International Merger Activity and the National Regulation of Mergers: A UK Perspective

ANDY COSH and ALAN HUGHES
ESRC Centre for Business Research, University of Cambridge, UK

Abstract. This paper traces out recent changes in the globalisation of merger activity and considers its implications for national and international regulation of mergers and joint ventures. It argues that a large proportion of mergers involve small firms which may have an important effect on the competitive process and that regulation of large mergers should be complemented by industrial and financial policies to encourage the growth of smaller independent firms.

Key words: International mergers, competition policy

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I. Introduction

Since the mid 1980s a wave of international merger activity has swept across the industries of the OECD economies. It mirrors an earlier wave in the 1960s and 1970s which was however predominantly national in character (Hughes and Singh, 1980). The current rise in merger activity is associated with a revived belief in market forces which led to deregulation and integration of product and capital markets across Europe (Cosh, Hughes and Singh, 1992). The intensification of global competition, privatisations and the single market programme generated substantial industrial restructuring (Smith and Walter, 1992). The responses to these forces have been several. As in the 1960s and 1970s there has been an increase in domestic acquisitions, often supported by governments, as companies have attempted to attain a sufficient scale to respond to the competitive threat of other EU countries. This has also been associated with rationalising divestments as companies at the same time focus on core activities. Efficiency arguments along these lines were particularly prominent at a national level in the 1960s and 1970s, as individual European countries responded to what they perceived to be an “American challenge” to their independent industrial existence. The argument has undergone a renaissance in recent discussions of the gains from European integration in the run up to and aftermath of 1992. Now, however, the challenge is seen as much as Japanese as American, and the perceived need is for the creation of European, as opposed to national champions (Jacquemin, Buiges and Ilzkovitch, 1989). Thus, companies have engaged in cross-border activity, both through acquisitions and
joint ventures, in order, it is claimed, to be able to compete globally. The single market has also encouraged cross-border activity by non-EU companies as they seek to establish secure footholds within the European market. This response of companies to the changed circumstances accords with a view of a positive role of acquisitions and joint ventures in achieving economies of scale and scope and in enhancing R&D more quickly and with less risk than would be possible through internal expansion (Ordover and Willig, 1985; Scherer, 1994).

The growth in mergers and acquisitions and in cross-border activity of various types has brought a potential conflict between bank-based and market-based governance structures. One view of this process is that it represents the workings of an efficient market for corporate control and its extension in geographical coverage to Europe as a whole. Superior management teams can buy control of assets run by inferior teams, and hence improve the overall efficiency with which assets are used. Moreover, the threat of takeover is seen by itself as a deterrent against poor performance by incumbent management. The development of an international market for corporate control by introducing a wider range of potential raiders into individual national markets may strengthen the competitive process via this mechanism, as well as spread its influence outside its traditional sphere of operation in the stock market economies of the UK and the US. A particularly trenchant expression of this view was provided by a UK Minister at the Department of Trade and Industry who, after noting that four out of every five takeovers in the European Community occur in the UK, wrote “The Government is keen to secure the removal of unnecessary barriers to takeovers throughout the EC and to extend the benefits of open and efficient markets throughout the communities.... Many companies have told me of the difficulties they experience in finding acquisitions in Europe. It is time governments acted” (J. Redwood MP in Coopers and Lybrand, 1990).

Arguments for taking a more circumspect or hostile view may be counterposed to these efficiency arguments. The argument which views takeovers on the stock market as an integral and virtuous part of the competitive selection process, depends crucially upon stock market prices providing the correct signals to incumbent management, and disciplinary raiders alike. Prices which may be manipulated through insider trading to facilitate successful raids, or which over-react to short term or speculative pressures and leave incumbent management vulnerable to opportunistic bids may have no efficiency inducing properties. Even worse, they may encourage incumbent management to develop strategies designed to protect short term share price stability, rather than foster long term investment and innovative activity (Carty et al., 1991). More generally, corporate performance may depend upon a sense of mutual commitment between management, workforce, customers and suppliers. An environment in which the outcome of bids is determined by equity holders alone threatens to produce breaches of trust in these relationships may have a generally inhibiting effect on actions to raise economic efficiency (Schleifer and Summers, 1988). It is in this connection important to emphasise that the usefulness of takeovers as a disciplinary mechanism must be judged by comparison with other