Cross-border Spillovers: How US Financial Conditions affect Mergers and Acquisitions Around the World

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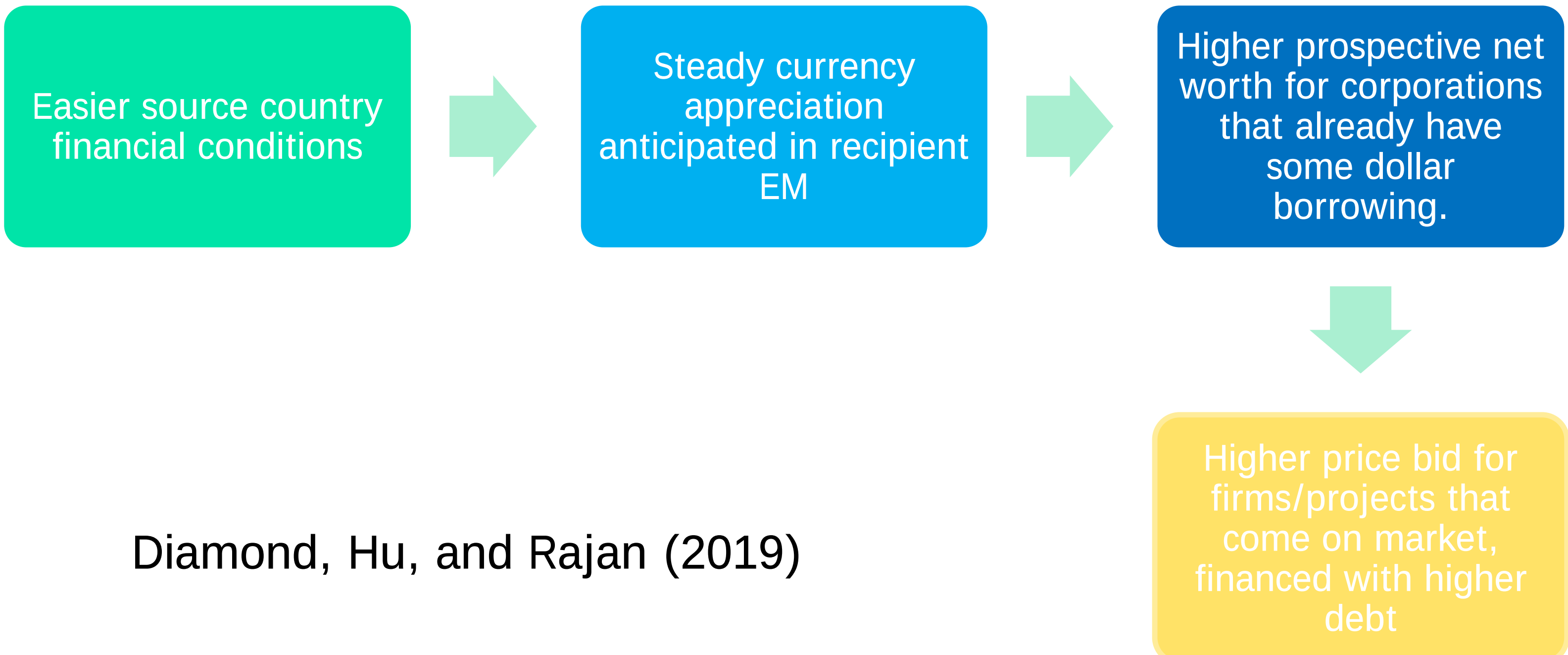
Easy financial conditions affect M&A activity

- Asset reallocation responds to easier financing conditions (Eisfeldt and Rampini (2006))
  - Is asset re-allocation affected by cross-border spillovers?
- Multiple rationales for cross-border spillovers of easier financing conditions in source countries
  1) Restructuring/completing global supply chains
  2) Exchange rate channel as a result of local currency appreciation
  3) Exchange rate channel as a result of local currency depreciation
  4) Other rationales

