Cross-border M&A for Global Expansion Growing in Japan Also

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I. Introduction

Recent years have seen an increase in cross-border mergers and acquisitions by multinational firms, aimed at (1) industry consolidation involving neighboring countries, (2) the development of new markets by firms in mature advanced economies, and (3) the acquisition of advanced economy firms and their brands by fast-growing emerging market firms[1]. Although the number and size of those deals has declined of late because of the financial crisis, which has lowered the earnings outlook of acquiring firms and made it harder to get funding, M&As appear to be resuming growth in step with the global economic recovery, as we explain later. In this paper, we overview the global trend in cross-border M&As over the last decade for deals valued at $1 billion or more[2], and also look at M&A activity by Japanese firms.

II. Cross-border M&A picking up globally

1. Cross-border M&A megadeals, primarily by European firms

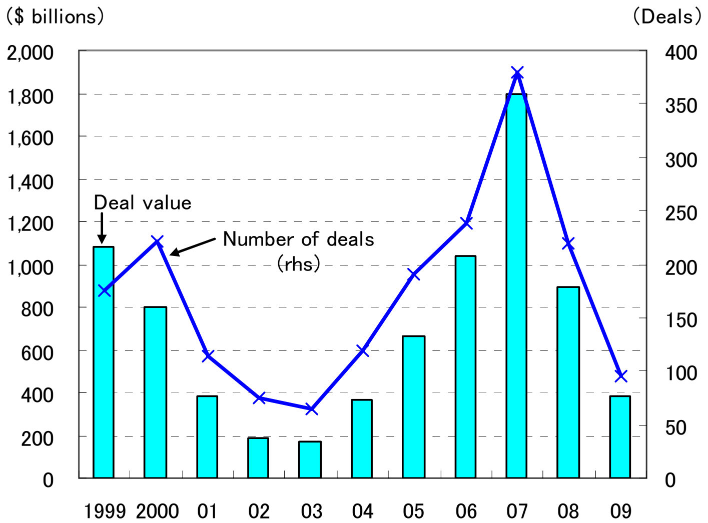
The value of cross-border M&A deals worldwide grew by more than a factor of 10 over a four-year period, from $170 billion in 2003 to $1.8 trillion in 2007. The drivers of this growth have been currency integration and deregulation in Europe and an increase in deals involving emerging market firms. The value of these deals shot up in 2007 because of a large number of megadeals, including the $98.2 billion acquisition of the Dutch firm ABN Amro by three European banks, including the Royal Bank of Scotland (RBS). The total value of deals dropped back to $890 billion in 2008, close to the $1 trillion recorded in 2006. Because of the financial crisis, deals thus far in 2009 are running at an annualized total of $390 billion, less than half of that in 2008.

All of the deals valued over $20 billion during the last 10 years have been acquisitions by European firms of either North American or other European firms (Figure 2). Until 2005, there were acquisitions by one large firm of another large firm

1 We define cross-border M&A as a merger, acquisition, or equity investment where the parent companies of the two sides involved are based in different countries.
2 Data collected and analyzed based on announced figures. Some of the deals shown have yet to fully close.

in the same industry for purposes of either industry consolidation or developing new markets (explained later), but in 2006 and 2007, the total value of deals was boosted by financial institutions and funds acquiring non-financial firms.

Figure 1: Cross-border M&A worldwide



Note: Figures for 2009 are annualized from January-June data.
Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker.

Figure 2: Cross-border M&A megadeals ($20 billion and larger)

	Acquiring company	Sector	Home country	Acquired company	Sector	Home country	Deal value ($ billions)
1999	Vodafone	Telecom	UK	AirTouch Communications	Telecom	US	65.8
	BP	Petroleum	UK	Atlantic Richmond	Petroleum	US	33.5
	Rhone-Poulenc	Chemicals	France	Hoechst	Chemicals	Germany	28.4
	Mannesmann	Telecom	Germany	Orange	Telecom	UK	35.3
	Vodafone	Telecom	UK	Mannesmann	Telecom	Germany	202.8
2000	Unilever	Foods	UK	Bestfoods	Foods	US	23.7
	France Telecom	Telecom	France	Orange	Telecom	UK	39.7
	Vivendi	Infrastructure	France	Seagram	Media	Canada	40.8
	Deutsche Telekom	Telecom	Germany	VoiceStream Wireless	Telecom	US	34.1
2004	Royal Dutch	Oil & gas	The Netherlands	Shell Transport & Trading	Oil & gas	UK	80.3
2005	Telefonica	Telecom	Spain	O2	Telecom	UK	31.8
2006	Investor group including GIC	–	–	BAA	Infrastructure	UK	30.2
	Iberdrola	Electric power	Spain	Scottish Power	Electric power	UK	26.6
2007	Investor group including KKR	–	–	Alliance Boots	Retail	UK	21.5
	Imperial Tobacco	Tobacco	UK	Altadis	Tobacco	Spain	21.5
	Enel	Electric power	Italy	Endesa	Electric power	Spain	26.4
	RFS Holding (a fund owned by RBS)	Finance	The Netherlands	ABN Amro	Finance	The Netherlands	98.2
	Rio Tinto	Mining	UK	Alcan	Mining	Canada	43.0
2008	Inbev	Foods	Belgium	Anheuser-Busch	Foods	US	60.4
	Roche	Pharmaceuticals	Switzerland	Genentech	Pharmaceuticals	US	46.7
2009	Xstrata	Mining	Switzerland	Anglo American	Mining	UK	42.5

Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker and news reports.

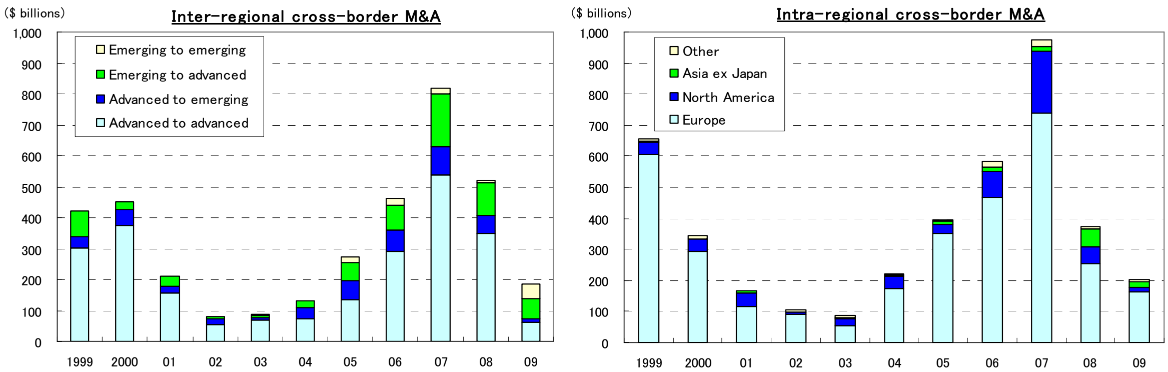
Japanese firms are also becoming more active in cross-border M&A, but the aggregate of their deals since 1999 only totals $200 billion, a mere 3% of the worldwide total of $7.6 trillion. Even in 2008, their biggest year over the past decade, Japanese firms were only involved in 16 deals valued at $44.7 billion.

