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# The Influence of Liabilities of Origin on EMNE Cross-Border Acquisition Completion

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## Introduction

A recent, and an increasingly salient, trend in the global business landscape has been the rapid rise in outward foreign direct investment (FDI) by multinationals from emerging economies such as India and China. The percentage of total world outward FDI from emerging economies grew from just 5 % in 1990 to a substantive 34 % in 2014 (UNCTAD, 2015). Emerging-market multinational enterprises (EMNEs) have been following trajectories different from those predicted by dominant theoretical perspectives on internationalization. One of these differences is a

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preference for high-commitment entry modes, such as acquisitions in heterogeneous geographies; this is contrary to the path of incremental internationalization predicted by the Uppsala model (Johanson & Vahlne, 1977). In fact, the cross-border acquisition (CBA) has been recognized as one of the key entry modes for emerging-economy firms, with the value of these acquisitions growing from US$9.5 billion in 1990 to US$152 billion in 2014, accounting for a record-high share of 38 % of the total M&A activity across the globe (UNCTAD, 2015). Scholars have theorized that EMNEs undertake acquisitions in order to obtain strategic assets, such as cutting-edge technology, or global brands, in order to compensate for lack of these conventional firm-specific advantages (Luo & Tung, 2007; Mathews, 2006; Contractor, 2013). Acquisitions may also be used as a means to overcome liabilities of origin, such as underdeveloped institutions in the home country, inadequate managerial capabilities, and the lack of global reputation (Child & Rodrigues, 2005; Bonaglia, Goldstein, & Mathews, 2007; Madhok & Keyhani, 2012). However, a question that has yet to be asked, and the focus of this study, is that, while CBAs may help EMNEs traverse the reputation barrier and gain global capabilities, to what extent do these liabilities of origin influence acquisition completion?

This question becomes interesting in light of reports that some EMNE acquisitions are not delivering the anticipated synergies (Karnani, 2012). Further, the abandonment rate of acquisitions is fairly high among EMNEs, with one estimate at 53 % for Chinese firms and 33 % for Indian firms, for CBAs made between 2000 and 2008 (Sun, Peng, Ren, & Yan, 2012). The reasons behind these low deal completion rates are not yet clear. Most studies on deal completion have focused on the influence of factors such as target firm performance, quality of the bid, ownership, deal structure, bid premiums, and size, and have generally involved MNEs from advanced economies (e.g., Holl & Kyriazis, 1996; King, Dalton, Daily, & Covin, 2004). In fact, there has been surprisingly little research on the factors influencing EMNE deal completion. In one of the few studies on this topic, Zhang, Zhou, and Ebbers (2011) investigated the influence of institutional quality, type of target industry, and firm type on deal completion among Chinese firms, and found that

deals involving targets in sensitive industries or located in countries with lower institutional quality had a lower likelihood of deal completion. In addition, if the acquiring firm was a Chinese state-owned enterprise, then the likelihood of success was also lower than for private companies.

Understanding the factors that influence deal completion is important, as the failure to complete acquisitions is associated with substantial costs, both financial and in terms of managerial opportunity (Dikova, Sahib, & van Witteloostuijn, 2010). Furthermore, failed attempts can also lead to long-term psychological costs, as managers may feel discouraged from attempting subsequent acquisitions (Thomas, Eden, Hitt, & Miller, 2007). Semadeni, Fraser & Lee, (2008) found that CEOs who fail to close M&A deals may face stigmas in their careers.

This study becomes particularly important, given both the increasing participation of EMNEs in cross-border M&A activity and the high failure rate of acquisitions, even among multinationals from advanced economies (AMNEs). The failure rate of AMNEs has been reported as anywhere in the range of 40–75 % (Cartwright & Schoenberg, 2006; Marks & Mirvis, 2011; Sirower, 1997). Given that AMNEs have been shown to have such a low success rate in acquisitions, even without facing origin-linked liabilities, our contention is that EMNEs will face even greater challenges in their CBAs. In other words, the success of the deliberate strategic choice of CBAs as a means of overcoming EMNEs' liabilities of origin may itself be impacted by these liabilities.

## The Liabilities of Origin

The term "liabilities of origin" was first used by Bartlett and Ghoshal (2000), to describe the cognitive liabilities of over- and under-confidence faced by EMNE managers in their efforts to go global. Ramachandran and Pant (2010) further investigated the concept of liabilities of origin (LOR), and identified three factors leading to LOR: underdeveloped institutions, the absence of organizational global experience, and the negative stereotypes that prevail for products and institutions from emerging markets. While the influence of origin-linked factors, such as

underdeveloped institutions and a lack of firm-specific advantages, on the internationalization of firms from developing countries was investigated in the early literature on EMNEs (e.g., Lall, 1982; Lecraw, 1977), these disadvantages were not looked at in the context of acquisitions. This is logical, given that cross-border M&A activity by EMNEs was very limited prior to 2000. The empirical research on the liabilities of origin has so far been limited, and has focused mainly on the issue of legitimization strategies used by EMNEs in response to the LOR that they face when internationalizing (Pant & Ramachandran, 2012; Bangara, Freeman, & Schroder, 2012; Klossek, Linke, & Nippa, 2012). Little is known about the impact of LOR on EMNE acquisition completion. It is our premise that the CBA experience of EMNEs is likely to be different from that of their advanced-economy counterparts, largely because of their LOR. In addition to the disadvantages caused by underdeveloped institutions and limited global experience, EMNEs' lack of legitimacy and status may also impact acquisition completion. The role of status becomes particularly interesting when EMNEs take over firms in developed countries, as it helps us to investigate a hitherto-unexplored paradox, namely, what happens when the traditional hierarchical positions of acquirer and target firms are reversed? In other words, what happens when the acquiring firm has a lower status than the target firm, because of its origin in an emerging economy? In the M&A literature, the lower status or relative standing of target firm managers has been shown to create conflicts and cause executive departures, adversely impacting performance (Hambrick & Cannella, 1993). Relative status could thus play an important role in influencing the success of an acquisition.

