Mergers & Acquisitions NOTE

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Editorial

By Klaus Regling, Director General, DG ECFIN

I am delighted to launch the first issue of DG ECFIN's mergers and acquisitions note. It is a subject which merits special attention, because mergers and acquisitions (M&A) affect all of us in the EU, whether we are consumers, entrepreneurs, academics, regulators or policymakers.

Consumers may or may not benefit from mergers and acquisitions. The pooling of assets through M&A can lead to efficiency gains, with benefits to consumers if the gains are passed on in the form of lower prices, higher quality or new products and services. However, if mergers and acquisitions are not controlled by an effective competition policy they may lead to excessive market concentration and anti-competitive behaviour, so that consumers find themselves paying higher prices or faced with poorer quality goods and services.

Businesses, for their part, need to follow M&A activities in order to respond to new economic conditions and changes in the strategies of their competitors, which often involve mergers and acquisitions. The importance of M&A can be seen from the extremely high ratio of cross-border M&A values to foreign direct investment worldwide (over 85% in 2000). Multinationals in particular need information on where, in what form and why competitors are investing so that they can make effective investment decisions themselves.

Lastly, academics, regulators and policymakers need to understand companies' strategies and their impact on economic performance so that they can design and implement policies which will help increase prosperity and raise living standards over time.

The note aims to meet these needs by covering recent M&A developments and setting M&A in the context of other key economic issues. The first part of each issue will consist of an overview of M&A activity over the last six months (in this first issue, the overview covers the whole of 2003). The second part will look at a specific M&A topic in more depth. This first issue looks at international M&A activity and discusses the impact of globalisation. It analyses to what extent the distribution of M&A has been affected by EU enlargement and the emergence of fast growing markets, such as India and China.

The note will appear twice a year. I wish it every success and trust you will find it informative and interesting. Your comments and suggestions are most welcome.

M&A overview

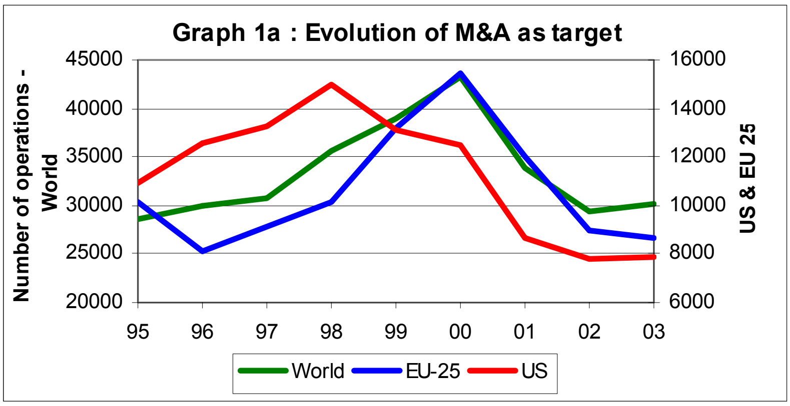
1. Overall M&A activity

Firms decide to merge or acquire other companies for various reasons. Some transactions may be motivated by firms trying to take advantage of free cash flows. Others may be explained by the strategies pursued by multinationals to enter new markets and extend their competitive advantage abroad, to seek strategic assets such as technology and management capabilities, to realise economies of scale and scope by restructuring their businesses on a global basis and, last but not least, to eliminate actual or potential competitors. Merger activity can have substantial and complex effects on the economy and therefore deserves attention. In addition, macroeconomic indicators such as the evolution of overall M&A activity may be useful in assessing business dynamism and confidence and to help forecast economic performance. Finally, an analysis of M&A at the global level can help explain flows of FDI around the world (See Box 1 below for a comparison of cross-border M&A and FDI statistics) and serve as a basis for a better assessment of European and world economic integration.

Slight increase in the number of world M&A in 2003…

…but a slight fall in the EU-25

After the worldwide peak in 2000 and subsequent decreases over the two following years, M&A activity in the world as a whole slightly increased in 2003. Globally the total number of operations reached 30 200 in 2003, against 29 300 in 2002 (an increase of 3%). The total number of operations involving the acquisition of a US company increased by 1% to 7 900 operations, due to an increase in domestic mergers and acquisitions (see Graph 1a). For the EU-25 the situation was different, with a decrease of 3.4% between 2002 (9 000 operations involving EU firms as a target) and 2003 (8 700 operations). The gap between the EU-25 and the USA may be explained in part by the delay in the economic recovery in the EU-15.



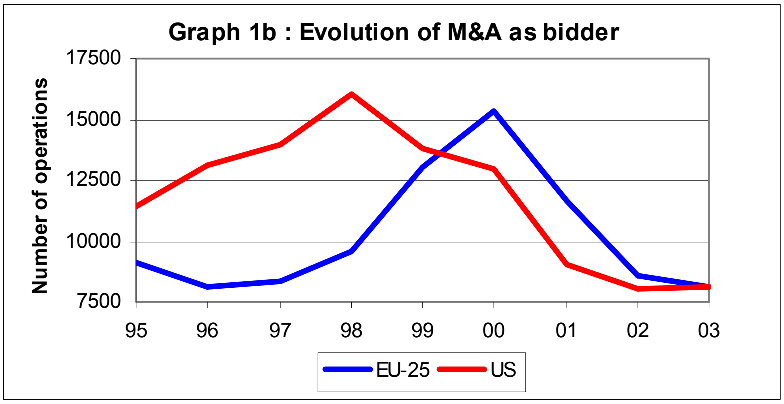
As a source of bidders (i.e. acquiring companies), the USA seem to have shown a slight recovery in the last two years with a higher number of acquisitions than the EU-25 in 2003 (8 153 against 8 100, see Graph 1b).