2. M&A between regions and within regions

We look at global trend in cross-border M&As over the past ten years for both inter-regional and intra-regional deals. Looking first at the inter-regional deals, we divide the world into advanced areas --- North America, Europe, Oceania, and Japan; and emerging areas --- Latin America, the Middle East, and Africa.

The total value of inter-regional deals since 1999 is $3.5 trillion, which is 46% of the $7.6 trillion total for all cross-border M&A. M&As between advanced countries account for the lion's share at $2.4 trillion, and has been in a rising trend since 2002 (Figure 3). Among deals between firms in advanced countries and firms in emerging economies, those in which the acquirer was based in an emerging country accounted for a greater share of deal value, the more so since 2003.

Figure 3: Cross-border M&A by region



Note: 1. Domestic deals are considered cross-border if they involve the local subsidiary of an overseas firm.
2. Figures for 2009 are annualized from January-June data.

Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker.

We divide the intra-regional deals into four categories, Europe (with the largest deal value), North America, Asia ex Japan, and other. The total value of intra-regional deals since 1999 is $4.1 trillion, of which $3.2 trillion was accounted for by Europe, by far the most owing to the large number of countries in that region. One reason for the recent growth in this activity in Europe is the increase in acquisitions by private equity funds, which appear to have accounted for about 10% (in value terms) of Europe's total intra-regional cross-border M&As in 2007. In 2008, although the value of intra-regional M&A deals in Europe and North America declined because of the financial crisis, the value of deals in Asia ex Japan reached a 10-year high of $60 billion. We take a more detailed look at this below.

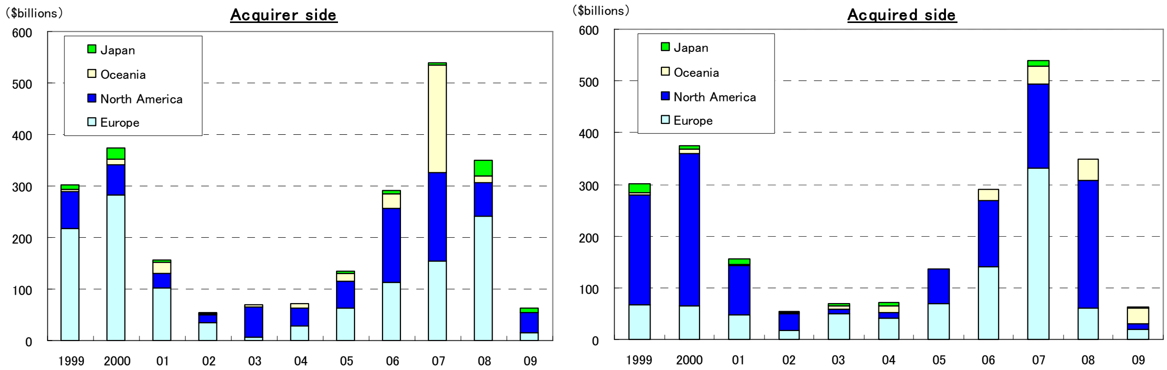
III. Three types of cross-border M&A

1. Cross-border M&A between advanced countries

1) M&A among European and North American firms seeking to expand their global market share

As noted above, deals between advanced countries account for the largest share of inter-regional cross-border M&A deal value. This can be attributed to efforts by European and North American companies to expand global market share in response to the maturation of their home markets (Figure 4). Over the past 10 years, there has been a noticeable trend of European companies in the food and pharmaceutical sectors moving into the huge US market.

Figure 4: Inter-regional M&A in advanced economies



Note: Figures for 2009 are annualized from January-June data.
Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker.

Examples of such deals include UK-based Unilever's acquisition of Best Foods, a major manufacturer of mayonnaise, for ¥23.7 billion in 2000, and acquisitions by Switzerland-based Nestle of Ralston Purina, a leading pet food manufacturer, for $11.7 billion in 2001, and of Gerber, a leading baby food maker, for $5.5 billion in 2007. The acquisition by Belgium-based Inbev of Anheuser-Busch for $60.4 billion in 2008 created the world's largest beer company, and attracted a lot of attention.

Acquisitions by North American firms of European firms include, in the pharmaceutical sector, US firms acquiring generic drug businesses and sales networks in Europe to raise their global share (Figure 5). In 2007, the acquisition of European firms by investor consortiums based primarily in the US, including JPMorgan and an Australian infrastructure fund acquiring Southern Water, a water utility in England, for $8.5 billion greatly increased the total value of deals involving North American and Oceania firms acquiring European firms.

Figure 5: Key cross-border M&A deals in the pharmaceutical sector

European firms acquiring American firms

Year	Acquiring company	Home country	Acquired company	Home country	Deal value ($ billions)	Comments
2005	Novartis	Switzerland	Eon Labs	US	1.7	Creates world's largest generic drug company
2007	Shire Pharmaceuticals	UK	New River Pharmaceuticals	US	2.7	UK's No. 3 acquires development partner
2008	Novartis	Switzerland	Alcon	US	10.5	Acquires major US eye care company
	Fresenius	Germany	APP Pharmaceuticals	US	5.6	Enters US market for IV generic drugs

North American firms acquiring European firms

Year	Acquiring company	Home country	Acquired company	Home country	Deal value ($ billions)	Comments
2000	Abbot Laboratories	US	BASF's pharmaceutical division	Germany	6.9	To strengthen sales base in Europe and Japan
2007	Mylan	US	Merck's generic drugs business	Germany	6.6	Acquires world's No. 5 to become No. 3
2009	Abbot Laboratories	US	Pharmaceutical business of major chemicals firm Solvay	Belgium	6.6	Acquires new drugs and sales network in Eastern Europe and Asia
	Johnson & Johnson	US	Crucell (bio venture)	The Netherlands	0.4	Takes 18% stake in capital and business tie-up

Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker and news reports.

