

Leading Comprehensive Internationalization: Strategy for Action

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Abstract

Internationalization strategies have interested scholars for since several decades. They have developed many theories about their causes, motivations, nature, outcomes etc. Starting from existing literature we explore the changing geography of international business that has led academics and practitioners to rethink cross-border Mergers & Acquisitions (M&A). This phenomenon raises an interesting question regarding factors that influence cross-border deals. The paper presents new insights in literature and discusses results of some case study on this topic.

Key Words: Business, Geography, Internationalization strategy.

Introduction

One of the most visible outcomes of the XXI century transformation of world economy is the rise of dynamic Asian countries. Consequently, Asian companies are becoming powerful actors of change in the global landscape achieving an international dimension through cross-border M&A. In 2013 the emerging economies comprised 28% of global deals and was dominated by China. Cross-border investment policy is made in a political and economic context that has been affected by challenges of current crisis. These challenges have increased the complexity of whole M&A process, from due diligence until post closing stage, accentuating the relevance of elements such as timing, planning, visioning, management and execution skills.

Chinese firms have made considerable progress in rethinking to M&A strategies integrating themselves into the traditional channels and institutions of international trade and finance. They are becoming more and more expert in acquiring developed economy firms. Despite of the relevance of this topic, little empirical analysis investigates factors driving firms domiciled in Asian countries to make M&A deals. To fill this literature gap, we discuss some cases that involve Chinese corporations as both bidder and target.

General framework

The geography of international business is defined, and periodically redefined, on the base of firms' processes of selection of markets in which to operate. Firms can operate simultaneously on different markets to achieve global profit (Schweiger and Goulet, 2000; Haspeslagh and Jemison, 1991). Global profit can be realized through price discrimination on many markets, economies of scale between

interdependent activities and accounting practices able to reduce the incidence of taxation (Carbonara and Caiazza, 2008a, 2008c).

Selection of countries in which firms aim to operate is based on economical, socio-cultural and political benefits (De Noble et al., 1988; Bastien, 1987; Napier et al., 1993; Schweiger et al., 1993; Schuler et al., 2004). The economic benefits concern the cost and availability of inputs and intermediate goods, the market dimension and the quality of infrastructure (Morosini, 1998; Dealscape, 2009; Ranft and Lord, 2002; Howell, 1970; Lindgren, 1982a; 1982b). The socio-cultural advantages concern the cultural closeness to original country in term of language, uses and habits. Finally, the political benefits concern the stability, the Government's attitude towards FDI (Carbonara and Caiazza, 2009a, 2009b, 2009c; Schweiger et al., 1994; Marks, 1991a, 1991b; Schweiger and Denisi, 1991).

On the base of firms' selection of markets in which to operate through FDI each country become net-exporter of FDI if outward are higher than inward or net-importer in the other case (Caiazza et al., 2013; Buono and Bowditch, 1989). A Net Outward-Inward (NOI) is expressed as the differential between the stock of direct investment abroad (outward) and those received (inward) (Dunning et al., 1998; Dunning 2005). According to the Investment Development Path of Nations (IDP theory) each country across five different levels of development based on the levels of economic development and Net Outward-Inward level (Dunning, 1979; Dunning and Narula, 1996).

This perspective evidences that the country ability to attract FDI is based on the combination of ownership, location and internalization benefits that companies can enjoy in it (Aguilar et al., 2009; Cartwright and Cooper, 1990; Carbonara and Caiazza, 2010). More specifically, the theory predicts that the countries with prevalence of labor intensive activities, with non-specialized work force and with an economy based on the exploitation of raw materials will have an higher number of inward than outward FDI (Haspeslagh and Farquhar, 1994; Dionne, 1988; Burke, 1987).

The first stage of development characterizes countries that have a low GDP and have not country specific resources able to attract foreign investors (Carbonara and Caiazza, 2008b). These countries have a low level of inward and outward FDI. In the second stage inward FDI starts to grow, while the outward remain low and in the third stage it is possible to see a decline in the rate of inward FDI while the outward growth. At fourth stage the country is net exporter of FDI. In the fifth stage there is a decline in FDI flow abroad, which in the long term lead to situation of net importer of FDI.