1. Restructuring/completing global supply chains

- Easier source country financing conditions give source country corporations plentiful funding.
- They can extend supply chains across the world.
- If EMs and developing countries are incremental new production locations
  - More cross-border acquisitions
  - Especially if country more open to trade and investment
- Acquire upstream and downstream services in DMs

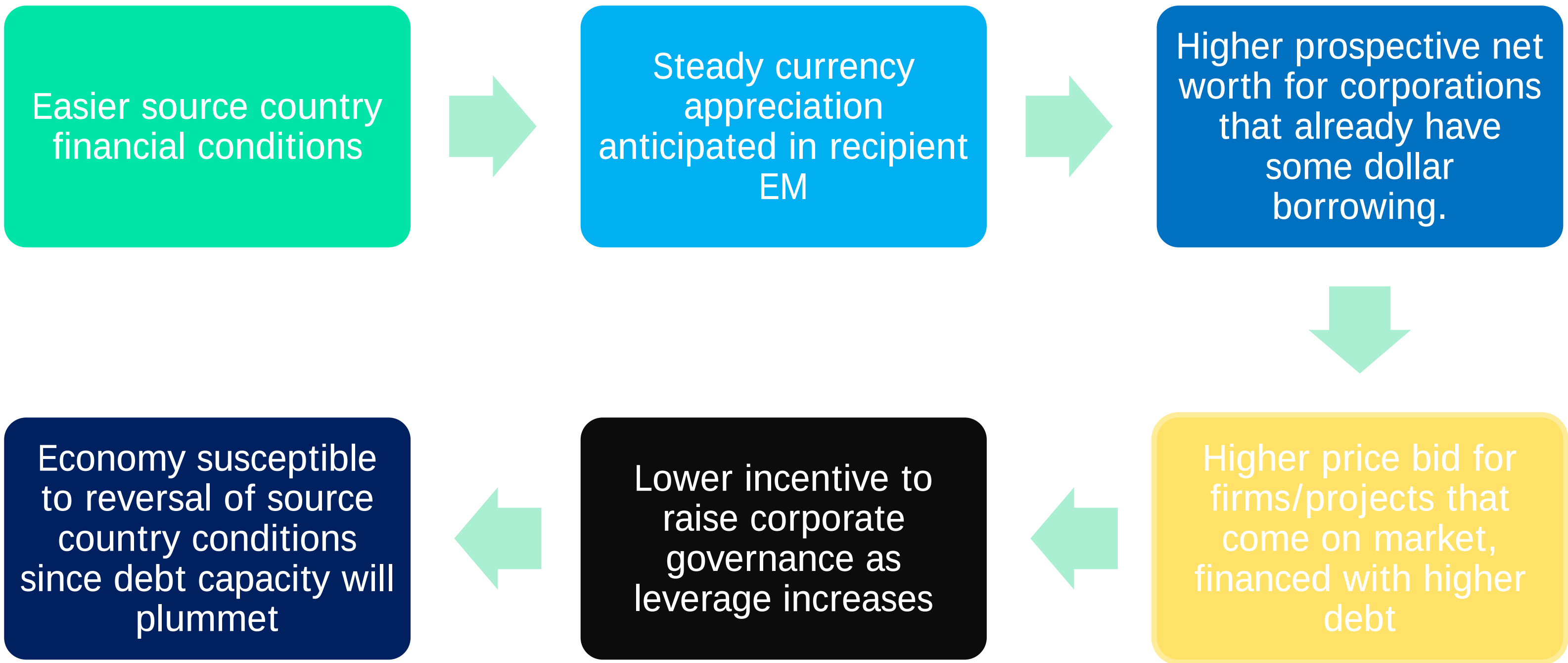
2. Easy US Financial conditions => anticipated local currency appreciation => higher local M&A activity



Diamond, Hu, and Rajan (2019)

- More M&A when local currency appreciates
- Especially if corporate sector has substantial fx liabilities.