The rest of the chapter is structured as follows. We draw upon theoretical insights from the literature on institutions, organizational learning, and organizational status to build our conceptual model. We then develop hypothesis relating to the influence of the different dimensions of LOR on the CBA process. This is followed by a description of the methodology. We detail the results of this analysis and its implications, and conclude with a discussion on the limitations of our study and directions for future research.

# Theory and Hypotheses

## The Advantages and Disadvantages of MNEs

Dominant theoretical perspectives on international business, such as Dunning's Eclectic Paradigm, or OLI framework (e.g., Dunning, 1988), have focused on MNEs' ownership-specific, location-specific, and internalization-specific advantages that pertain to internationalization. Rugman and Verbeke (2003) posited that EMNEs internationalize to expand on their firm-specific advantages (FSAs), which they define as unique capabilities proprietary to an organization, such as technology, managerial, and marketing skills. Scholars have proposed that, while EMNEs may not possess conventional FSAs, they possess other advantages, such as resilience, frugality, embeddedness within family businesses and conglomerates, a large and technically competent workforce, and tolerance for ambiguity (e.g., Guillen & Garcia-Canal, 2009; Rugman & Li, 2007; Contractor, 2013).

There have been attempts to extend or adapt existing internationalization theories to improve their relevance to EMNEs. For example, in the linkage, leverage, and learning model, Mathews (2006) presented an adaptation of Dunning's OLI framework, suggesting that MNEs from Asia are able to expand internationally by accessing resources through linkages to external firms, leveraging these resources, and subsequently engaging in a process of learning from repeated application of linkage and leverage. While the importance of EMNE-specific *advantages* cannot be denied, it is our contention that, in spite of these advantages, EMNE liabilities of origin could still lead to constraints in their internationalization. These liabilities of origin are faced by EMNEs, in addition to the liability of foreignness that is faced by all foreign firms. The liability of foreignness is defined as the additional costs an MNE operating in a market overseas incurs that a local firm would not (Zaheer, 1995), and has been widely investigated in the IB literature; see Denk, Kaufmann, and Roesch (2012) for a review.

## Liabilities of Origin Versus the Liability of Foreignness

Theoretical perspectives on the disadvantages faced by MNEs in their host countries can be traced back to Stephen Hymer's classical study, which stated that firms faced additional costs when doing business abroad (Hymer, 1976), including relative production costs; the costs of managing operations at a distance; and the costs of managing negotiations, monitoring, and dispute resolution with different stakeholders. Additional costs include discrimination hazards faced if the host country governments favor local firms, and unfamiliarity hazards that can be attributed to lack of knowledge of the local market (Eden & Miller, 2001). Zaheer (1995), building on this concept, included the cost of multinationality—the cost of managing operations at a distance—as a liability of foreignness (LOF), and excluded the relative production costs in the definition of LOF. While EMNEs, like all other MNEs, face LOF in their foreign operations, they may also face LOR.

The concepts of LOR and LOF are distinct. First, LOR pertains to disadvantages borne by MNEs in host countries because of "where they are from", that is, their specific nationality, while LOF relates to the disadvantages borne by MNEs in host countries as a result of "where they are not from" (i.e., not local) (Ramachandran & Pant, 2010: 25). The liability of foreignness is a relative term, pertaining to the additional cost incurred by a foreign firm, compared to local firms. Second, home country influence is explicitly excluded in the measurement of LOF (Mezias, 2002), while it is this very influence that gives rise to LOR, which is linked to the country of origin. In the marketing field, one of the most widely researched concepts is the country-of-origin (COO) effect, or the influence of the national origin of a product or service on the purchase decision (Peterson & Jolibert, 1995), with developing countries often found to suffer from a negative country image. The focus of the COO literature has traditionally been on consumer products and services, rather than the origin-linked disadvantages faced by firms from emerging economies. The concept of liability of origin is thus distinct from both the liability of foreignness and the country of origin.

## Theoretical Underpinnings

The literature on the liabilities of origin has drawn on institutional theory (e.g., North, 1990; Scott, 1995) and organizational learning theory (e.g., Levitt & March, 1988; Fiol & Lyles, 1985), to explain the sources of these liabilities. Institutions can be defined as the "the rules of the game in a society or, more formally, as the humanly devised constraints that shape human interactions" (North, 1990: 3). Scott defined institutions in terms of regulatory, normative, and cognitive pillars that provide stability and meaning to social behavior (Scott, 1995). The regulatory pillar relates to the laws and regulations in a society, the normative pillar defines what people "should or should not do" (Eden & Miller, 2004: 201), and the cognitive pillar affects the ways in which people interpret stimuli from the environment and what people "can or cannot do" (Eden & Miller, 2004: 201). In developing countries, the regulatory pillar contributes to the LOR because rules, laws, and sanctions are often underdeveloped. The normative and cognitive pillars contribute to the LOR, as the EMNE's home country's normative and cognitive pillars may be perceived as conflicting with the corresponding pillars in the host country, especially when the institutional distance between the two countries is large (Xu & Shenkar, 2002; Liou, Rose, & Ellstrand, 2012). These perceptions may lead to negative stereotypes of EMNEs, making it difficult for them to gain organizational legitimacy.