China is an interesting case that shows the changing geography of international business. In a few years, the country has gone from first to fourth stage of development. From areas in which foreign investments were made for acquiring cost advantages has become a country able to invest abroad. This article presents some case studies aimed to evidence the new role of China's firms in the global scenario.

Methodology

Although research on internationalization has received increased attention in recent years, very little research has been carried out on M&A between Chinese and Western firms. Considering the exploratory nature of our research objectives, we present some case study for highlighting the main challenges in these cross-border M&A. To build an initial understanding of the case, we first conducted web-based database research (Google Scholar, ProQuest, Wiso-net, etc.). Then we verified our findings with several external consultants and scholars to refine our analysis.

Case Study

Diageo is the world's leading premium drinks business with an outstanding collection of beverage alcohol brands across spirits, beer and wine. These brands include Johnnie Walker, Crown Royal, J&B, Windsor, Buchanan's and Bushmills whiskies, Smirnoff, Ciroc and Ketel One vodkas, Baileys, Captain Morgan, Jose Cuervo, Tanqueray and Guinness. The marketing, sales and distribution of the brands are organized across five geographic regions: Diageo North America; Diageo Europe; Diageo Latin America & Caribbean; Diageo Africa; and Diageo Asia-Pacific. The company is listed on both the London Stock Exchange (DGE) and the New York Stock Exchange (DEO). In 2011, the European Diageo launched a mandatory takeover offer for Swellfun, the holding company which was 39.7% owned by Quanxing and distillers of Shuijingfang, a premium baijiu spirit that prides itself on being one of China's oldest liquors.

The deal was complex from many reasons. In order to allay prospective regulatory concerns, Swellfun proactively spun off a controlling 55% interest in its Quanxing Distillery subsidiary that produces another brand of Baijiu called Quanxing Daqu. The divestment was primarily aimed at countering potential issues thrown up by Chinese foreign investment regulations stating that domestic famous and high-quality white spirit brands should remain in Chinese hands. Shuijingfang was on the national list of the 'Intangible Cultural Heritage of China' because its distilling techniques reportedly date back to the 14th century, meaning that once this had been divulged, regulators had to return to consult the rule books yet again. However, over the intervening period, Chinese regulatory agencies worked hard to educate foreign investors on how to acquire in China, bolstered their own domestic deal-making institutions and attached a greater visible importance to attracting inbound deal flows and during which Diageo received the final thumbs-up from Chinese regulators.

The senior management teams at Diageo and Swellfun, and their advisors formulated a well-planned M&A strategy in order to alleviate any concerns regulatory authorities might have had over the takeover. At the same time, they remained completely resolute during the one-year-four-month regulatory review period, preparing contingency plans in case the authorities rejected the transaction and saying little to the press despite intense media interest in the deal. Swellfun shares dropped close to 10% as rumors spread that certain institutional investors had an insight into the outcome of the regulatory review process and were selling their Swellfun holdings in advance. In summary, foreign investors looking to acquire in China would be wrong to think that big-ticket inbound transactions of well-known Chinese brand names are now becoming the norm as opposed to the exception. The deal took a considerable amount of time to gain antitrust approval highlights the time that investors may need to allow to complete a transaction, particularly when there are valuable brands in question. However, this particular deal did much to open up doors and break down misconceptions about acquiring a business in China. Both bidder and target worked together in order to mitigate regulatory risk prior to applying for clearance, and remained fully committed to the transaction amidst growing uncertainty over its ultimate outcome.