2) Active industry consolidation in Europe

Europe had the largest total value of intra-regional cross-border M&As, and we attribute this to the EU's move to a single currency in 1999 and adoption of international accounting standards in 2005, changes that eliminated the need for bilateral adjustments of currency and accounting differences. Consequently, as each country deregulated, the major firms in those countries became active in the M&A arena to expand their share of, and become one of the dominant players in, the EU market.

The telecom sector, for example, has accounted for the largest share of the world's cross-border M&As over the past 10 years[3]. The standardization of mobile phone communication formats sparked a competition to expand global reach, and the major telecom providers of each country in the EU have actively pursued M&As (Figure 6).

The specific deals that were signed around 2000, including between the major providers in the UK, Germany, and France, resulted in an industry consolidation, and since 2005, the majors have been actively doing deals to establish a presence in Eastern Europe, which is the emerging area of the EU. By acquiring a leading local provider, these companies can quickly establish their network and customer base.

With the maturation of the EU's mobile phone market, there have recently been M&A deals aimed at expanding market share in the broadband business, which is the telecom sector's growth segment, and at establishing a presence in India and other

[3] Over the past decade, the sector with the largest total value of M&A deals was telecom ($1.3 trillion), followed by finance ($1.2 trillion) and then electric power and energy ($1.2 billion).

emerging markets. We expect to see continued industry consolidation by way of cross-border M&A.

Figure 6: Key M&A deals in Europe's telecom sector

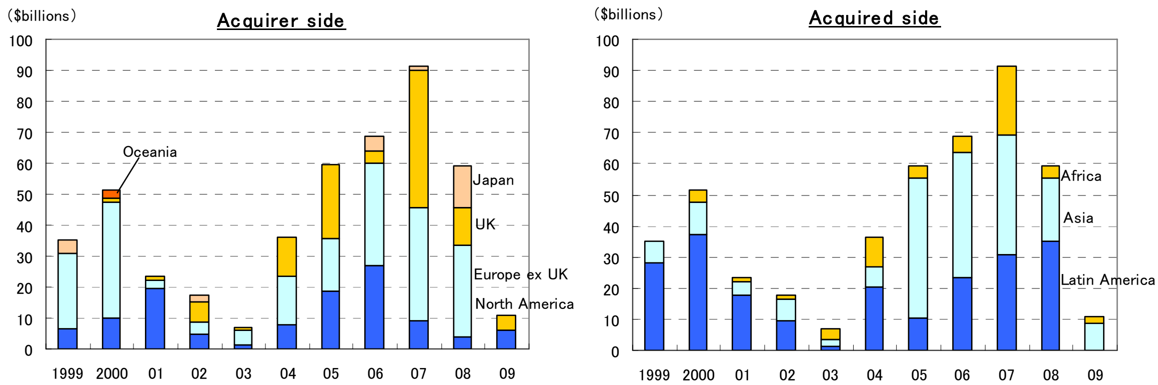
Year	Acquiring company	Home country	Acquired company	Home country	Deal value ($ billions)	Comments
1999	Vodafone	UK	AirTouch Communications	US	65.8	Connects the UK and US and becomes world's largest mobile provider.
	Deutsche Telekom	Germany	One2One	UK	13.6	Acquires UK's No. 4 to expand share of UK's mobile phone market.
	Mannesmann	Germany	Orange	UK	35.3	Acquires UK's No. 3 to become Europe's largest mobile phone provider.
	Vodafone	UK	Mannesmann	Germany	202.8	Acquires largest phone company in hostile acquisition.
2000	France Telecom	France	Orange	UK	39.7	Acquires UK's No. 3, sold as part of Vodafone acquisition.
	Telefonica	Spain	Four major Latin American telecom providers	–	19.1	Expands share of mobile phone market in Spanish- and Portugese-speaking countries.
2005	Vodafone	UK	Oskar Mobile	Czech Republic	4.4	Acquires Czech Republic's No. 3 mobile phone provider.
	Telefonica	Spain	Cesky Telecom	Czech Republic	4.7	Acquires state-owned enterprise from Czech government.
	TeliaSonera	Sweden	Turkcell	Turkey	3.1	Acquires Turkey's largest mobile provider with a 70% market share.
	Telenor	Norway	Vodafone Sweden	Sweden	1.2	Norway's largest provider acquires Vodafone's Swedish broadband business.
2007	Vodafone	UK	Hutchison Essar	India	12.8	Acquires India's No. 4 mobile phone provider.

Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker and news reports.

2. Acquisitions by advanced economy firms of emerging economy firms

Acquisitions by advanced economy firms of emerging economy firms have totaled more than $450 billion. European firms have been the most active buyers between 2004 and 2007, accounting for 71.0% of the acquisitions (Figure 7). The sectors most often targeted for acquisition by European firms have been telecommunications, finance, and resources, in that order, with the objective of increasing global market share, just as with intra-European industry consolidation. Spanish firms were very actively moving into culturally similar Latin America in 1999 and 2000. The major oil firm Repsol acquired YPF of Argentina for $16.7 billion in 1999, and the telecommunications giant Telefonica used acquisitions totaling $19.1 billion to enter the Brazilian, Argentinean, and Peruvian markets in 2000.

Figure 7: Acquisitions by advanced economy firms of emerging economy firms



Note: Figures for 2009 are annualized from January-June data.
Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker.

UK firms have been focusing on markets in Asia and Africa since 2004. In the telecom sector, Vodafone, which had been building its communications network in Europe, moved into South Africa, Turkey, and India (making acquisitions totaling $20.1 billion from 2005 until 2007), and there were deals in a number of other sectors, including HSBC's investments in China's Bank of Communications (BoCom) and China Ping An Life Insurance (a total of $2.8 billion in 2004-05), and in 2005 the $6.4 billion acquisition by the world's third-largest brewer, UK-based SABMiller, of Latin America's third-largest brewer, Columbia-based Bavaria.

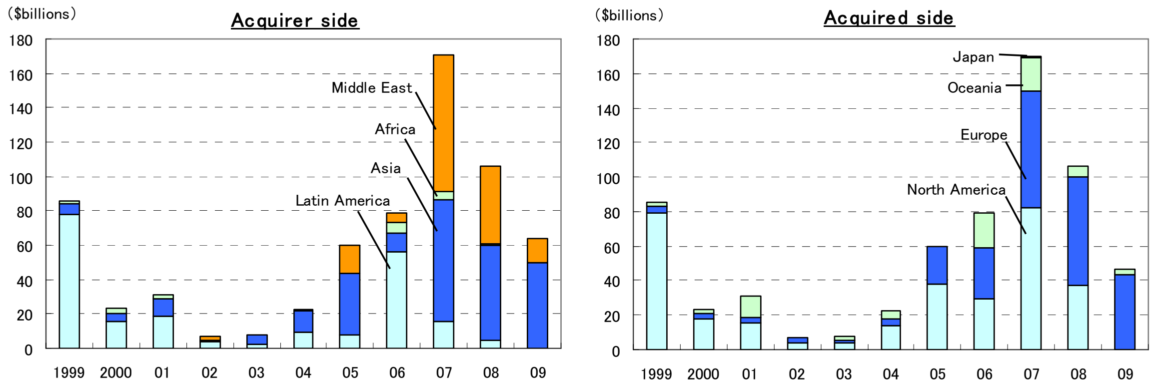
In the resources sector, M&A activity has centered on emerging markets. The Luxembourg-based steel giant Arcelor Mittal invested $3 billion in the China Oriental Group, also a major steel producer, in 2007. We expect to see further growth in M&As aimed at establishing a presence in emerging markets by companies that have already expanded their share of advanced economy markets.