Organizational legitimacy has been defined as the "congruence between the social values associated with or implied by organizational activities and the norms of acceptable behavior in the larger social system" (Dowling & Pfeffer, 1975: 122). In order to gain organizational legitimacy, in addition to following rules and regulations in the host country, firms may need to adapt the cognitive structures, normative values, and ways of doing things that are typical in the host country. Even if EMNEs are able to overcome resource constraints and institutional voids, gaining legitimacy has been shown to be extremely challenging (Bangara et al., 2012; Pant & Ramachandran, 2012). Legitimacy can enhance credibility and the firm's chance of survival, because local players are more likely to support and supply resources to organizations that appear to be

desirable and trustworthy (Suchman, 1995; Kostova & Zaheer, 1999). EMNEs are able to build legitimacy and overcome LOR through strategies such as alliances with international firms from advanced economies, acquiring global brands, locating their headquarters in western nations, and acquiring international certifications (Bonaglia et al., 2007; Pant & Ramachandran, 2012).

In addition to legitimacy, status may play an important role in EMNE acquisitions. Status has been defined as the "prestige accorded actors because of their social positions" (Jensen & Roy, 2008: 495) or the "socially constructed, inter-subjectively agreed-upon and accepted ordering or ranking of individuals, groups, organizations, or activities in a social system" (Washington & Zajac, 2005: 284). Even though status and legitimacy are complementary, they are distinct (Bitektine, 2011). While legitimacy denotes a level of acceptability, status (while implying acceptability) is concerned with prestige. Empirical research has shown that associating with a lower status firm may lead to a loss of status, while associating with a higher status firm may improve status (Podolny & Phillips, 1996; Jensen & Roy, 2008). Transaction costs have been found to be lower for high-status actors than for low-status actors (Podolny & Phillips, 1996). An important ramification of status for the current study is that low status of organizations has been associated with discrimination in the selection of business partners or participation in events (Washington & Zajac, 2005; Jensen, 2008). This has been corroborated by studies in the international human resource management literature, which found that job candidates tend to show a preference for advanced-economy MNEs to EMNEs as future employers (Alkire, 2014; Thite, 2012; Tung, 2007). The extant literature thus suggests that EMNEs are likely to face problems in getting a higher status target firm (e.g., an AMNE) to accept them as an acquirer.

## The Role of Organizational Learning

In addition to institutional voids, lack of legitimacy, and low status, another liability of origin is the EMNE's lack of global experience. Understanding the processes of organizational learning (Levitt & March,

1988; Fiol & Lyles, 1985) becomes critical to understand this liability. Organizational learning has been defined as the development of knowledge based on past firm behavior and applying these insights and associations to future actions (Fiol & Lyles, 1985). According to this theory, learning is a dynamic process, as firms are constantly learning, building, and adapting routines and processes to apply in future experiences (Levitt & March, 1988). Acquisitions can provide firms with quick access to knowledge and resources, and help them to learn new routines and repertoires (Morosini, et al., 1998; Barkema & Schijven, 2008). CBAs have been recognized as important tools of learning, and provide access to potentially valuable embedded knowledge and capabilities (Vermeulen & Barkema, 2001). However, learning from acquisitions is not straightforward. Acquisitions are often made for different reasons and may be irregular; each acquisition is unique. Relatively inexperienced acquirers may generalize acquisition experience inappropriately to dissimilar acquisitions (Haleblian & Finkelstein, 1999; Hayward, 2002). It has been shown that a certain level of context specificity is necessary to foster learning, and firms do not learn from every acquisition (Vermeulen & Barkema, 2001). In the context of EMNE acquisitions, this theoretical insight will be used to investigate whether experience in the same country (a similar context) plays a more important role than breadth, or a range of geographical experience. These theoretical inputs help to design the conceptual model described in the next section.

## Conceptual Model

The extant literature has described different types of liabilities of origin Bartlett and Ghoshal (2000) focused on psychological liabilities faced by EMNE managers, namely, a liability of under-confidence in their global capabilities and the converse liability of over-confidence caused by lack of exposure. Ramachandran and Pant (2010) classified LOR along three dimensions: (i) underdeveloped institutional intermediaries in the home country, (ii) discrimination in the host country, and (iii) organizational weaknesses. Developing on this work, Madhok and Keyhani (2012) classified what they termed “liability of emergingness” into two types, one

caused by factors external to the firm ("institutional deficit"), and the other caused by factors internal to the firm ("managerial and capability deficit"), leading to a "legitimacy and credibility" deficit. The classifications of Ramachandran and Pant (2010) and Madhok and Keyhani (2012) are essentially similar, as they include liabilities relating to organizational weaknesses, institutional voids, and credibility. While these scholars described different aspects of LOR, they did not undertake empirical testing of the influence of LOR.

Careful analysis of the extant literature reveals that EMNE liabilities seem to be caused both by an *actual* lack of capabilities and by a *perception* of a lack of capabilities. In our model, we term the actual lack of liability as "capability liability". This capability liability can be attributed to the EMNE's lack of global experience, which may result in inadequate routines and processes for handling the complex process of CBAs. Further, this lack of experience may result in a low level of confidence among EMNE managers during negotiations and post-acquisition integration. The firm's capability can also be limited by institutional voids, such as inadequate financial and investment freedom, and related bureaucratic hurdles. We term the second category of liabilities, or the perception of lack of capability, as "credibility liability". The credibility liability can be attributed to both a lack of legitimacy and a low status. Even if an EMNE is familiar, and its structure and processes are acceptable and hence legitimate, it may still be considered lower in status than an MNE from advanced economy. AMNEs may enjoy a higher status in the business world than EMNEs because of superior brand image, more advanced technology, and their international strategic presence and stature (Sethi & Judge, 2009; Smith & Meiksins, 1995). Based on this categorization, we build our conceptual model as shown in Fig. 7.1.

