

NOW, MORE THAN EVER, COMPANIES ARE seeking and making acquisitions abroad. As multinational companies expand around the world, the firms that do business with them may be required to think globally as well. Foreign markets can provide growth opportunities for companies that have dominant domestic markets and minimal growth prospects at home. Access to lower cost of production can be a critical competitive advantage to be obtained through acquisition of a foreign operation. Emerging economies are building economic wealth and spawning consumer markets which generate significant opportunities for expansion-minded companies.

While the benefits of making foreign investment through merger and acquisition transactions can be siz-

able, there are risks to doing business in locations that are unfamiliar to the investor. Cultural mores, commercial practices, government rules and regulations can all interfere and frustrate the acquisition approach of foreign buyers. It is best to understand some of the pitfalls that might be expected in a cross-border transaction and to always involve local professionals to advise on the project.

Our IMAP partner firms have seen a significant growth in cross-border transactions during the last several years. Just within the IMAP membership cross-border acquisitions increased from 24 in 2002 to 49 in 2003 to 65 in 2004. This is a 171% increase in just over two years. We expect the trend to continue.

Acquisitions of foreign operations is generally a more economical method to conduct Foreign Direct Investment (FDI) than the other alternative; a greenfield start-up. A greenfield investment can occupy substantial time and financial resources to accomplish the same market penetration objectives. A firm can spend money on executive trips to visit sites, local advisors to help get the investor acquainted with the commercial landscape, setting up offices, hiring people, procuring production and establishing a distribution network. Your competitors have time to adjust to your arrival and the greenfield is likely to incur start-up losses and mistakes during the early years.

Acquiring a company in the desired foreign location can overcome many of these issues and provide the buyer immediate market position. When factors supporting M&A activity are all in alignment (as they have been during the last several years), cross-border acquisition can generally provide superior results much faster than a greenfield investment. Some of the factors that need to be considered in cross-border acquisitions include the following:

1. Available funding to support acquisition activity.
2. Available targets with reasonable valuation expectations.
3. Ability to meet unfilled needs present within the buying entity.
4. Confidence in the near term economic outlook.
5. Political stability and supportive government rules and regulations.
6. Ability to integrate the acquisition after closing.

## Elements of A Successful Cross-Border Acquisition

*By Oddbjorn Skredderberget and Mark Esbeck*



## Funding Availability

A major factor to be able to even consider a cross-border acquisition is to have the ability to finance the purchase. During the last several years, buyers have been able to access low cost debt funding from banks and other financial institutions in all parts of the developed world. Low cost senior debt funding allows the buyer to pay a multiple or so higher than a firm might be able to pay in a more restrictive credit environment.

Equity has also been quite abundant globally over the last several years and many equity providers have become quite aggressive in meeting the competitive pressures to become involved in transactions. The combination of inexpensive senior debt and abundant sources of equity has propelled the M&A market both domestically and abroad in 2004 and into 2005.

A caveat to consider: As interest rates have now started to rise and past acquisitions are needing to demonstrate performance, it is likely that there will be greater credit issues associated with the accommodative credit markets of late. Rising debt costs can impact the ability of a leveraged acquisition to perform while having the overall affect of slowing down the general economy. Reduced growth opportunities and increased debt service could be a recipe for credit deterioration in late 2005 and early 2006. If so, this could slow down the availability of funding for both domestic and international acquisitions. The present time could be opportune to move forward on an international acquisition, if all of the elements to make the transaction successful are involved. Buyers should attempt to fix or limit interest costs, be prepared for possible slowing economies and have liquidity in place to support their purchase through any possible slowdowns that might occur post-acquisition.

## Identifying Acquisition Targets

If funding is readily available, locating suitable acquisition targets is equally important. Generally acquisition searches will not be limited to one country, but be more regional in nature. Information is the critical factor in being able to locate acquisition targets. Generally, it is relatively easy to locate possible targets. However, since you are generally dealing with privately-owned sellers, it may be a little more difficult to evaluate their attractiveness.