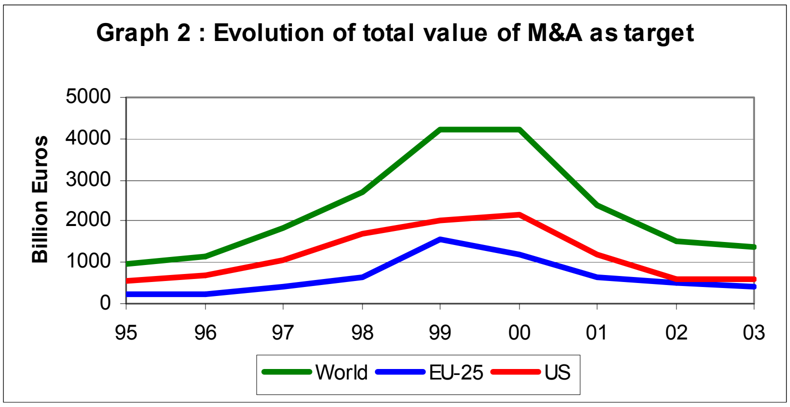
Box 1 : Important differences between M&A and FDI statistics

Broadly speaking, FDI includes M&A statistics, Greenfield investments, reinvested earnings and intra-company loans. However, the following issues should be noted. Firstly, M&As record capital transactions without deducting disinvestment while FDI data deduct disinvestment. Second, cross-border M&A may be financed by external and domestic settlements while FDI are financed by external settlements and reinvested earnings. Third, while M&As record all acquisitions of shareholdings of 5% or more, only acquisitions of holdings of more than 10% of the capital qualify as FDI

Box 2: Notes on the data base and conventions

M&A statistics in this note are based on data provided by Thomson Financial Services (TFS). The database covers all acquisitions of shareholdings of 5% or more and with a value over US$1 million as well as acquisitions for which the value is unknown. Although it endeavours to collect and present information which is as complete as possible, the nature of the information makes the coverage somewhat arbitrary. This is because although major operations affecting publicly listed companies are often officially published, the numerous purchases of smaller or unlisted companies are more difficult to identify. Also, subjective assessments are often inevitable e.g. as regards the date and sectoral classifications of a merger and acquisition operation.
In addition a number of conventions have been established when drafting this M&A note. We take account of both completed and pending deals. We use the TFS classification for the sectoral aspects of M&A (SIC classification, different from NACE classification). Moreover, sectoral activities are defined according to the target's main activity, as this is the activity most likely to interest the bidder and also because the targeted sector is the one in which the effects of an operation are likely to be the greatest. Finally it is important to note that the database does not contain value data for a significant number of deals. However these are mostly small deals since the value of large operations can usually be ascertained. The value data are therefore underestimated, though not by a large amount.





The value of M&A has decreased in the world as a whole, the EU-25 and the USA since 1999-2000. Globally the total value decreased by 8.6% in 2003 to 1 365 billion euros. The decrease was 15.6% in the EU-25 and 4.2% in the USA (see Graph 2). The decline in value of mergers can be attributed in part to weak the economic performance, concerns about international security, a pause in the consolidation of some industries and declining stock prices, but can also be seen as a correction of the exceptional surge in M&A during 1999-2000. [1]

A decline in the value of world M&A since 2000

2. M&A activity in the EU-25 countries

Table 1 shows the relative intensity of M&A activity in each EU-25 country and makes it possible to compare the share of M&A in each Member State with its share of EU GDP. The intensity of M&A activity is defined as the country's share of EU-25 M&A as target and bidder. 70% of M&A activity was accounted for by the four largest economies (Germany, France, UK, and Italy). The share of activity was higher than might be expected from the relative size of the national economies in the UK, Netherlands, Sweden, and Finland. The new Member States represent a low share of M&A activity, although this has doubled between 1990-1993 and 2000-2003. The Czech Republic, Poland, Slovak Republic and Hungary represented almost all of the M&A activity in the new member states. M&A activity in transition countries largely reflects the privatisation process. The progressively decreasing State involvement in those economies should lead to increasing levels of activity.

Table 1: Distribution of M&A activity and GDP between Member States 1990-1993, 2000-2003

	1990-1993		2000-2003	
	Share of M&A (%)	Share of GDP (%)	Share of M&A (%)	Share of GDP (%)
United Kingdom	34.53	13.8	33.39	17.1
France	18.63	17.2	15.04	15.9
Germany	11.13	24.7	14.60	22.2
Italy	8.62	15.3	9.22	13.2
Netherlands	6.58	4.3	6.61	4.6
Sweden	6.30	3.2	6.00	7.2
Spain	5.56	7.3	3.35	2.7
Belgium	2.26	2.9	2.22	2.7
Finland	1.16	1.5	2.05	1.5
Ireland	1.02	0.7	1.59	1.9
Portugal	0.93	1.1	1.17	1.3
Denmark	0.82	1.9	1.02	1.3
Austria	0.75	2.4	0.90	0.2
Luxembourg	0.71	0.2	0.69	2.3
Hungary	0.45	0.4	0.59	1.5
Poland	0.29	0.8	0.51	0.8
Greece	0.27	1.3	0.49	2.1
Czech Republic	0.02	0.4	0.22	0.3
Slovak Republic	0.01	0.2	0.17	0.7
Cyprus	0.00	0.1	0.07	0.2
Estonia	0.00	0.0	0.03	0.1
Malta	0.00	0.0	0.03	0.1
Lithuania	0.00	0.0	0.02	0.1
Latvia	0.00	0.0	0.02	0.1
Slovenia	0.00	0.2	0.01	0.0
Old Member States	99.24	97.85	98.32	96.15
New Member States	0.76	2.15	1.68	3.85