We now explore the influence of these two categories of liabilities on acquisition completion. The steps in acquisition completion include the search for the strategic partner, negotiations, integration planning, and closing the deal (DePamphilis, 2013). After selecting a suitable target, the due diligence, or review of the target firm's records and facilities, often takes place through the negotiation phase. In addition to agreeing on the purchase price, negotiations involve deciding on the form of payment, tax and accounting considerations, and legal details. Integration planning involves deciding how operational, functional, and socio-cultural

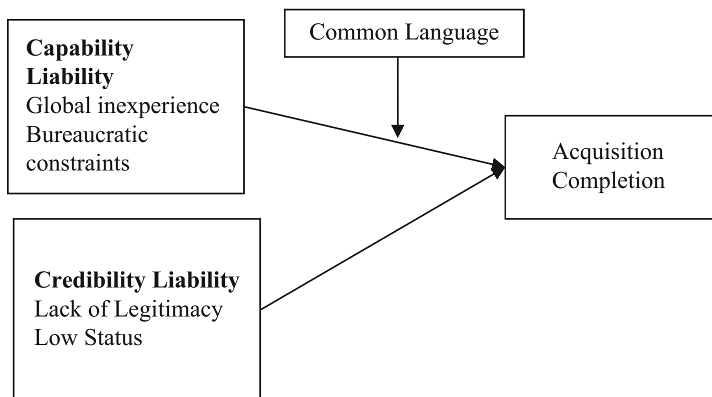


**Fig. 7.1** Conceptual model for the influence of liabilities of origin on EMNE cross-border acquisition completion

integration will be structured and implemented (Shrivastava, 1986). After these stages, if both parties are satisfied, the acquisition is completed. The final stage includes obtaining approvals from regulatory authorities, shareholders and other stakeholders with whom the target firm has existing contracts (DePamphilis, 2013). Thus, acquisition completion is a very complex process, involving multiple stages and several stakeholders

## Capability Liability and Acquisition Completion

### *First Experience in a Nation*

Organizations learn from direct experience and develop processes, routines, and frameworks from the interpretation of that experience (Levitt & March, 1988). Firms have been found to benefit from previous acquisition experience in a country (e.g., Barkema, Bell, & Pennings, 1996). Cross-border investments often involve complicated negotiations that may last for several months, and even years, between multiple stakeholders. In order to be successful in these negotiations, the managers involved have to understand the rules of the "negotiating game", such as determining the key players and decision-makers (Sebenius, 2002). Another skill required during this phase is cross-cultural competence and

team management (Brett, Friedman, & Behfar, 2009). EMNE managers may not be internationally savvy, and may lack the capabilities required for handling these processes. The effect of inexperience is likely to be exacerbated when the EMNE acquires a firm for the very first time in a particular nation; because of the lack of familiarity with laws, regulation, practices, and national culture, the EMNE will be something of a "stranger in a strange land". EMNE managers may not know fully what financial, legal, and other resources are required for deal completion in the new setting. On this basis, we hypothesize:

**Hypothesis 1** The likelihood that the cross-border acquisition deal will be completed is lower when it represents the firm's first acquisition experience in the target nation.

### *The Influence of Language*

The negotiation process is facilitated if the two parties share a common language. The use of interpreters and translators can hamper and lengthen the process, and lead to miscommunication (e.g., Sebenius, 2002). Language barriers can especially delay due diligence processes. A common language has been found to lower transaction costs and facilitate doing business in unfamiliar markets (e.g., Doh, Bunyaratavej, & Hahn, 2009). For example, the lack of English-speaking capability among Chinese CEOs has been found to be a major barrier to their success in the USA (Peng, 2012). Deal completion also involves extensive documentation, requiring language skills. Thus, the lack of a common language is likely to further accentuate the capability liability, while a common working language is expected to mitigate the influence of this liability. We, therefore, propose the following hypothesis:

**Hypothesis 2** A common working language moderates the relationship between the first time experience in a target nation and the likelihood that the cross-border acquisition deal will be completed, such that the negative relationship becomes weaker if the partners' home nations share a common working language.

### *Prior Acquisition Experience*

Organizational learning theory suggests that there will be transfer of prior acquisition experience to a subsequent acquisition (Barkema & Schijven, 2008). The literature indicates that it is not just the number of acquisitions that affect organizational learning positively, but also their breadth and whether the context of the previous experience is related to the current acquisition experience (Haleblian & Finkelstein, 1999). Organizations with prior acquisition experience are more likely to be able to manage the targeting process effectively, which, in turn, will facilitate acquisition completion (Larsson & Finkelstein, 1999). This suggests the following hypothesis:

**Hypothesis 3** There is a positive relationship between prior successful cross-border acquisition experience and the likelihood that the cross-border acquisition deal will be completed.

### *Geographic Acquisition Experience*

Acquisition experience has been shown to be of greater value in related contexts (Haleblian & Finkelstein, 1999). Specificity of experience helps a firm to transfer knowledge and make appropriate changes to organizational processes and routines (Barkema & Schijven, 2008). When acquisitions are heterogeneous, it is more difficult to apply learning to the new settings (Hayward, 2002). If firms have previously acquired targets in a particular country, they are more likely to be familiar with both the legal requirements and host country stakeholders; learning may not necessarily occur from experiences in dissimilar countries (Barkema et al., 1996), and firms may not be able to apply more general knowledge about new cultures in different settings (Nadolska & Barkema, 2007). On this basis, we suggest the following hypothesis:

**Hypothesis 4** There is a negative relationship between the number of countries (other than the focal country) in which a firm has made acquisitions and the likelihood that the cross-border acquisition deal will be completed.