3. Acquisitions by emerging economy firms of advanced economy firms

1) Investment in US and European firms by sovereign wealth funds (SWF)

Acquisitions by emerging economy firms of advanced economy firms over the past 10 years have totaled $620 billion (Figure 8). This is $170 billion more than acquisitions in the reverse direction, with much of that difference coming since 2003. The sharp increase in the value of acquisitions by Asian and Middle Eastern firms of European and North American firms in 2007 and 2008 can be partly explained by sovereign wealth funds in those regions investing in European and US financial institutions[4].

Figure 8: Acquisitions by emerging economy firms of advanced economy firms



Note: Figures for 2009 are annualized from January-June data.
Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker.

[4] For more on investing by sovereign wealth funds, see Tetsuya Kamiyama, *Daitou suru Kokufu Fando* (The emergence of sovereign wealth funds), *Capital Market Quarterly*, Winter 2008 issue (in Japanese).

Citigroup, for example, received total investments of $14.4 billion from Abu Dhabi Investment Authority (ADIA) and Singapore's Government Investment Corporation (GIC), while Merrill Lynch received $8.4 billion in investment from three different sovereign wealth funds. There is a possibility that sovereign wealth funds will increase their investments in nonfinancial corporations of advanced economies for strategic objectives, i.e., to obtain technology.

Although the risk of political issues arising between sovereign wealth funds and the countries they invest in has been made an issue, there have been few such problems thus far, and the funds have been quite circumspect when investing in advanced economies. The ADIA, for example, has announced that it will strictly adhere to the Generally Accepted Principles and Practices (the "Santiago Principles") established under the auspices of the IMF[5].

Figure 9: Major instances of sovereign wealth fund investments

Name of sovereign wealth fund	Home country	Firm being invested in	Home country	Amount ($ billions)
Abu Dhabi Investment Authority (ADIA)	United Arab Emirates	Citigroup	US	7.5
Kuwait Investment Authority (KIA)	Kuwait	Merrill Lynch	US	2.0
Korea Investment Corporation	Korea	Merrill Lynch	US	2.0
Temasek	Singapore	Merrill Lynch	US	4.4
Government of Singapore Investment Corporation (GIC)	Singapore	UBS	Switzerland	9.8
		Citigroup	US	6.9
China Investment Corporation	China	Blackstone	US	3.0

Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker and news reports.

2) Rapid growth in acquisitions by emerging market firms

Emerging economies now have firms with substantial cash reserves as a result of rapid growth fueled by globalization and their home economy's growth, and those firms have been quite active in acquiring advanced economy firms since 2006. One area where this is true is both horizontal and vertical integration by large resource firms. In 2006, Vale do Rio Doce of Brazil, the world's largest mining company, acquired the Canadian nickel mining company Inco for $20.7 billion, and the Mexican cement major Cemex acquired the Australian building materials firm Rinker for $15.4 billion, pushing up the total value of deals made by Latin American firms. Vale also prevailed in battles to acquire two other major advanced economy firms, US-based Phelps Dodge, the world's largest copper mining company, and Canada-based Teck Cominco, a leading producer of nonferrous metals. Cemex used its acquisition to solidify its business base in the US.

5 See the press release from the Abu Dhabi Investment Authority dated 11 October 2008 (http://www.adia.ae/ADIA_AE_press.asp). For more on the guidelines followed by sovereign wealth funds, see Tetsuya Kamiyama, *Koudoukihan no Sakutei to Saikin no Doukou* (SWF: establishing guidelines and recent trends), *Capital Market Quarterly*, Winter 2009 issue (in Japanese).

There have also been deals aimed at acquiring brands owned by advanced economy firms. India's Tata Group acquired the large US chemicals firm General Chemical and the UK-based luxury car brand Jaguar, and China's Lenovo Group bought IBM's PC business. We expect emerging market firms flush with cash as a result of strong growth to increasingly move to acquire advanced economy firms for purposes of expanding global share as well as acquiring brands and technology.

IV. Rising prospects for growth in Asia

1. Asia attracts investors' attention

The number of cross-border M&A deals has declined as a result of the financial crisis, but to gauge the future trend we reference a survey on foreign direct investment by the United Nations Conference on Trade and Development (UNCTAD). That survey, the World Investment Prospects Survey 2009-2011, was conducted from February to May 2009 and collected answers from 241 transnational corporations doing business in multiple countries and regions.

In brief, the results of the survey predicted an increase in foreign direct investment, including cross-border M&A, from 2011. Only 22% of the firms answered that their investments in 2009 would decline relative to 2008, while 58% expected that investment to decline, a consequence of the financial crisis (Figure 10). These numbers improved slightly for 2010, when 33% expect an increase and 41% expect a decline, and for 2011 fully half (50%) of the firms responding expect an increase and only 19% expect a decline. At this point, a genuine recovery in foreign direct investment is expected in 2011, and cross-border M&A should recover around the same time.