Source: SDC M&A, Ameco

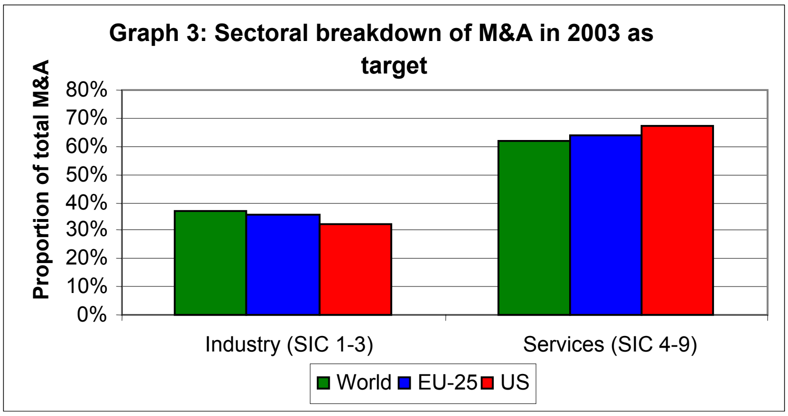
Over seventy percent of M&A activity in the EU-25 is accounted for by the four largest economies

1 UNCTAD, World Investment Report 2003.

Two thirds of M&A as target are services

3. Sectoral comparisons

From a sectoral point of view, the breakdown between industry and services (see Graph 3 on M&A targets) shows the predominance of the service sectors, accounting for roughly two thirds of all M&A operations. Breaking the figures down into more detail, the most targeted sectors worldwide were the manufacturing sector (SIC 2 & 3) directly followed by the 'service industries'[2] (SIC 7 & 8) with respectively 30% and 23% of the total M&A operations. The finance, insurance and real estate sector (SIC 6) was the third most targeted sector (18%), followed by network industries (SIC 4, 11%) and distribution (SIC 5, 9%). At the EU-25 and US level, the situation was slightly different. In the EU-25, the manufacturing sector (SIC 2 & 3) was predominant with 30% of all M&A operations, while in the USA the service industries sector (SIC 7 & 8) was the most targeted with 31.5% of the total number of operations.



The global, US and EU pattern of evolution was similar between 1995 and 2003. M&A operations in the manufacturing, distribution and finance sectors tended to decrease as a proportion of the total while the network industries and the service industries experienced an upward trend (see Table 2).

Table 2: evolution of the sectoral breakdown by aggregates (targeted sectors)

	World			EU-25			USA		
Sector	1995	2000	2003	1995	2000	2003	1995	2000	2003
Agri & forestry	0.9%	0.8%	0.9%	0.9%	0.7%	0.6%	0.5%	0.4%	0.5%
Mineral industries	7.7%	5.3%	7.8%	7.7%	3.1%	3.9%	4.9%	3.4%	5.0%
Manufacturing	32.5%	27.1%	29.5%	32.5%	29.7%	31.5%	27.3%	24.3%	27.0%
Network industries	10.4%	11.3%	11.2%	10.4%	11.1%	12.7%	9.5%	9.8%	10.1%
Distribution	10.9%	9.2%	9.4%	10.9%	10.8%	10.8%	11.2%	9.0%	8.5%
Finance, insurance and real estate	18.5%	14.8%	18.1%	18.5%	13.2%	16.1%	19.8%	14.4%	17.8%
Service industries	19.0%	31.3%	22.9%	19.0%	31.3%	24.2%	26.7%	38.5%	31.1%
Public administration	0.2%	0.2%	0.2%	0.2%	0.1%	0.2%	0.1%	0.2%	0.1%

[2] 'Service industries' include hotels, rooming houses, camps and other lodging places, personal services, business services, automotive repair, services and parking, miscellaneous repair services, motion pictures, amusement and recreational services, legal services, engineering and management services.

4. Cross-border operations

The share of domestic operations relative to cross-border operations has always been high in the EU-25. Within the category of cross-border operations, the share of mergers between EU-25 and the rest of the world is larger than the share of intra-EU-25 M&A (see Table 3 below). It is also worth noting that while the upsurge in M&A reflected the wave of domestic as well as cross-border M&A until 1998, the decline in the EU reflected a sharper decrease in cross-border M&A, and particularly international M&A, than in domestic transactions. While cross-border M&A played a dominant role in increasing flows of foreign direct investment in the 1990s, they have also played a large part in the recent downturn of FDI.[3] This halt may be partly explained as a pause needed to give companies time to integrate the foreign acquisitions of recent years into their corporate strategies. This process may be rendered particularly difficult by the financial burden imposed by the excessive prices paid in certain sectors, for example new economy activities.[4]

Decrease in the share of cross-border operations in the EU since 1998

Table 3: Breakdown of total EU M&A into Domestic, Community and International Operations

	Domestic	Community	International	Bidder unknown	Total
1995	58%	14%	20%	8%	100%
1996	56%	14%	23%	7%	100%
1997	56%	15%	24%	4%	100%
1998	54%	15%	26%	4%	100%
1999	56%	16%	23%	4%	100%
2000	55%	17%	22%	6%	100%
2001	56%	17%	21%	7%	100%
2002	59%	16%	20%	6%	100%
2003	58%	15%	21%	6%	100%

5. Largest M&A operations in 2003

Table 4 shows the five largest M&A operations in 2003. It is interesting to note that two of the top five mergers featured companies involved in the supply of natural gas.