*Bureaucratic Constraints*

Institutions affect organizational success (Scott, 1995), and regulatory quality can influence acquisition. The rules of the cross-border M&A game, such as antitrust laws and governing regulations, are extremely complex (Dikova et al., 2010). EMNEs may find it easier to complete an acquisition in a country in which laws and regulations are transparent and consistent, and where legal enforcement of acquirer interests is assured. Location choices of acquisitions by Chinese and Indian firms have been found to be related to regulatory quality except in the mining sector (De Beule & Duanmu, 2012). The likelihood of deal completion for Chinese firms shows evidence of being positively related to the host country's institutional quality (Zhang, et al., 2011). This suggests the following hypothesis:

**Hypothesis 5** There is a positive relationship between regulatory quality in the target host nation and the likelihood that the cross-border acquisition deal will be completed.

*Credibility Liability and Acquisition Completion*

Status Differences

Status is a multilevel concept that can operate at the level of the individual, the firm, and the nation. In M&As, status conflicts at the individual level, between managers of the target and acquirer firm, have been shown to lead to executive departures (Hambrick, 1993). At the organizational level, status has been found to influence the choice of partners, transaction costs, negotiation outcomes, and access to resources (Sauder, Lynn, & Podolny, 2012). At the national level, status can be measured on the basis of economic, political, cultural, geographical, and other factors (Shimbori, Ikeda, Ishida, & Kondô, 1963).

A negative country image contributes to the low status of developing nations. Country image has been measured along several dimensions, including standard of living, level of education, and cultural and political similarity (Parameswaran & Pisharodi, 1994; Pereira, Hsu, & Kundu,

2005). Social status is used as a criterion for selecting partners, and high-status actors have been shown to experience a drop in status if they collaborate with low-status actors (Jensen & Roy, 2008; Sauder et al., 2012; Washington & Zajac, 2005). High-status actors tend to have more favorable outcomes in negotiations (Ball & Eckel, 1996). Further, status signals matter more under conditions of uncertainty, such as cross-border ventures, increasing the reluctance of firms to enter into relationships with those who are lower in status (Podolny & Phillips, 1996). EMNEs, therefore, are less likely to be the preferred partner because of their low status, and also likely to be at a disadvantage during the negotiations process, delaying acquisition completion. Collectively, these arguments suggest the following hypothesis:

**Hypothesis 6** There is a negative relationship between the status difference between the M&A firms' home nations and the likelihood that the cross-border acquisition deal will be completed.

*Legitimacy of Public Sector Firms*

Firms operating in the public sector are likely to be less acceptable or legitimate when they attempt to acquire foreign firms. The lack of transparency in their accounting practices, excessive bureaucracy, and possible cronyism with respect to the appointment of top officials are some of the factors that make these firms less credible in foreign countries. They are often perceived as being inefficient and vulnerable to political interference, leading to a lack of socio-political legitimacy. (Zhang et al., 2011). Further, public sector firms often operate in industries that are critical to the economy, such as oil and mining Acquisitions in the mining and petroleum sector by EMNEs have been blocked by host country governments in advanced economies, because of issues of national security (De Beule & Duanmu, 2012). Public sector firms are thus more likely to suffer from a lack of legitimacy and face hurdles in their acquisition completion, leading to the following hypothesis:

**Hypothesis 7** The likelihood of cross-border deal completion is lower when the acquirer is a public sector firm.

EMNEs can undertake strategic efforts to increase their credibility in the target firm's home nation. For example, they may register their headquarters in an advanced economy, signaling that they are capable of adhering to stringent regulations (Bangara et al., 2012). They may hire the services of global branding firms, or develop strategic alliances with high-status firms before undertaking acquisitions (Bonaglia et al., 2007). Indian IT firms have been undertaking legitimacy-building measures in the USA through various strategies, including listing on US stock exchanges and appointing members of the Indian diaspora to senior management positions, to assist in the development of trust with potential clients. They have also formed associations such as National Association of Software and Service Companies, and obtained prestigious US certifications such as the Capability Maturity Model and ISO 9001 (Pant & Ramachandran, 2012). Such strategic legitimacy-building efforts are likely to make the EMNE firm more known and acceptable in target nations, leading to the following hypothesis:

**Hypothesis 8** Strategic legitimacy-building efforts by an industry increase the likelihood that cross-border acquisition deals will be completed in that sector.

# Methodology

## Data and Sample

The current study uses a sample of CBAs made by Indian MNEs between 1999 and 2013. Developing countries in Asia have been very active in CBAs since 2000 (UNCTAD, 2014), and Indian MNEs have stood out for both the range of sectors in which they invest and their success with acquisitions in advanced economies. Indian MNEs have been acquiring companies in the primary, manufacturing, and service sectors (Kumar,

2008; Ray & Gubbi, 2009), and approximately 70 % of the acquisitions made by Indian MNEs have been in advanced economies (Pradhan, 2007). These acquisitions have been made in spite of the image of a country that is not business-friendly, as indicated by India's very low rank of 142 (among 189 countries) in the 2014 World Bank Group's "Ease of Doing Business" assessment. Thus, selecting MNEs from India for this study, with their diverse range of cross-border ventures in varied geographic locations in spite of a poor country image, is expected to provide rich insights on the influence of LOR on cross-border M&A.

