academia and management. With our study, we hope to have added some interesting initial insights into the intersection of these two promising fields.

TABLE 1

Means, standard deviations, and correlations[a]

	Mean	s.d.	1	2	3	4	5	6	7	8	9
1 Acquirer CAR [-1;1]	0.44	4.73	1.00								
2 Acquirer CSR	45.10	25.72	-0.03	1.00							
3 Institutional differences	0.98	0.58	0.00	-0.02	1.00						
4 Cultural differences	24.18	9.66	-0.05	-0.03	0.00	1.00					
5 Acquirer leverage	0.52	0.21	-0.08	0.05	-0.05	-0.05	1.00				
6 Diversifying acquisition	0.28	0.45	0.00	-0.10	0.10	-0.06	0.02	1.00			
7 Public target	0.18	0.39	-0.09	0.00	0.07	0.07	0.09	-0.08	1.00		
8 Deal size	0.34	0.93	-0.11	0.08	0.12	0.07	0.05	-0.09	0.32	1.00	
9 Method of payment	0.91	0.28	0.00	-0.04	-0.07	0.08	0.04	-0.05	-0.01	-0.01	1.00

[a]N = 545. Values greater (smaller) than .07 (-.07) are significant at $p < .05$.

TABLE 2

Results of regression analysis[a]

Acquirer CAR [-1;1]	(1) Controls only	(2) Direct effect	(3) IA with Institutional differences	(4) IA with Cultural differences	(5) Full model
Acquirer CSR		-0.00371	-0.00377	-0.00325	-0.00332
		(0.00723)	(0.00722)	(0.00723)	(0.00722)
Acquirer leverage	-1.453*	-1.429*	-1.424*	-1.538*	-1.533*
	(0.859)	(0.846)	(0.847)	(0.848)	(0.849)
Diversifying acquisition	-0.184	-0.203	-0.203	-0.211	-0.207
	(0.441)	(0.447)	(0.452)	(0.451)	(0.456)
Public target	-0.813*	-0.824*	-0.871*	-0.701	-0.746
	(0.492)	(0.492)	(0.487)	(0.500)	(0.495)
Deal size	-0.000442***	-0.000433***	-0.000439***	-0.000430***	-0.000434***
	(0.000156)	(0.000158)	(0.000167)	(0.000157)	(0.000164)
Method of payment	0.476	0.441	0.440	0.519	0.508
	(1.012)	(1.000)	(1.006)	(1.004)	(1.010)
Institutional differences			0.115		0.0796
			(0.312)		(0.312)
Acquirer CSR x Institutional differences			-0.0135		-0.0123
			(0.0111)		(0.0111)
Cultural differences				-0.0137	-0.0126
				(0.0210)	(0.0211)
Acquirer CSR x Cultural differences				0.00132*	0.00129
				(0.000797)	(0.000793)
Year trend	-0.110	-0.111*	-0.110*	-0.101	-0.101
	(0.0669)	(0.0664)	(0.0661)	(0.0660)	(0.0658)
Constant	1.457	1.654	1.546	1.908	1.816
	(1.054)	(1.092)	(1.186)	(1.205)	(1.283)
Observations	545	545	545	545	545
R-squared	0.028	0.028	0.030	0.034	0.035

[a] N = 545. Unstandardized regression coefficients are reported with standard errors in parentheses. *** p<0.01, ** p<0.05, * p<0.1.

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