Table 4: Top 5 M&A operations at world level

Date		Name	Nation	Industrial Classification	Amount (million €)
27/10/2003	Target	FleetBoston Financial Corp	United States	National commercial banks	41 803
	Bidder	Bank of America Corp	United States	National commercial banks	
12/03/2003	Target	Telecom Italia SpA	Italy	Telephone communication, except radio	25 190
	Bidder	Ing C Olivetti & Co SpA	Italy	Radiotelephone communication	
10/03/2003	Target	Iberdrola SA	Spain	Electric services	15 339
	Bidder	GasNatural SDG SA	Spain	Natural gas transmission	
27/10/2003	Target	WellPoint Health Networks Inc	United States	Hospital and medical service plans	13 953
	Bidder	Anthem Inc	United States	Hospital and medical service plans	
22/04/2003	Target	Sibirskaya Neftyanaya Co	Russia	Crude petroleum and natural gas	12 401
	Bidder	Yukosneftegaz(Laguna)	Russia	Crude petroleum and natural gas	

3 See footnote 1 above.

4 OECD, *Trends and recent developments in foreign direct investment 2004.*

International M&A activity: impact of globalisation

By Gaëlle Garnier

1. Introduction

How attractive are firms in the EU-15 compared to other parts of the world, in particular Asia and other parts of Europe? What is the impact of EU enlargement and globalisation on world firms' investment in the new Member States? Do EU firms invest sufficiently in the fast-growing markets of Asia? This article attempts to suggest some answers to these questions in the light of the analysis of the evolution of cross-border M&A in the main regions of the world over the 1990s.

The first part describes the main targeted regions in the world, paying special attention to the EU-15, and compares their performances at the beginning of the 1990s with the current situation. The second part examines foreign companies' investment in the new Member States and in the Rest of Europe (defined as all of Europe, including the new Member States, Russia and Turkey, except the EU-15) over the same periods of time. The third part analyses the position of Asia as a target and the economic implications of EU firms' investment decisions in this region.

2. Main targeted regions in the world

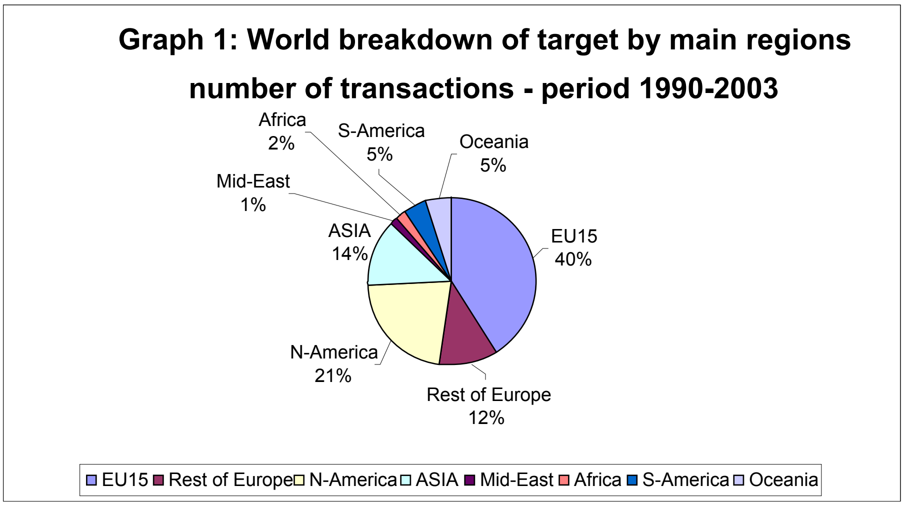
The last decade has been characterised by a very rapidly increasing number of cross-border M&A

The beginning of the 1990s opened a new wave of industrial restructuring, characterised by a very rapidly increasing number of cross-border M&A operations[5]. The worldwide annual number of cross-border M&A tripled between 1990 and 2000. Cross-border M&A progressively replaced greenfield investments as the dominant component in FDI. In 2000 the ratio of M&A values to FDI reached more than 85%, although M&A have declined relative to entry through greenfield investments since then[6]. The ratio of M&A to total FDI in developing countries also increased from zero in the late 1980s to half of the total in the late 1990s[7]. Most M&A activity is concentrated in a limited group of mainly developed countries. Just as the EU-15 and North America have always been the main bidders, they have also attracted the bulk of inward M&A. From 1990 to 2003, they together represented 61% of the total number of M&A operations as targets with the EU-15 accounting for 40% (see Graph 1).

[5] Bertrand O., Muchielli J.L., Zitouna H., 2003, Location choices of Multinational Firms: the case of M&A, University of Paris I, *Mimeo*.