Figure 10: Foreign direct investment plans over the next three years (2009-11)

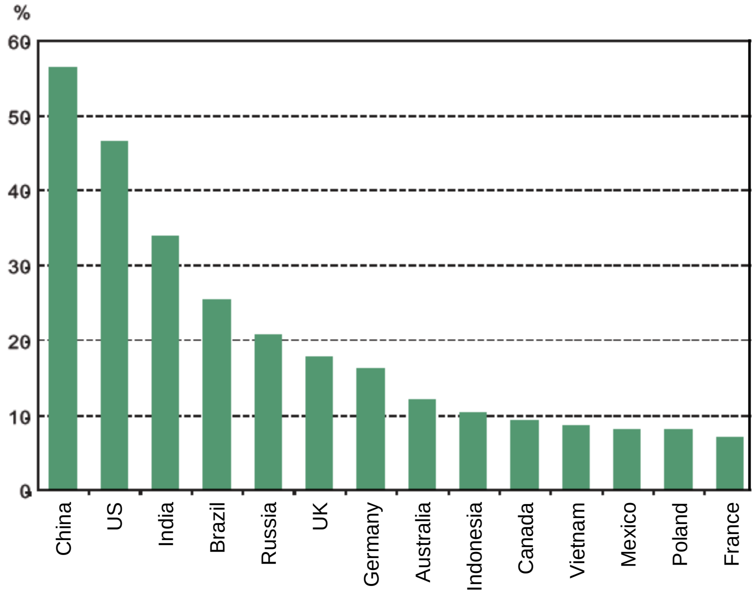
(%)

Foreign direct investment plans	Increase	Maintain current level	Decrease
2009	22	20	58
2010	33	26	41
2011	50	31	19

Note: 241 companies responded. Answers are relative to 2008.
Source: Nomura Institute of Capital Markets Research, based on UNCTAD data.

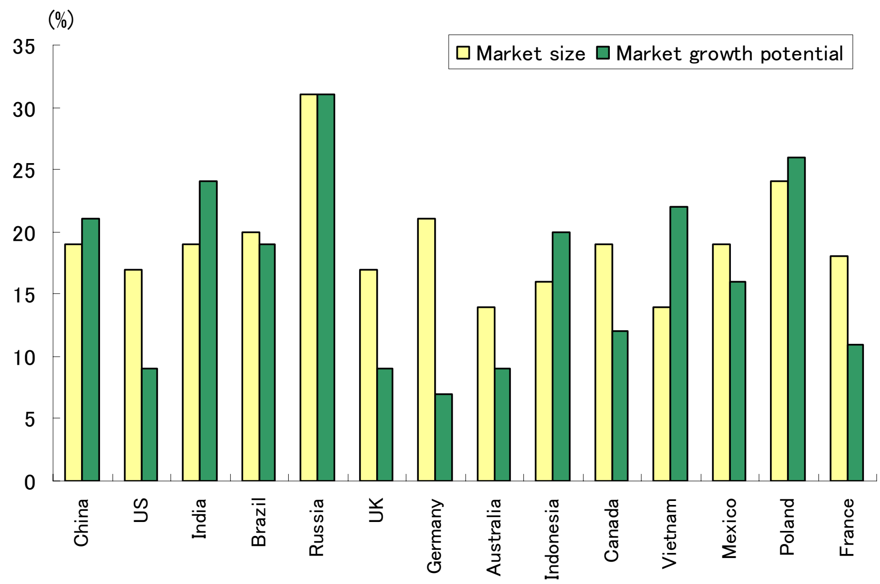
The detailed data at the country level ranks China as the most attractive destination for investment by global farms (56%), followed by the US (47%), India (34%), Brazil (25%), and Russia (21%) in the No. 5 spot (Figure 11). It is notable that four of the five top-ranked countries are BRICs countries, with the US the lone exception.

Figure 11: Favored countries for foreign direct investment (2009-2011)



Note: 241 companies responded. Percentages reflect multiple answers.
Source: Nomura Institute of Capital Markets Research, based on UNCTAD data.

Figure 12: Reasons for each country's desirability (top two)



Note: 241 companies responded. Percentages reflect multiple answers.
Source: Nomura Institute of Capital Markets Research, based on UNCTAD data.

The most important factor determining this attractiveness was market size, followed by market growth. In terms of market size, Russia and Poland ranked highly worldwide, while China and India ranked highly within Asia (Figure 12). In terms of market growth, Russia ranked highly, and in Asia it was India followed by China. There were also strong expectations for market growth in Indonesia and Vietnam, both members of ASEAN.

The survey indicates that transnational corporations have a strong appetite for investment from 2011, and Asia is a favored destination, based on expected market growth.

2. Valuation of targeted firms rising in Asia

We expect an increase in acquisitions of Asian firms based on expected market growth, and given that the growth potential and valuations of the target firm are important factors affecting a deal, we look next at cross-border M&A valuations. We value deals in two ways, the nominal value of each deal and the deal value as a multiple of earnings before interest and taxes (EBIT), i.e., as a valuation multiple.

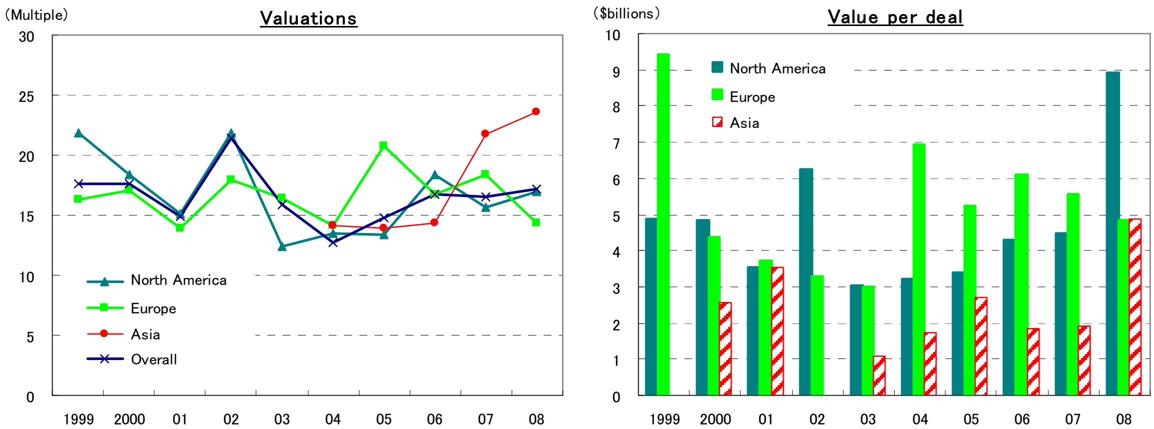
Comparing first the valuations of cross-border M&A with domestic M&A, with the exception of 2002 and 2008, multiples ranged from 13X to 18X in both cases (Figure 13). There were few large cross-border acquisitions in 2002, and the totals were affected by just a few deals, including Microsoft's acquisition of a customer relationship management software firm (at 53.8X) and the acquisition by Publicis, a leading European advertising firm, of a US ad agency (at 29.6X). In 2008, the financial crisis caused the number of deals to decline, particularly in the second half of the year, and although the valuations of domestic deals declined, cross-border deals were still being closed at high valuations.

Figure 13: M&A valuations

Note: Valuations are the median ratio of deal value to EBIT.
Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker.

Classified by the region of the acquired company, valuations since 2007 have been stable in North America and declined slightly in Europe, but have risen in Asia including Japan to over 20X (Figure 14).