The data are derived from the Thomson Reuters SDC Platinum Database, which has been used widely in the cross-border M&A academic literature (e.g., Contractor, Lahiri, Elango, & Kundu, 2014; Dikova et al., 2010; Sun et al., 2012). The current study focuses on publicly announced acquisitions made by Indian MNEs between 1999 and 2013. We chose the year 1999 because the number and value of CBAs made by Indian MNEs before 1999 were not substantive. This can be attributed to the regulatory restrictions on foreign exchange in place at that time. In 1999, with the introduction of the Foreign Exchange Management Act, external trade and payments were facilitated. Companies were then permitted to invest up to 100 % of their global depository receipts in CBAs (Gopinath, 2007). These supportive policy changes resulted in the value of CBAs by Indian MNEs crossing US$ 1 billion for the first time in 2001.

Given the hypotheses and the focus of the analysis on credibility and capability liabilities faced by EMNEs, the selection of the sample took the following criteria into account. First, since the unit of analysis is a firm, acquisitions by individuals were eliminated. Second, we excluded the category of "investor groups", as our unit of analysis is the EMNE, and investor groups are often formed of diverse groups and individuals, often of different nationalities. We excluded instances of round-tripping and those in which the acquirer and the target firm were from the same parent company. We also eliminated subsidiaries of foreign MNEs, as our focus was on Indian MNEs. After eliminating firms that did not match our selection criteria, we have a sample of 1864 acquisitions undertaken during the period of interest, 67 % of which were completed.

## Measures

Our dependent variable is "closing the deal". This variable takes the value of 1 if the deal is recorded as being completed in the Thomson Database, as indicated by the variable "Date Effective".

Credibility liability is measured by two related, but different, concepts: legitimacy and status. We test our proposition by focusing on the difference in legitimacy between firms in the Indian IT and related industries and firms in other sectors. The IT and related sectors from India have gained global legitimacy at a slow, but steady, pace since the late 1990s, through measures such as off-shoring and listing on international stock exchanges. It was only after 2000, when Indian IT firms helped to tide over the global Y2K crisis, that they started to gain a taken-for-granted cognitive legitimacy (Pant & Ramachandran, 2012; Dossani & Kenney, 2006). Pant and Ramachandran (2012) posited that the Indian software industry attained a legitimacy threshold by the year 2004, based on inputs from senior executives in Indian software firms and a detailed analysis of reports by US technology analysts. To test our hypothesis, we compare the number of deals closed by Indian MNEs from the IT and related sectors with the number of deals closed by Indian MNEs from all other sectors. This is operationalized as a variable (AcquirorITLegit) that took the value 1 if the three-digit SIC code for the acquirer firm was either 737 or 738, and if the year of acquisition was 2005 or later. We specifically test for the success of acquisition completion post-2004, after Indian IT firms attained a necessary threshold of global legitimacy.

We have operationalized the role played by organizational learning in mitigating the impact of liability of origin in three different ways. We measure the depth of organizational learning in terms of the number of successful CBAs made by the acquiring firm prior to the focal acquisition (NumberAcqSucc), and the breadth of prior acquisition in terms of the number of countries, other than the focal country, in which the acquiring firm has had acquisition experience (GlobalExp). We also test for the impact of the relative absence of familiarity with a country's institutions and practices the first time an acquiring firm ventures into any country (CountryFirstTime). This liability is expected to be mitigated by the presence of a common language (in this case, English) for doing business (English).

We argue that the poor standard of living in India contributes to the low status of Indian MNEs. To measure status, we use the UNDP's Human Development Indices (HDI). HDI is a composite measure that takes health, education, and income into account. We operationalize the relative status difference in terms of the ratio of the HDI scores for the acquired firm's home country to that of India for the year in which the acquisition took place; specifically, the dummy variable HDIStatus takes the value of 1 if the relative HDI ratio is in the top quartile of its distribution, representing countries whose living standards are substantially higher than those of India. Ideally, status should be measured at the organizational level. In the extant literature, organizational status has commonly been estimated at the industry-nation level (e.g., Washington & Zajac, 2005; Jensen & Roy, 2008). Hence, selecting a measure for status that would hold across industries in different target countries proved a challenge. The variable PublicSector captures the relatively lower legitimacy of public sector enterprises from emerging markets such as India, given the experienced vulnerability of these public enterprises to political pressures and compulsions. Finally, we capture the mitigating impact (when present) of the relatively stronger institutions of regulatory governance in the country of the acquired firm through the corresponding Quality of Governance variable from the World Bank(QOG_RQE), and expect a positive relationship between QOG_RQE and the likelihood of deal completion.

We consider two control variables in our analysis: CashOnly and Related2. We expect deals involving only cash payments to have a higher probability of completion, given that deals involving stock payments can lead to delays in completion, as they are more complex due to the varying prices stocks; this can lead to renegotiations and delays in closing the deal (Dikova et al., 2010). The Related2 variable takes the value of 1 if the acquiring and acquired firms come from the same industry—operationalized as having the same two-digit SIC code. Acquisitions in a related industry are more likely to add to skills and expertise, and this experience in related industries may help to reduce the time required for closing the deal

## Results

The dependent variable for our analysis is Deal Completion. While our sample covers 1864 CBAs by Indian firms during 1999–2013, many of the firms made multiple acquisitions over this period, with the mean number of acquisitions in the sample being 2.8. Table 7.1 describes the variables used in the analysis, Table 7.2 presents the summary statistics for the variables, and Table 7.3 presents the pair-wise correlations.