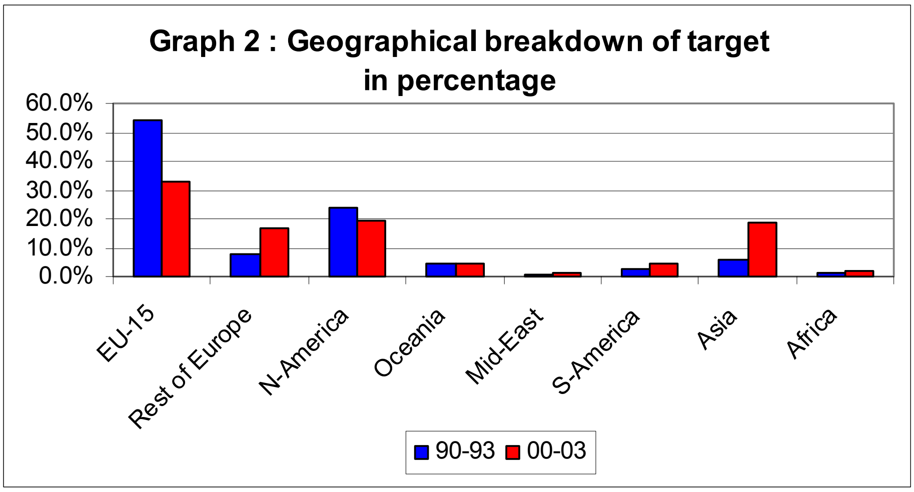
[6] See footnote 1.

[7] Calderon C., Loayza N., Serven L., 2004, Greenfield Foreign Direct Investment and Mergers and acquisitions: Feedback and macroeconomic effects, *WPS3192*.



While the EU-15 and North America continue to be involved in the bulk of cross-border M&A, their importance as targets is diminishing

However, interest in EU-15 and North American companies as targets (measured as a share of the total number of companies purchased in the world) weakened at the beginning of the 2000s relative to the early 1990s – to the benefit of all the other main regions of the world. The EU-15 share decreased from 54% in 1990-1993 to 35% in 2000-2003 (see Graph 2).



Although weak economic conditions and declining stock prices may partially explain the recent reduction of M&A inflows into the EU-15, a more important explanation is the increased international competition which has pushed firms to become more competitive and to seek a more efficient allocation of productive assets.

The new Member States and Asia seem to be more attractive places to invest due to their potential market growth, cost advantages and FDI-friendly attitudes

Firms undertook M&A in order to enter new markets, to extend competitive advantage abroad, and to realise economies of scale and scope by restructuring their businesses on a global basis. They shifted their pattern of investment to Asia and the Rest of Europe, where cost advantages and new market opportunities were greater. Asia and the Rest of Europe became respectively the world's third and fourth largest destinations for M&A in 2000-2003 (see Graph 2). The Rest of Europe share doubled from 8% in 1990-93 to nearly 17% in 2000-03. Access to new markets, above-trend growth prospects, cheap skilled labour and to some extent low corporate taxes particularly in the acceding countries, boosted the stock of investment[8]. The Asian share increased from 6% to 19% over the same period to nearly equal the North American share of total operations (see Graph 2). M&A as a mode of entry have played an important role in increasing FDI inflows in Asia, especially after the economic crisis which led to the relaxation of restrictions on equity participation and to the huge decline in the values of East Asian currencies and assets (M. Kawai, 2004). Other factors that contributed to the region's increasing attractiveness were labour skill advantages and access to growing markets.

[8] Hamilton D.S. and Quinlan J.P., 2004., *Partners in Property: the Changing Geography of the Transatlantic Economy*, CTR.

Finally, this geographical shift of M&A activity can also partly be explained by a worldwide FDI-friendly attitude as countries came to recognise that cross-border M&A can play a useful role in promoting reform and modernisation of local corporate governance and production capabilities, creating employment and boosting industrial sectors in difficulty. In Asia and the Rest of the World, privatisation processes were partly driven by such considerations. Asia was also one of the most rapidly liberalising host regions for FDI, making more national policy changes in a direction favourable to foreign investors in 2002 than any other region[9]. The introductions of economic reforms as a result of the EU enlargement preparation since the beginning of the 1990s have also helped to attract foreign investors in the new Member States.

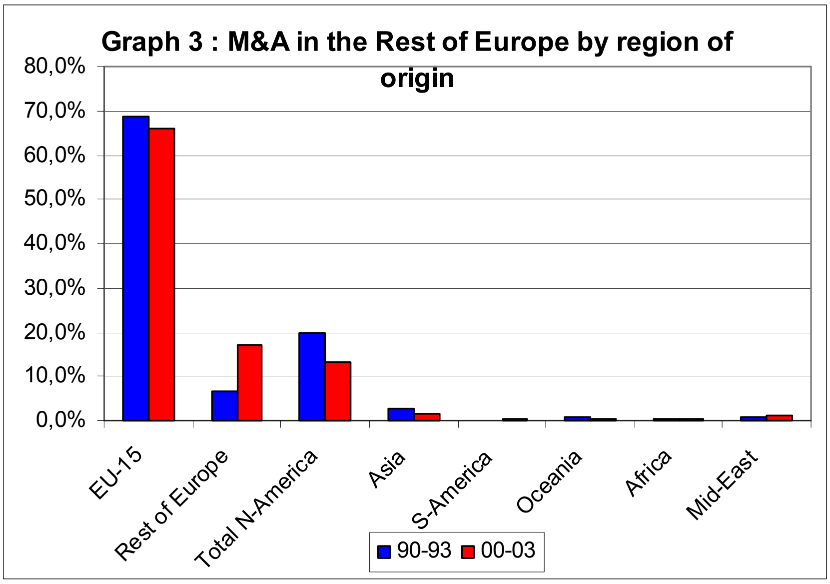
The decreasing share of EU-15 firms as target is mainly due to decisions of EU-15 multinationals which have been attracted by new markets in the rest of Europe and Asia

Although companies from all the main world regions have decreased their cross-border M&A investment in the EU15 relative to their investment in the Rest of the World, EU-15 multinationals were mainly responsible for the decreasing share. Intra-regional investments in the EU-15 decreased by 12 percentage points between 1990-93 and 2000-03 as EU15 firms increasingly invested in the Rest of Europe and to a lesser extent in Asia (see Graph 4). As globalisation has led EU-15 firms to shift their investment to where cost advantages and potential market growth are greater, it should increase their economic efficiency and competitiveness.