China National Cereals, Oils and Foodstuffs Corporation (COFCO) is one of China's state-owned largest food processing, manufacturer and trader. Between 1952 and 1987, it was the sole agricultural products importer and exporter operating under direct control of the central government. Besides the foodstuff business, COFCO has developed itself into a diversified conglomerate, involving planting, cultivation, food-processing, finance, warehouse, transportation, port facilities, hotels and real estate. COFCO has four companies listed in Hong Kong, namely, China Foods, China Agri-Industries Holdings, Mengniu Dairy, and COFCO Packaging Holdings and three companies listed in mainland China, namely, COFCO Tunhe, COFCO Real Estate, and BBKA. COFCO boasts a wide range of branded products and service portfolios, such as Fortune edible oil, Great Wall wine, Mengniu dairy, Lohas fruit and vegetable juice, Le Conte chocolate, Tunhe tomato products, Joycome meat products, Joy City shopping mall, Yalong Bay resorts, Gloria hotels, Snow-Lotus cashmere, Zhongcha tea products, COFCO-Aviva Life Insurance, COFCO

Trust, etc. Tully Sugar is one of the Australian last grower-owned milling companies with a production line that delivers a quarter of a million tons of premium grade sugar every year.

In 2011, Bunge, COFCO and Mackay Sugar, a local sugar producer who already held 4% in the target, all put forward formal offers for acquiring Tully Sugar. COFCO approached the pre-bid stage of the deal diligently, personally approaching Tully shareholders and offering them the same price that Bunge had previously offered. However, Bunge raised its offer while COFCO were anxiously waiting for regulatory approval from Australia's Foreign Investment Review Board (FIRB).

However, with Tully shareholders showing increased interest in Bunge's offer document, COFCO upped the stakes and their offer, again putting Bunge and Mackay on the back foot and forcing them to reciprocate, which they did just days later. Finally, COFCO got the result it was looking for: a board recommendation to its shareholders urging them to accept COFCO's offer. From then on in, the ball was in COFCO's court. By the 18th July 2011, COFCO had acquired a 99% stake in the target and was therefore entitled to acquire the remaining share in Tully on mandatory basis.

COFCO evidenced that acquirer has to stay close to its target. Even though it was every bidder's aim to win the support from the target's board, only COFCO managed to win Tully's senior management over at a critical juncture during the bid process. COFCO pro-actively grew relationships with all its stakeholders, from local and regional associations through to its contracted exporter QSL. Such a strong bond ultimately meant that COFCO extended the bidding period so as to help individual shareholders split their tax arrangements over two fiscal years. COFCO adopted also an inclusive approach from the outset, a move which finally paid off in the end. As the acceptance deadline neared, Bunge, who COFCO had maintained a 'good working relationship' with, threw in the towel and offered its 6.9% interest in Tully to COFCO, allowing the latter to build a momentum for full take-over and pocketing the former, a tidy profit.

COFCO evidenced also that it is likely to engage the local community face-to-face. To some Tully shareholders, what made COFCO's bid stand out was their personable approach to the acquisition, with shareholders commenting that the cocktail party at the pre-bid document signing ceremony did a lot to break the ice between the local community whose lives had revolved around the mill, and their new owners. Furthermore, COFCO also hired a local firm who monitored local market and community dynamics during the bid process, which allowed the bidder to move quickly to quell any market or community rumors that might adversely sway opinion against it. Finally, COFCO's efforts in engaging local populations impacted by the proposed takeover paid off with the local newspaper grudgingly praising COFCO for their professionalism and offering its support going forward.

Conclusions and Discussion

This article explores the recently visible and interesting phenomenon of changing geography in cross-border M&A. It discusses the strategic motivations and challenges of this process. It presents and discusses some case study of recent cross-border M&As involving Asian firms aimed to identify main challenges and strategic actions.

The first case evidenced that firms have to recognize the potential asset leverage, cost efficiencies and new opportunities in order to set up the appropriate post-merger structure that will reap anticipated synergies. In addition, they should understand the regulatory environment of both companies and reconcile them, give careful thought to potential deal structures in order to anticipate tax issues and antitrust considerations, consider collaboration between management groups and develop a public relations strategy.

The second case evidenced that is important to move quickly and decisively. As the timeline demonstrates, COFCO looked to move quickly allowing it, by and large, to dictate the pace of events to its liking. And when the situation looked to be getting complex, it moved decisively, increasingly its bid and going unconditional simultaneously in order to take the sheen of previous offer. Perhaps the lesson that cross-border M&A acquirers fail to heed the most often is that regulatory approvals take time and in that intervening period, a bid can very easily collapse. COFCO was well aware of this eventuality, and went to great pains to mitigate its affect.

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