Given the binary nature of the dependent variable, we estimate three separate logit models. In Model 1, we include only the constant term, the year dummies, and our control variables. In Model 2, we add the capability liability-related explanatory variables, and in Model 3, we further add the credibility liability-related variables for the fully specified model. Table 7.4 presents details of the three analytic models.

The Wald $\chi^2$ values for all three models are significant, indicating that each model has at least one variable that has significant explanatory power with respect to the probability of deal completion. The log-likelihoods for the three models indicate significant increases in the explanatory powers as we add the explanatory variables to the models, with the fully specified model having the best goodness of fit.

In line with our expectations, NumAcqSucc—our measure for the depth of the acquiring firm's acquisition experience—has a positive and significant relationship with the likelihood of deal completion in Models 2 and 3. Similarly, GlobalExp—our measure for the breadth of the acquiring firm's acquisition experience—offers significant explanatory power; as hypothesized, this relationship is negative, such that an increase in the number of countries (other than the focal country) in which the acquiring firm had attempted acquisitions is associated with a lower probability of deal completion. Taken together, these two results suggest that the impact of prior acquisition experience on the probability of completion of the current acquisition works in two important—and opposing—ways; depth helps and breadth hurts, marginal to the other variables in the model.

We had also posited that the probability of completion would be lower if the acquiring firm was entering a country for the first time (CountryFirstTime), but that this effect would be moderated by language

**Table 7.1** Description of variables

| Name | Description | Source |
|---|---|---|
| ***Dependent variable*** | | |
| Deal completion *(Completed)* | Date effective<br>Takes on a value of 1 if deal is closed "Deal Effective"<br>Takes on a value of 0 if withdrawn | Thomson SDC Platinum |
| ***Independent variables*** | | |
| First time country experience *(CountryFirstTime)* | Takes on a value of 1 for the first time the EMNE acquires a firm in a particular nation, 0 otherwise | Thomson SDC Platinum |
| Common business language *(English)* | Takes on a value of 1 if English is the official language in the target firm nation, 0 otherwise | |
| Number of successful cross-border acquisitions prior to focal acquisition *(NumberAcqSucc)* | The number of successful acquisitions undertaken by the EMNE prior to focal acquisition. A measure of the *depth* of acquisition experience | Thomson SDC Platinum |
| Geographic global experience *(GlobalExp)* | The number of countries other than focal country the EMNE has acquisition experience in before undertaking the focal acquisition. A measure of the *breadth* of acquisition experience | Thomson SDC Platinum |
| Public sector enterprise *(PublicSector)* | Takes a value of 1 if the EMNE belongs to public sector, 0 otherwise | Thomson SDC Platinum |
| Industry-specific legitimacy-building efforts *(AcquirorITLegit)* | Takes on a value of 1 if the firm is from the IT and related sectors (SIC Codes 737, 738) and the acquisition was announced after the year 2004 | Thomson SDC Platinum |
| National quality of life status *(HDIStatus)* | Relative UNDP HDI of target firm host nation to India's HDI in the year of acquisition announcement | UNDP |
| Regulatory quality in target firm country *(QOG_RQE)* | The score for the regulatory quality WB QOG variable for the given target country and year of announcement of acquisition | World Bank Quality of Governance Indicators |
| ***Control variables*** | | |
| All cash deal *(CashOnly)* | Takes the value 1 if the deal was all cash only | SDC Platinum |
| Industry relatedness *(Related2)* | Takes a value of 1 if the two-digit SIC code for acquirer firm's industry matches with that for the target firm | SDC Platinum |

Constructed from http://en.wikipedia.org/wiki/List_of_territorial_entities_where_English_is_an_official_language.

**Table 7.2** Summary statistics

| Variable | Obs | Mean | Std. Dev. | Min | Max |
|---|---|---|---|---|---|
| CashOnly | 1864 | 0.14 | 0.35 | 0 | 1 |
| Related | 1852 | 0.61 | 0.49 | 0 | 1 |
| Number of successful Acqns | 1864 | 1.11 | 1.91 | 0 | 15 |
| CountryFirstTime | 1864 | 0.76 | 0.43 | 0 | 1 |
| English | 1864 | 0.61 | 0.49 | 0 | 1 |
| GlobalExp | 1864 | 1.02 | 1.76 | 0 | 12 |
| QOG_RQE | 1849 | 1.10 | 0.80 | −2.08 | 2.16 |
| AcquirorIT2004 | 1864 | 0.19 | 0.39 | 0 | 1 |
| HDIStatus | 1864 | 0.50 | 0.50 | 0 | 1 |
| PublicSector | 1864 | 0.06 | 0.25 | 0 | 1 |

commonalities (English) between the two countries; these hypothesized relationships are not supported by the data. The absence of the hypothesized negative impact of relative inexperience with the focal country was surprising, and merits further investigation. One possible explanation is that, while this was the first time the firm was acquiring in the focal country, it may have already been familiar with the country owing to earlier internationalization efforts, such as an earlier joint venture or subsidiary.

The results were in line with our expectations about the positive impact of the quality of regulatory governance (QOG_RQE) in the acquired firm's country (our capability argument), as well as the impact of the acquiring firm's belonging to the public sector (PublicSector) in India (our credibility argument).

Finally, the analysis also underscored the impact of the deal structure and industry relatedness on deal completion, with both of the control variables (CashOnly and Related2) offering significant explanatory power in the fully specified model.