Figure 14: Valuations and deal values of cross-border M&A



Note: 1. Valuations are median ratio of deal value to EBIT. Shows data on deals for which data was available.
2. Valuations and average deal values not shown for regions in years when there are less than three deals

Source: Nomura Institute of Capital Markets Research, based on data from Thomson One Banker.

Valuations were high in North America and Europe in 2005 and 2006 because deals between financial institutions and acquisitions/investments by investment funds were done at high valuations. Excluding those, the valuations of large deals were relatively stable. In addition, the increase in the average deal value in 2008 can be attributed to large deals associated with the restructuring of the beer and pharmaceutical sectors, as already noted.

Expectations of future profits have been kept deals at high valuations in Asia since 2007: in addition to the major Spanish bank BBVA's investment in China Citic Bank (CNCB) in the financial sector ($1.2 billion at 252X), Daiichi Sankyo acquired Ranbaxy Laboratories ($5 billion at 86.7X) and Telekom Malaysia acquired India's Idea Cellular ($1.7 billion at 35.6X). The value of each deal averaged over $4.9 billion in Asia and over $4.8 billion in Europe in 2008, a higher than the $4.5 billion average in North America in 2007, and these deals may continue getting larger.

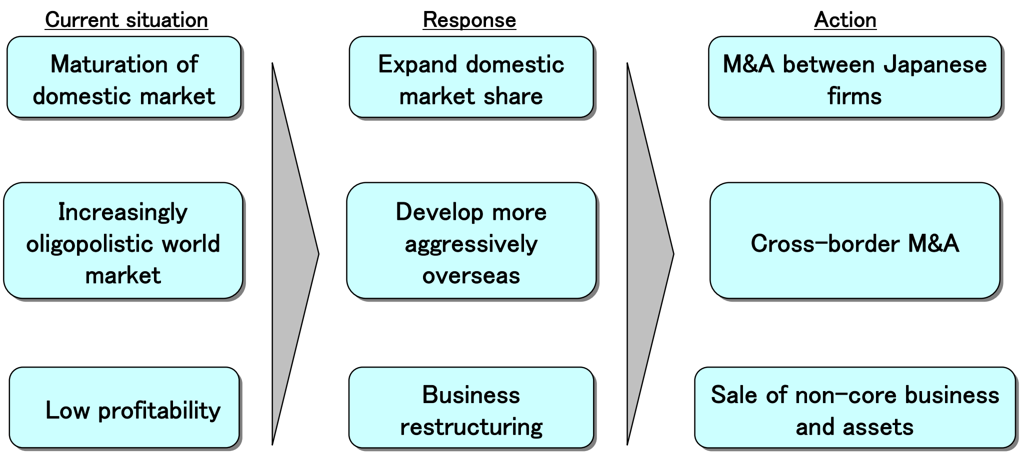
The above numbers indicate that the acquisition of large firms in Europe and the US are being made at relatively stable valuations. In contrast, Asian firms, which have high growth prospects, are being acquired at increasingly higher valuations, and this probably makes it more important for acquirers to shift through and select acquisition candidates based on their growth potential and market valuations.

V. Asian Business Development and Cross-Border M&A by Japanese Firms

1. M&A as a Solution to Problems at Japanese Firms

We turn now to the situation at Japanese firms, which need to deal with the long-standing problems of a maturing domestic market, the increasingly smaller number of firms dominating global markets, and low profitability by restructuring their businesses, aggressively developing overseas markets, and expanding their domestic market share in step with domestic industry consolidation (Figure 15). This explains why Japanese firms have become more active in developing overseas markets by establishing local subsidiaries and acquiring local firms.

Figure 15: Issues facing Japanese Firms

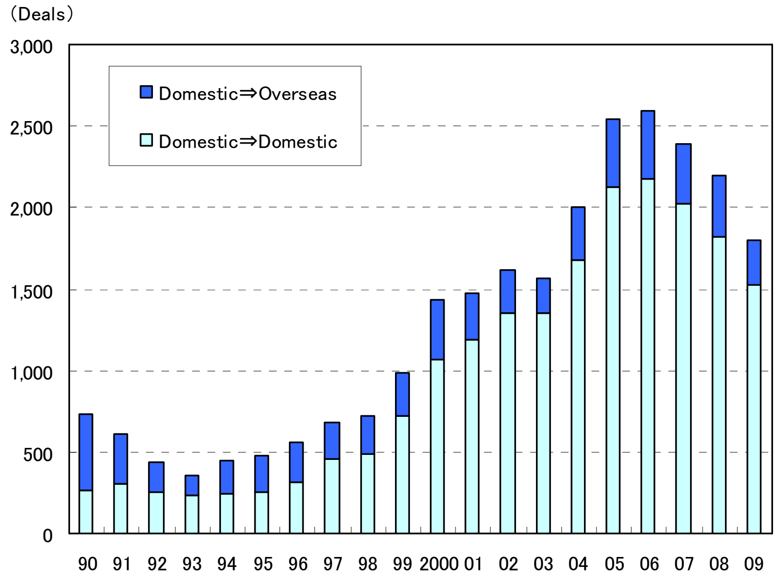


Source: Nomura Institute of Capital Markets Research.

In response to the increasingly intense competition worldwide, Japanese firms have worked to expand their share of global markets in recent years by moving into Asia, where growth looks promising. To that end, Japanese firms' acquisitions of both domestic and foreign firms increased by a factor of 2.2X over a 10-year period, from 987 deals in 1999 to 2,201 deals in 2008, despite a decline since 2007 (Figure 16).

Next, we look at the market valuations of the firms that have announced cross-border acquisitions, which are now widely used by Japanese firms.

Figure 16: Number of deals involving Japanese firms



Note: Figures for 2009 are annualized from January-June data.
Source: Nomura Institute of Capital Markets Research, based on data published in MARR, by Recof.

2. Market valuations of cross-border M&A deals

We measure here the market valuation of Japanese firms that have announced cross-border M&A deals by looking at their share price before and after the announcement. Specifically, we measured the excess return over their industry index of the companies announcing the 96 deals valued at $100 million or higher from 2005 until 2008, measured over the periods from five trading days prior to the announcement to five trading days after and to 20 trading days after[6].

The median excess return[7] was 1.3% until five trading days after the announcement and 1.4% for until 20 trading days after (Figure 17). Looked at by deal size, the excess return was 2.5% (45 trading days after) and 2.0% (20 trading days after) for deals valued at it least $500 million, higher than the 1.0% (five trading days after) and 0.4% (20 trading days after) excess return for deals valued below $500 million. This suggests that expectations are higher for larger deals (Figure 18).