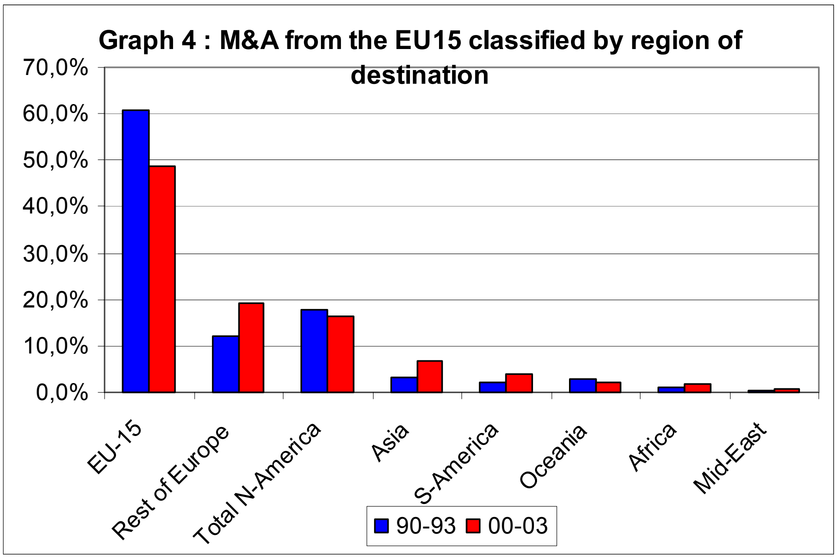
3. Companies' investment in the new Member States and the Rest of Europe

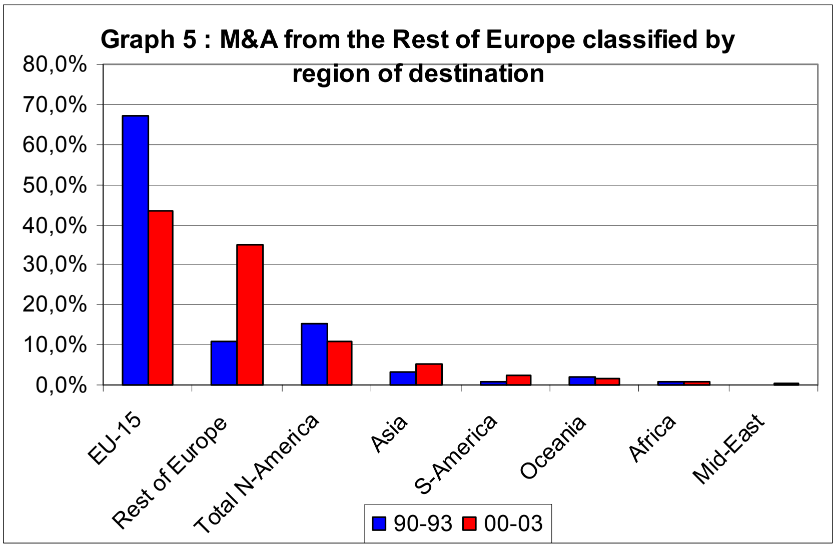
Enlargement has resulted in increasing numbers of acquisitions by the EU-15 in the new Member States as well as cross-border mergers between new Member States

The increasing importance of the Rest of Europe as a target for M&A reflected the ongoing integration of central and eastern countries with the EU. The increased world share of the Rest of Europe is mainly due to the rising number of acquisitions originating from the EU-15 and the Rest of Europe. They accounted for 83% of the total number of operations in 2000-2003 (see Graph 3). The shares of cross-border M&A originating from the EU-15 and the Rest of Europe increased respectively from 12% and 11% in 1990-1993 to 19% and 35% in 2000-2003 (see Graphs 4 and 5).



[9]See footnote 1.