## Discussion

Our study makes several contributions to the literature on EMNE internationalization. We have integrated the existing frameworks on the disadvantages faced by EMNE and categorized these liabilities along two dimensions: capability liability, or the actual deficit of managerial

**Table 7.3** Correlations

| | CashOnly | Related2 | NumAcq Succ | Country FirstTime | English | Global Exp | QOG_ RQE | AcquiIT | HDI Status |
|---|---|---|---|---|---|---|---|---|---|
| CashOnly | 1.00 | | | | | | | | |
| Related2 | 0.07 | 1.0 | | | | | | | |
| NumAcqSucc | 0.03 | 0.08 | 1.00 | | | | | | |
| CountryFirstTime | –0.08 | –0.07 | –0.41 | 1.00 | | | | | |
| English | 0.11 | 0.01 | –0.01 | –0.17 | 1.00 | | | | |
| GlobalExp | –0.01 | 0.05 | 0.74 | –0.20 | –0.09 | 1.00 | | | |
| QOG_RQE | 0.11 | –0.02 | –0.03 | –0.10 | 0.44 | –0.19 | 1.00 | | |
| AcquirorIT2004 | 0.05 | 0.17 | 0.09 | –0.12 | 0.18 | –0.02 | 0.19 | 1.00 | |
| HDIStatus | 0.08 | 0.00 | –0.03 | –0.12 | 0.42 | –0.12 | 0.59 | 0.13 | 1.00 |
| PublicSector | –0.07 | 0.02 | 0.07 | –0.01 | –0.10 | 0.31 | –0.33 | –0.13 | –0.13 |

**Table 7.4** Acquisition completion results

| | Model 1 | Model 2 | Model 3 |
|---|---|---|---|
| Variables | *Controls only* | *Capability liabilities* | *Capability and credibility liabilities* |
| Constant | 0.362 | 0.168 | 0.388 |
| | (0.386) | (0.472) | (0.483) |
| CashOnly | 0.507** | 0.436** | 0.395** |
| | (0.156) | (0.161) | (0.162) |
| Related2 | 0.142 | 0.165 | 0.188* |
| | (0.103) | (0.106) | (0.110) |
| NumAcqSucc | | 0.221** | 0.161** |
| | | (0.048) | (0.048) |
| CountryFirstTime | | 0.056 | –0.006 |
| | | (0.236) | (0.241) |
| CountryFirstTime*English | | 0.148 | 0.149 |
| | | (0.241) | (0.248) |
| English | | –0.261 | –0.192 |
| | | (0.254) | (0.263) |
| GlobalExp | | –0.321** | –0.230** |
| | | (0.049) | (0.051) |
| QOG_RQE | | 0.289** | 0.211** |
| | | (0.072) | (0.092) |
| AcquirorIT2004 | | | –0.084 |
| | | | (0.144) |
| HDIStatus | | | –0.119 |
| | | | (0.167) |
| PublicSector | | | –1.584** |
| | | | (.257) |
| *Cases* | 1852 | 1837 | 1837 |
| *Log likelihood* | –1155.04 | –1101.94 | –1080.04 |
| *Wald* $\chi^2$ | 0.00 | 0.00 | 0.00 |

** $p<0.01$, * $p<0.05$

resources and capabilities, and credibility liability, or the lack of status and legitimacy. We extend the literature on M&A deal completion by building a conceptual model reflecting the influence of the liabilities of origin on deal completion. Existing studies on EMNE disadvantages have focused on financial performance in EMNE-driven cross-border M&As, rather than the processes. We adopt a novel approach by analyzing the influence of LOR on acquisition completion; this influence has not been considered in earlier work. Specifically, we introduce variables pertaining to legitimacy and status, along with both the depth and breadth of global experience, into the model.

Many of our hypotheses were supported by our analysis of the cross-border acquisitions done by Indian firms during 1999–2013. Our analysis showed that prior acquisition experience has the potential to mitigate the liability of origin, but that the learning may not necessarily be transferable across countries. What also stood out in our results was the relative lack of impact of credibility-linked liability. We suspect that this was probably more a matter of an absence of evidence, reflecting the nature of the variables we used to operationalize the construct, rather than an evidence of absence of the hypothesized effects themselves.

## Limitations and Further Research

In the current study, status has been measured at the country level. In further research, a measure for status at the firm level could be generated and tested. The impact of status differences on post-integration could then be investigated. A high-status difference has been found to lead to deferential behavior by the lower status firm, and to fewer conflicts during post-acquisition (Cowen, 2012). This may be investigated empirically in the context of acquisitions by EMNEs. The current measure of capability liability can be made richer by testing additional firm-level proxies, such as R&D and marketing capabilities; investments in R&D and marketing have previously been found to relate positively to internationalization.

The current study has relied on secondary data for its analysis. Case studies and in-depth interviews could add invaluable insights. However, the fact that M&A processes are highly confidential, given their impact on share prices, employment, and industry structure, makes access to rich process data very challenging. Further, acquisitions are sometimes undertaken because of managerial hubris (Roll, 1986) or national pride (Hope, Thomas, & Vyas, 2011), and top managers are understandably reluctant to share unfavorable information about their strategies. Another factor is that Indian MNEs, like other EMNEs, are based in environments that may lack transparency. Since companies cannot rely on the institutional environment to protect their systems, they may rely more on protecting themselves by not openly sharing information. Thus, even while we recognize that this study would be enriched by primary data, we found that

even if managers were willing to discuss sensitive issues relating to M&As off the record, they were reluctant to have the information made public, in spite of assurances of confidentiality.

Acquisition completion is just one of the steps in the M&A process. Further research could explore the influence of LOR on other stages. The current study has focused only on Indian MNE acquisitions. Future work could compare the influence of LOR across different emerging economies. The concept of LOR, we believe, is not relevant to M&As alone, but can also contribute to understanding the dynamics associated with other cross-border ventures, such as strategic alliances and joint ventures.

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