

## Chapter 13

# Firm–Level Determinants of Foreign Investment and M&A Activity: Evidence from Turkey

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### ABSTRACT

*The last decade is marked with acceleration of mergers, corporate restructuring and governance activities. M&A activity has been driven by factors such as technological change, globalization, free trade, deregulation, attempts to attain economies of scale, rise in entrepreneurship, and economic growth. Corporations need to adjust to the change in the environment and expand their markets to achieve growth and protection against volatile economic conditions. Firms can achieve international expansion through foreign direct investments (FDIs) which can take the form of cross-border acquisitions (brown-field investments) and Greenfield investments. This chapter covers an overview of the literature on the determinants of FDI forms of entry, and M&A activity followed with an empirical investigation of the firm-level determinants of foreign investment in Turkey with emphasis on cross-border acquisitions and Greenfield investments. Summary of the findings is followed with the economic implications of forms of FDI entry. The concluding remarks cover the implications of the results for policy makers.*

### INTRODUCTION

Increasing volatility and complexity of the business environment forces companies to reduce their vulnerability to adverse changes and enhance their competitiveness in the market. In addition to the emergence of new industries like e-commerce and biotechnology, old industries are being trans-

formed. The high rate of technological change and development in transportation and communications have increased the pace of globalization. The intensity of competition in global markets has led to deregulation in airlines, financial services, telecommunications, electricity and other utilities industries. Globalization is driven by reduced barriers to the free flow of goods and

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services and technological advancements that lead to better communication, information processing and transportation technologies (Hill, 2006). Firms can expand into international markets in a variety of ways such as licensing, franchising, strategic alliances exporting and through foreign direct investments (FDIs) with either a wholly- or partially-owned local enterprise.

Firms have economic and strategic motives for participating in mergers and acquisitions (M&As). The economic motive is to create value for shareholders through the realization of synergies that stem from additional revenues and savings in costs. Strategic motives aim to improve the strategic positioning of the firm to achieve long-term growth and protection against volatile conditions in the region. The quest to survive in the global market is a strategic driver of cross-border M&As.

The first part of this chapter includes a theoretical overview that covers country-level determinants of M&A activity and foreign direct investment (FDI), integrated with evidence from firm-level drivers of M&As and foreign investment. The second part of the chapter documents an empirical study that displays firm-level determinants of M&A activity and foreign investment in the 500 largest firms of the Istanbul Chamber of Industry in Turkey. The initial part of the empirical study focuses on the determinants of the M&A activity in the sample. The second part displays the foreign investment determinants with a comparative analysis of drivers of cross-border mergers and Greenfield investments. A summary of the findings is followed by a section that elaborates on the economic implications of the evidence on FDI and its forms of entry. Concluding remarks cover the implications of the results for policymakers of the host country.

There are several contributions of this study. While most of the studies on M&A activity rely on data from developed countries, this study documents differences in firm-level determinants of M&A activity and FDI modes of entry in an emerging country. Unlike most of the studies

in this field, the sample for this study includes unlisted firms which are surrounded by higher information asymmetry and documents the differences in firm-level drivers of M&As and foreign investment for private and publicly traded firms.

The results have implications for policymakers of the host country and firm managers that aim to attract FDI. The higher likelihood of foreign investment in R&D-intensive firms implies the need to increase R&D efforts at the country level. The findings, therefore, point to the need for government investment in accumulating knowledge and human capital that will serve to reduce the technological gap between foreign investors and local firms. The results indicate that M&A involvement is a means of sharing risks and attaining improvements in efficiency for corporations. Foreign investment seems to be driven by high exports, R&D intensity, production of high value added goods, and existence of operational efficiency in local firms. These findings reveal the need for local firms to focus on productivity and innovativeness in the products and services they provide to generate high value added output that will increase their competitive advantage in global markets.

## **THEORETICAL BACKGROUND**

The studies on determinants of mergers and acquisitions can be grouped as those that focus on country-level drivers of M&A activity and firm-level analyses. After an overview of the literature on the country-level drivers of M&A activity, the theoretical background covers evidence on firm-level determinants of M&A activity with an emphasis on cross-border mergers and Greenfield investments.

### **Country-Level Determinants of FDI**

The existing literature on FDI determinants has generally focused on macroeconomic factors that

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