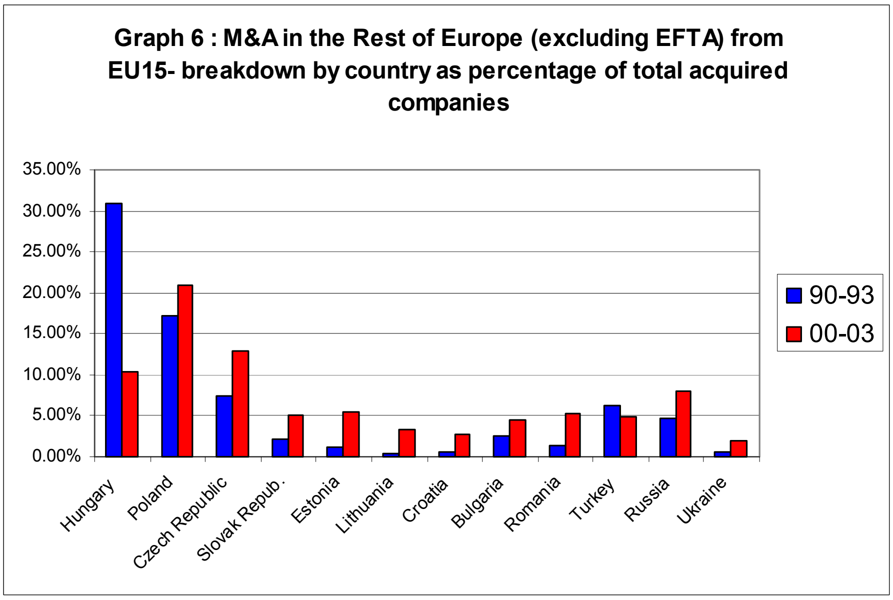




Trade and investment links between the EU-15 and the accession states have been expanding since the beginning of the 1990s, when multinationals started to prepare for enlargement. As they were the first economic reformers to undertake major privatisations, Poland, Hungary and, to a lesser extent, the Czech Republic led the other central European countries in integrating their economies with the EU. While these three have always accounted for the bulk of investment in the new Member States, others, particularly Estonia, the Slovak Republic, and Lithuania, have recently been increasingly targeted by the EU-15 (see Graph 6). In the last few years, the number of cross-border mergers between new Member States has also contributed to the integration of those countries with the EU. In 2000-2003, 46% of cross-border M&A within the Rest of Europe excluding EFTA was between new Member States.

But enlargement has also shifted M&A investment increasingly towards countries bordering the new Member States

Although M&A targeting the new Member States account for the bulk of cross-border M&A investment in the Rest of Europe excluding EFTA, their share has recently decreased. The share of EU-15 investment in the new Member States decreased from 78% in 90-93 to 64 % in 2000-2003. With the progressive integration of the new Member States into the EU through the process of enlargement, the countries bordering them, such as Bulgaria, Croatia, Romania, and Russia, have increasingly been targeted by companies from the EU-15 and the Rest of Europe (see Graph 6). Our assumption is that multinationals have shifted their labour-intensive activities to these lower income nations with cheaper labour while at the same time boosting their efficiency-seeking investment in the most developed Central and Eastern European countries such as Hungary, the Czech Republic, Slovakia, Slovenia and Estonia[10]. As a result of increasing competition from countries such as China, firms in the recently acceded Member States have tended to shed activities based on unskilled labour and to expand higher value-added activities, taking advantage of their educated labour force.[11]



The ongoing process of European integration should continue to create business opportunities contributing to increased growth in the EU

The economies of the countries in the Rest of Europe are growing fast and their integration into the EU should therefore continue to create business opportunities. In addition, if new Member States progressively upgrade their activities towards higher value-added products and services as we expect, this may stimulate competition in the enlarged EU. Furthermore, new Member States could benefit from externalities such as technology transfer and knowledge spill-overs. These developments, in which M&A plays a major role, are positive for growth in the EU.

However, the capacity of new Member States to remain attractive in the future will depend, in particular, on their ability to continue to implement structural reforms conducive to the development of comparative advantages in higher value-added activities. Poland and the Czech Republic come out in the top two places for future direct investment from 2004 to 2007 in the Rest of Europe according to UNCTAD's survey of international location experts. However, they are fifth in the world ranking. Finally, even though they will retain their cost advantage in the near future, they will probably fall further behind China and India in the medium term in terms of FDI since they started from a relatively higher cost level and generally experience substantially higher annual cost increases.[12]

[10] See footnote 8.
[11] Boston Consulting Group, 2004, Capturing Global Advantage: How Leading Industrial Companies are Transforming their Industries by Sourcing and Selling in China, India and Other Low-Cost Countries. See also footnote 3.
[12] See footnote 11.

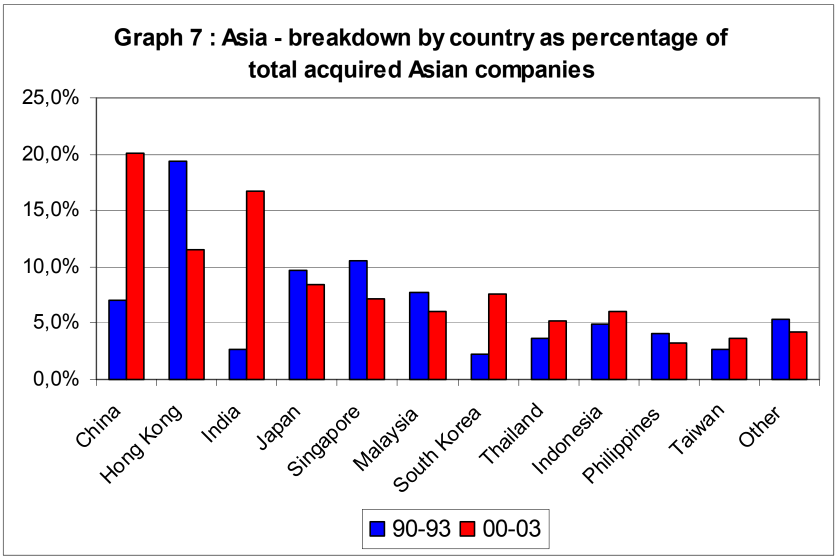
4. Companies' investment in Asia

The favourite M&A destination countries in Asia were China and India, which represented respectively 20% and 17% of the total number of cross-border operations in Asia in 2000-03 (see Graph 7). In 2003 China became the world's foremost recipient of FDI[13]. China's entry into the World Trade Organisation helped to spur investment. Foreign investors were initially attracted to both China and India because of improved economic performance, increasingly competitive information technology industries, cheap land and labour, the promise of a large market, the impetus of recent liberalisation and, to some extent, fiscal incentives[14]. While China already represents a major and very fast-growing source of industrial products, India is specialised in outsourced services.

Since adopting more open economic policies, China and India have become the main target countries of M&A in Asia

China is a large market. For example, it is the largest market in the world for machine tools, the second largest market for transmission and distribution equipment and the fourth largest market for automobiles (including passenger cars and trucks)[15]. As domestic suppliers are unable to meet domestic demand, western companies see the opportunity to fill those gaps by acquiring and expanding Chinese companies.