Why currency fluctuation makes M&A activity more volatile



3. Tighter US financial conditions => anticipated local currency depreciation => Higher M&A activity

- Local depreciation makes assets cheaper and more attractive
- Should enhance profitability of local production
- More M&A when local currency depreciates

Other rationales

- Rising “real” tide lifts all ships
- Easier US financial conditions boosts US activity, trade, and activity elsewhere.
- Higher local activity boosts M&A.

=> US financial conditions indirectly boosts M&A activity elsewhere.

Data

- SDC Mergers and Corporate Transactions data 1998-2017
  - 0.9 million deals, 124 countries
  - Total deal value of $ 77.3 trillion of which 26% are cross-border
  - Normalize annual deal value by 2010 country $ GDP
- IMF US Financial Conditions Index
  - Rates, spreads, equity prices, equity vol, house prices
- FX liabilities of non bank sector to reporting banks
  - Crude measure of fx liabilities of corporate sector
  - Includes households, government, and some cross-border local currency loans
  - Not net liabilities
- Openness
  - Exports plus imports to GDP

Figure 1. Average M&A over time, 1998-2017

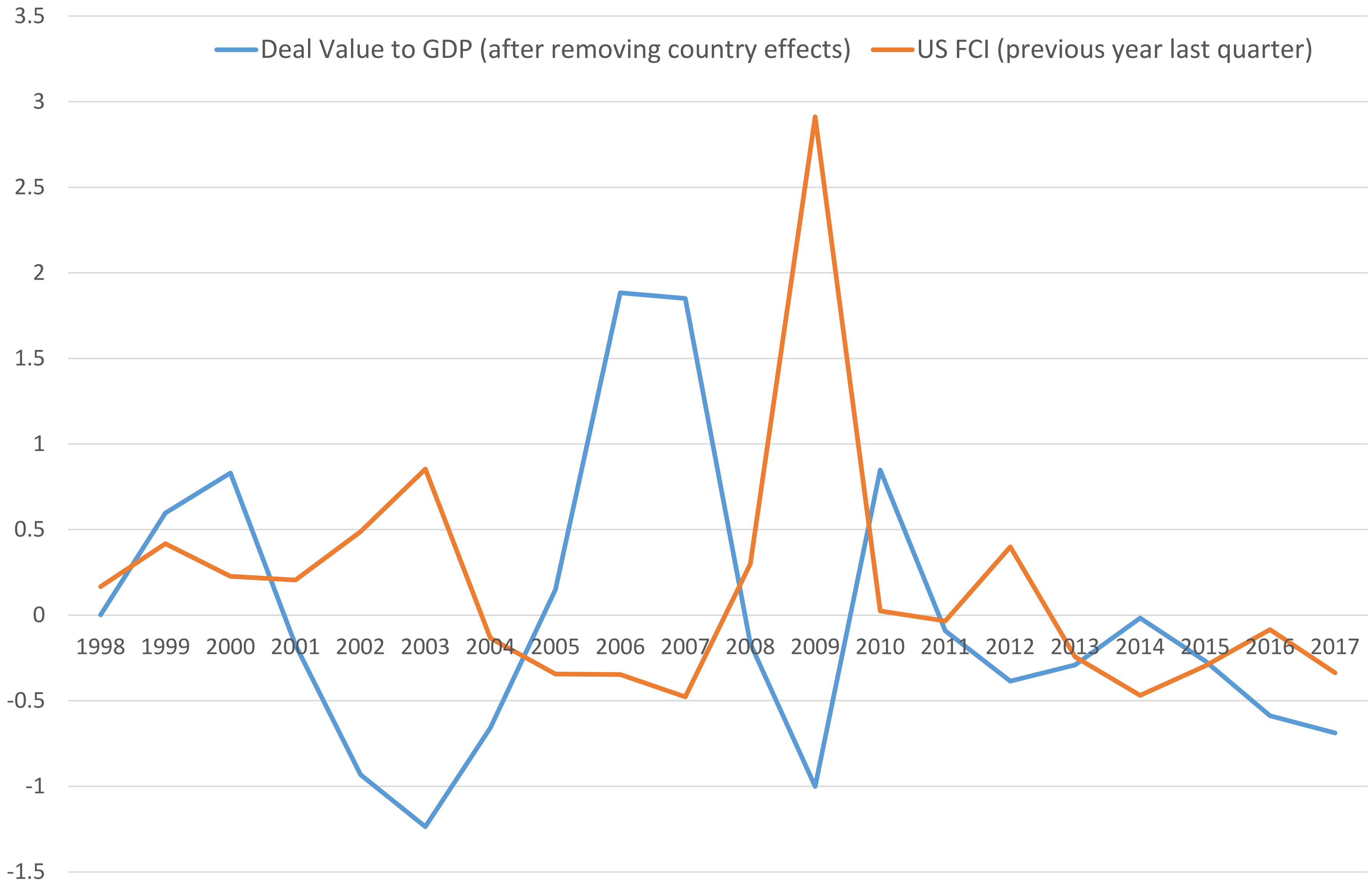


Table 1: Summary Statistics of the main variables used in empirical analysis

	(1)	(2)	(3)	(4)	(5)
VARIABLES	Observations	Mean	Standard Deviation	Minimum	Maximum
Trade openness	2,762	89.09	53.64	22.49	358.2
Deal Value/GDP(2010 $)	2,543	3.173	6.176	0.00161	43.22
Lagged per capita GDP	2,731	8.719	1.509	5.811	11.56
Lagged GDP growth	2,739	2.496	3.887	-10.21	13.64
Lagged lending rate	2,032	6.638	8.703	-24.74	44.29
US FCI previous year quarter 4	2,951	0.152	0.733	-0.478	2.912
Lagged FX claims	2,622	.2596	0.960	0.007	7.883