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6 For the performance benchmark, we use the TSE industry index to which the announcing firm is assigned.

7 When rank ordering by size, we use the median figure.

Figure 17: Excess return on firms announcing cross-border M&A deals (96 deals)

	Value of deal ($ mns)	After five trading days	After 20 trading days
Average	732	1.6%	0.5%
Median	245	1.3%	1.4%
Maximum	7,839	27.3%	19.4%
Minimum	100	-16.5%	-26.4%
Std. dev	1,245	6.0%	7.3%

Source: Nomura Institute of Capital Markets Research, based on Bloomberg data.

Figure 18: Excess return on firms announcing cross-border M&A deals (96 deals)

＜Deals valued at at least $500 million (28 deals)＞

	Value of deal ($ mns)	After five trading days	After 20 trading days
Average	1,990	2.6%	3.2%
Median	1,236	2.5%	2.0%
Maximum	7,839	13.9%	19.4%
Minimum	500	-9.3%	-12.1%
Std. dev	1,765	5.4%	7.4%

＜Deals valued at below $500 million (68 deals)＞

	Value of deal ($ mns)	After five trading days	After 20 trading days
Average	214	1.2%	-0.6%
Median	194	1.0%	0.4%
Maximum	493	27.3%	16.0%
Minimum	100	-16.5%	-26.4%
Std. dev	101	6.3%	7.0%

Source: Nomura Institute of Capital Markets Research, based on Bloomberg data.

Excess returns were higher for acquisitions of companies located in Asia or Oceania, 1.9% by five days after and 2.4% by 20 days after, as shown in Figure 19. The standard deviation in excess return among companies announcing an acquisition was 6.0% (five trading days after) and 7.3% (20 trading days after) for all deals, and relatively lower at 3.4% (five trading days after) and 6.4% (20 trading days after) for acquisitions of firms located in Asia or Oceania. This higher excess return and lower standard deviation suggests that the market tends to assign higher valuations to those deals in which the acquired firm is located in Asia or Oceania.

We look below at specific examples of Japanese firms developing their Asian business.

Figure 19: Excess return on firms announcing cross-border M&A deals in Asia and Oceania (38 deals)

	Value of deal ($ mns)	After five trading days	After 20 trading days
Average	588	1.8%	1.3%
Median	258	1.9%	2.4%
Maximum	3,442	7.4%	16.0%
Minimum	100	-5.8%	-8.2%
Std. dev	777	3.4%	6.4%

Source: Nomura Institute of Capital Markets Research, based on Bloomberg data.

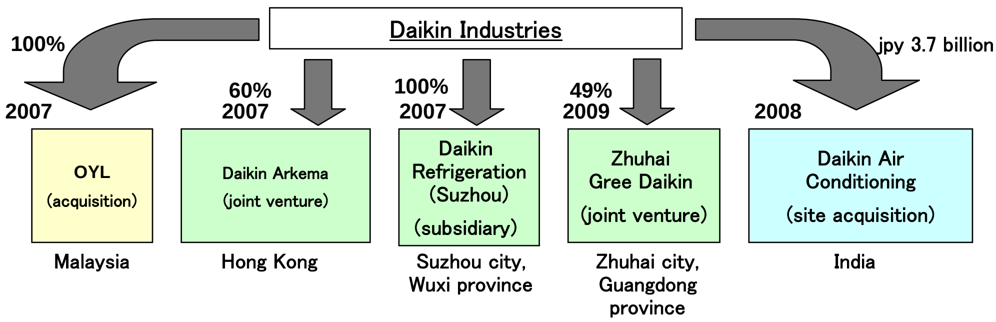
3. Japanese firms' use of M&A to expand overseas

1) Acquiring local firms and establishing local subsidiaries in Asia

In the past, when Japanese firms sought to establish manufacturing operations and develop new markets in Asia, they would either establish a local subsidiary or acquire a large firm that already had a brand, manufacturing facilities, and sales network.

For example, since moving into the European market in 1973, Daikin Industries, the world leader in inverter air-conditioners (commercial and residential), has been using a combination of acquiring local firms and establishing joint ventures and subsidiaries to develop its overseas business, and in recent years it has aggressively moved into China and other countries in Asia (Figure 20). It acquired Malaysia-based OYL Industries, the world's fourth largest company in the large-scale commercial HVAC segment, in January 2007, an acquisition that in addition to helping with its expansion in Asia, also helped it to develop the North American market through OYL's US subsidiary. When Daikin expanded in the Chinese mainland in September 2007 and Hong Kong in October 2007, it either went solo by establishing its own subsidiary or, if technical cooperation was needed, established a joint venture. In March 2009, it established a joint venture for the manufacture of core components and molds with China's Gree Electric Appliances, now the world leader in conventional air conditioners. Daikin's objective was to combine its technological expertise with Gree's low-cost purchasing and manufacturing capabilities to raise its presence in the global market for inverter air-conditioners.

Figure 20: Daikin Industries major subsidiaries in Asia



Source: Nomura Institute of Capital Markets Research, based on disclosures and media reports.

A similar case occurred in the food industry, when Japan's No. 2 brewer Asahi Breweries expanded its presence in Asia by establishing a 50-50 joint venture with Tingyi, China's largest food company, in 2004. It has increasingly expanded its presence in Asia and Oceania since January 2009, purchasing a 20% stake in Tsingtao Brewery, a leading beer manufacturer in China and acquiring Schweppes Australia, a drink subsidiary of the Cadbury group, which is a major producer of sweets based in the UK.

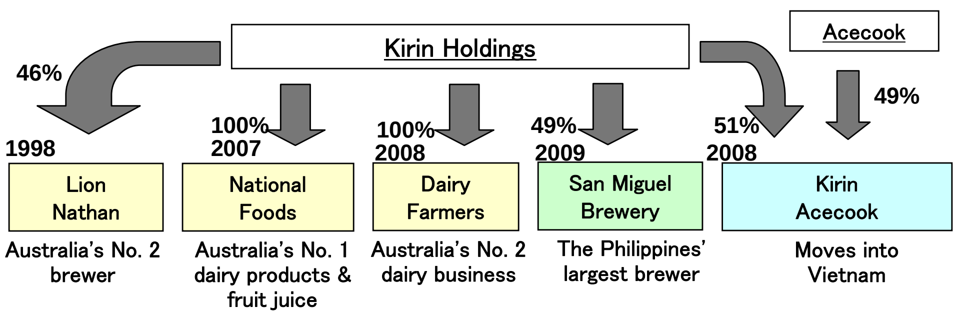
Japanese firms have thus made acquisitions and equity investments, as well as established joint ventures and subsidiaries, to enter and expand in new markets, and we expect to see further use of M&A aimed at acquiring local market brands and sales networks in the future.