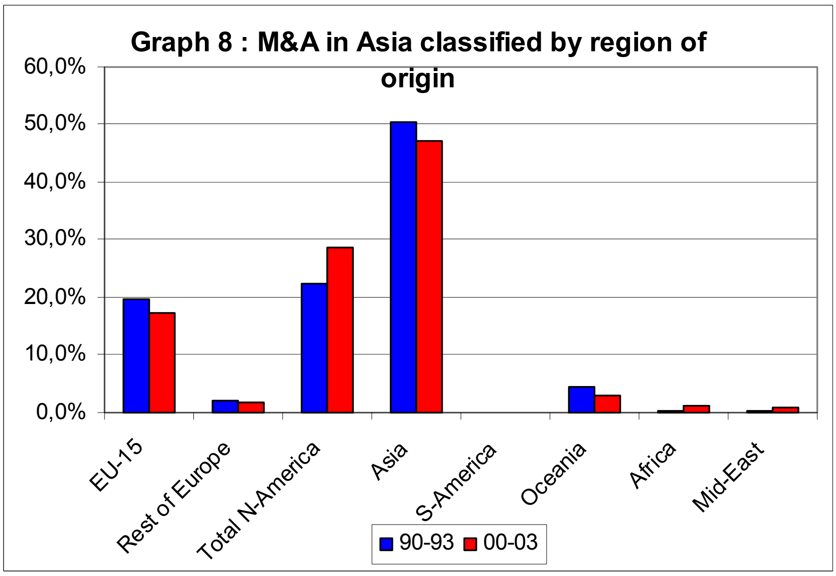
India is specialised in Information Technology (IT) and offshore Business Process Outsourcing (BPO) services. One of its major advantages is the availability of large numbers of highly educated English-speaking workers and managers, together with a strong telecommunications infrastructure. From 1999 to 2002, India's service-outsourcing revenue grew more than 70% annually[16].



North America and Asia itself were the main contributors to Asia's increased world share as target (see Graph 8). North American firms have refocused their interest towards M&A in Asia, shifting away from the EU. The share of acquisitions in Asia in the total number of cross-border acquisitions made by North American firms tripled from 6% in 1990-93 to 18% in 2000-03.

While the EU increasingly invested in countries bordering the new Member States North America invested more in Asia

[13] OECD, 2004, Trends and recent developments in Foreign Direct Investment.
[14] OECD, 2003b, International Investment Perspectives. See also footnote 3.
[15] See footnote 8.
[16] See footnote 8.



Conversely, while the EU-15 was by far the largest bidder in the world in 2000-03, its share of inward M&A in Asia was relatively low, indeed 3% lower than it was in 1990-93 (see Graph 8). While EU-15 firms increasingly invested in countries bordering the new Member States such as Russia, North American firms invested more in Asian countries such as China. The slow development of investment by EU firms in Asia is not new but the gap is increasing despite efforts to encourage European firms to invest more in Asia[17].

Increasing the EU's presence in rapidly growing countries such as China and India would be beneficial to the Union's growth prospects

Increasing the EU's presence in these rapidly growing countries would probably be beneficial to the Union's growth prospects. First, surveys of international investment location, which assess future developments in FDI, rank China and India in the first place in the world for investment over the next few years.[18] They already represent the world's largest growing markets. In addition, they are the largest producers for many industrial goods, maintaining a very low cost base leading to high-margin production.

Second, experts and businesses believe that there is a first-mover advantage to be gained by securing sources of supply, building relationships, developing organisational capabilities and learning by doing.[19] Pioneering access to markets may also be an advantage. Third, while non-acceding countries in the Rest of Europe, such as Russia, have the potential to attract investment thanks to their natural resources, human capital and potential market growth, their less favourable business environment and higher relative political and economic instability may render the investment riskier than in Asia.

[17] Report by the European Commission and UNCTAD, 1996, *Investing in Asia's dynamism: European Union direct investment in Asia.*

[18] AT Kearney, 2004, Established Players and New Locations Compete for Offshore Jobs, Increasing Complexity for Companies. See also footnote 6 and 11.

[19] See footnote 18.

4. Conclusion

Globalisation has led to a more widespread geographical distribution of cross-border M&A activity throughout the world. The EU-15 and the US seem to have become less attractive places to engage in M&A activities. In particular, while EU-15 companies still account for 35% of the total number of companies purchased in the world over the period 2000-2003, their importance as target is diminishing. However, this should not necessarily be considered as a negative development as it is mainly the result of EU-15 firms' investment in rapidly growing markets with lower costs of production such as Asia and the Rest of Europe, which reflects their strategy of becoming more efficient and competitive.

The enlargement process has progressively integrated the new Member States into the EU. This has resulted in a rise in the number of acquisitions by EU-15 firms in the new Member States as well as intra-regional mergers between new Member States. This may stimulate competition in the EU if it is the result of an increasing specialisation of the new Member States in higher value-added activities, as we postulate. However, the capacity of new Member States to remain attractive in the future will depend on their ability to implement structural reforms conducive to the further development of comparative advantage, since competition from Asia is likely to intensify.

The prospects for economic growth in the EU will also depend on the future investment strategies of EU firms in Asia. While North American firms have increasingly invested in the world's largest growing markets, the EU share of such acquisitions has fallen as EU firms have invested more in countries bordering the new Member States such as Russia. If this trend persists, as recent data suggest, it may contribute to increasing the growth gap between the USA and the EU.