Number of gr	110	110	110	110	110

VARIABLES	(1) No controls	(2) With Controls	(3) FCI & FX Liab	(4) FCI & FX Liab Ind	(5) FCI & FX Liab EMD
US FCI previous year quarter 4	-0.497***	-0.537***	-0.266***	-0.978***	-0.137*
	(0.099)	(0.109)	(0.075)	(0.253)	(0.081)
Lagged FX loans			1.653**	1.336***	2.995
			(0.686)	(0.246)	(2.479)
Lagged FX loans*FCI			-0.766***	-0.733***	-0.755***
			(0.078)	(0.066)	(0.235)
Constant	3.249***	5.682	5.675	-29.076	4.781
	(0.015)	(3.632)	(3.536)	(57.784)	(3.345)
Observations	2,543	1,815	1,743	377	1,366
R-squared	0.007	0.013	0.036	0.090	0.029
Number of gr	171	137	132	22	110

Robust standard errors in parentheses

*** p<0.01, ** p<0.05, * p<0.1

VARIABLES	(6) Trade Openness & FCI	(7) All direct effects and Interactions	(8) Industrials	(9) EMD
US FCI previous year quarter 4	0.175	-0.039	-1.214**	0.143
	(0.266)	(0.148)	(0.480)	(0.173)
Lagged FX loans		1.813**	1.547***	2.988
		(0.729)	(0.476)	(2.500)
Lagged FX loans*FCI		-0.687***	-0.828***	-0.696***
		(0.111)	(0.175)	(0.264)
Trade openness	-0.002	-0.015*	-0.014	-0.007
	(0.009)	(0.008)	(0.019)	(0.008)
Trade Openness*FCI	-0.008**	-0.003*	0.002	-0.003
	(0.003)	(0.002)	(0.004)	(0.002)
Constant	5.914	6.596*	-38.441	5.212
	(3.625)	(3.723)	(63.449)	(3.452)
Observations	1,755	1,683	377	1,306
R-squared	0.019	0.039	0.091	0.032
Number of gr	132	127	22	105

Robust standard errors in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Conclusion

- M&A activity elsewhere seems to be correlated with US financial conditions
- Spillovers stronger for more open economies and economies with higher net foreign liabilities.
- More work needs to be done
  - Precise measures of net corporate fx liability
  - Exchange rate channel
  - To establish causality.