2) Mergers between Japanese firms expanding in Asia

As was seen with inter-regional M&A deals, in recent years mergers between European and US global firms have made markets more oligopolistic, while the rapid growth of emerging market firms has intensified competition in global markets for a number of different industries, including food, pharmaceuticals, and telecommunications. Consequently, Japanese firms, which had previously been expanding in Asia on their own, are increasingly finding it necessary to partner with others.

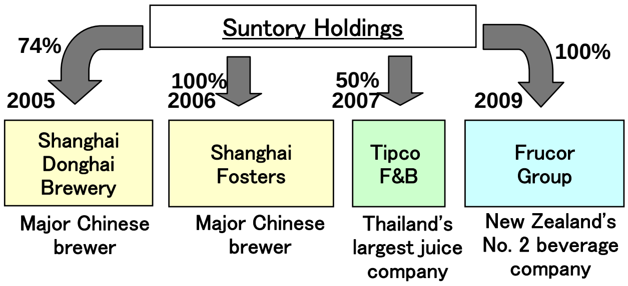
Large Japanese firms have thus begun joining forces with each other to develop their businesses across Asia. One example of this is the ongoing merger negotiation between Kirin Holdings and Suntory Holdings, both of which had been expanding in Asia on their own until now. Kirin has increased its share of Australia's beverage market by acquiring and investing in large companies starting in 1998. In 2008, it established a beverage joint venture in Vietnam with Acecook, and in 2009 it acquired the Philippines' largest brewer (Figure 21). Suntory estimates that it now has the largest share of the Shanghai beer market as a result of its acquisition of a major Shanghai brewer, and it has used acquisitions of and investments in large beverage companies to raise its market share in both Thailand and New Zealand (Figure 22). The merger of Kirin and Suntory, both of which have established presences throughout Asia, allows them to further buttress their brands in Asia, and puts them a major step closer to becoming Asia's largest food company.

Figure 21: Kirin Holdings' major subsidiaries in Asia and Oceania



Source: Nomura Institute of Capital Markets Research, based on disclosures and media reports.

Figure 22: Suntory Holdings' major subsidiaries in Asia and Oceania



Source: Nomura Institute of Capital Markets Research, based on disclosures and media reports.

Hence this merger has a similar objective and impact to a cross-border M&A deal, in that both domestic industry consolidation and the acquisition of overseas businesses are important objectives. There are other negotiations underway over capital tie-ups between major beverage firms, and it will be interesting to see whether there will be an increase in mergers between large Japanese firms that have already expanded overseas on their own.

Although not aimed at expansion in Asia, Suntory is now in the process of acquiring a major French beverage company, in order to obtain that company's product line up and license to sell in 20 European countries.

3) Acquiring growth subsidiaries and restructuring businesses

M&A is a tool for accelerating expansion into overseas markets, and there appears to a resurgence of such deals aimed at speeding up business restructuring, such as adding subsidiaries with growth businesses, so as to better compete with emerging market firms.

There have been some large-scale business restructurings in the past, one example of which was in 2002, when Matsushita Electric Industrial (now Panasonic) delisted four subsidiaries and made them into business domains, while also merging 22 regional sales companies. Hitachi Ltd., which had 16 listed subsidiaries, recently announced a tender offer to make wholly owned subsidiaries out of five listed subsidiaries chosen for their future revenue potential in the (1) information and communication systems, (2) social infrastructure, and (3) lithium-ion battery businesses. The tender offers were completed on 8 October (Figure 23). Its objectives in doing so were to (1) improve efficiency by merging related businesses, (2) improve the profitability of value added businesses through the prioritized allocation of management resources, and (3) become more capable of quickly responding to market trends. Hitachi had already been strengthening its value-added businesses in the integrated electronics sector in response to increased competition from emerging market firms, and we expect it will accelerate its business restructuring efforts through the use of M&A.

Figure 23: Listed subsidiaries of Hitachi Ltd. made into wholly owned subsidiaries

Subsidiary (listing exchange)	Year established	Sales ($ billions)	Operating profit ($ billions)	Change in parent company's ownership stake
Hitachi Systems & Services (TSE 2)	1978	126.2	7.3	51% to 99%
Hitachi Software Engineering (TSE 1)	1970	165.8	12.4	52% to 97%
Hitachi Information Systems (TSE 1)	1959	192.0	11.6	52% to 98%
Hitachi Plant Technologies (TSE 1)	1929	395.7	74.0	69% to 94%
Hitachi Maxell (TSE 1)	1960	172.7	−2.3	52% to 94%

Note: Sales and operating profit are for the period ended March 2009. Ownership stake prior to tender is as of announcement of public tender offer, and includes indirectly held shares.

Source: Nomura Institute of Capital Markets Research, based on disclosures.

The five listed companies have been expanding globally by establishing a datacenter operating company in China for its information and communications systems business to increase efficiency, by providing power stations and trains, primarily in emerging markets, in the social infrastructure business to improve profitability, and by offering products for hybrid vehicles in the lithium-ion battery business as a rapid response to market trends. Although Hitachi's restructuring equates to domestic M&A because it involves the acquisition of a subsidiary, it has the same objective as a cross-border M&A deal from the perspective of targeting growth businesses for global expansion. We do not think such moves are limited to the integrated electronics sector, and think a company's global reach can become an important criterion for selecting domestic and overseas companies to acquire in other industries, as well.

VI. Conclusion

The global trend in cross-border mergers and acquisitions provides evidence that competition has become fiercer as a result of the rise of emerging market firms and because of global companies merging with each other to consolidate their market dominance. Rapid expansion using cross-border M&A aimed at maintaining and improving a global market presence is becoming ever more important for Japanese firms, as well.

Although the financial crisis has affected corporate investment activity, transnational corporations are increasingly looking to invest in Asia based on Asia's potential for market growth, and fully half of those global firms expect their investment activity to pick up from 2011. Japanese firms are also leveraging cross-border M&A deals to increase their share of Asian markets and confront the competition on a global scale.

The Japanese firms that have announced cross-border M&As have outperformed their industry, and this excess return has been even greater for larger deals and deals where the acquired company is located in Asia and Oceania. This suggests that the market takes a positive view of such deals. In addition, mergers between Japanese firms can be viewed in the same light as cross-border M&A when their purpose is to reinforce their overseas regional brands and acquire growth businesses, and we expect such mergers to increase substantially.

We do not think it would be an exaggeration to say that cross-border M&A as well as deals between Japanese firms that have already established an overseas presence will have a major impact on whether Japanese firms succeed in expanding overseas in the future.

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