Information availability varies substantially from country to country. Some countries (like Norway or Sweden) have a much more transparent information system than others (like German or Italy). When turnover and profitability information is part of the public domain it contributes to the buyer's ability to refine the acquisition search. When this information is not available, local knowledge is even more important. Even when the buyer is able to obtain sufficient information to narrow the search, information on the seller's willingness to sell,

their pricing expectations, their willingness to consider a foreign buyer and other important seller considerations may only be adequately managed with the involvement of a local advisor.

The majority of sellers interested in negotiating sales to a foreign buyer are likely family-owned and inexperienced in dealing with merger and acquisition issues (not to mention issues associated with foreign parties). We have found that obtaining local advisory for the buyer (or at least the seller) is often times conducive to moving the discussions forward and improving the parties understanding of each other's issues.

Cultural understanding can play a significant role in the cross-border acquisition project. Some countries have not only language(s) differences, but also regional biases that affect commercial activity. Having an awareness of history and cultural perspective can be critical to the start of a cross-border project and important throughout to its conclusion.

## Obtaining the Right Fit

Sorting through acquisition candidates is most efficient when a detailed acquisition profile has been developed to which the targets can be compared. If a primary driver is to access low cost production, does the target company provide this in a fashion that is consistent with other criteria of the buyer (quality control, delivery dependability, etc.)? The buyer needs to make a determination of the risks associated with the ability for it to realize the acquired attributes into the future.

The seller's labor stability, access to raw materials, competitive market pressures, strength and continuity of management, technological competence and other such factors need to be carefully evaluated by the buyer both in present terms and into the future. It is important in all acquisitions that a company understands what it is buying and assures itself that it is getting what it pays for. This requires knowledge of local rules and regulations involving employment, property ownership, social costs, capitalization, management responsibilities and other issues that might be particular to the country where the seller is located.

Equally important is an objective assessment by the purchaser of its own capacity, skill and capabilities to make the cross-border acquisition successful. Does the buyer possess the management depth, financial resources and social skills necessary to manage this type of project? If the assessment is that it doesn't, then the company should address these areas before starting the project.

## Economic Timing

It is important that an acquirer have confidence in the outlook for the economy that it will face after the acquisition. Whether the outlook is optimistic or cautionary is not as important as the fact that the buyer has a solid understand-

ing of the economic environment it which it will be operating. This understanding should form the basis of the purchase negotiations and drive the structure of the transaction.

A buyer can justify a higher price for a company that it can acquire with inexpensive financing in an expansionary economy. However, it may not be prudent for a buyer to pay the same price when its borrowing costs could rise while the business economy is in a downturn. In this case, the transaction will need to be structured to offer the buyer protection against these possibilities.

### Political Stability and Government Regulations

Some of the greatest cross-border opportunities can exist within emerging economies with developing political structures. It is important to for the buyer to understand the political realities associated with making acquisitions in foreign markets. Attitudes toward business and foreign ownership of both the current and prospective political leaders should be carefully evaluated before an acquisition is considered.

The degree of democratic freedom is often not as important as the degree of consistency and stability that is provided to the business community and foreign investors. Provided that business can be conducted fairly between competing organizations and the buyer is able to maintain integrity with its own set of business ethics it may not be important (in all cases) that the ruling parties are of the same political persuasion as the foreign buyer. Real problems can develop when insiders and domestic operators are treated differently than foreign owners.

Countries with trade agreements, tax treaties and investment incentives offer more attractive venues for FDI than those that have more restrictive and less encouraging policies. Legal protections available to both the buyer and seller during the negotiations and after the closing are important for the buyer to understand, as are the buyer's legal responsibilities to all parties affected by the transaction.

### Acquisition Integration

Finally, after all of the careful work leading up to and resulting in the conclusion of a cross-border transaction has been completed, it is important to have a plan to quickly implement any type of organizational changes the buyer wishes to implement with the acquired company. Speed is more critical than perfection in this activity. The management and employees of the acquired company will expect changes due to the sale. However, if changes aren't made quickly and confidently, routines will become reinforced and new ownership may face increased opposition to its ideas at a later

date. It is far better to encounter the immediate pain associated with changing over reporting responsibilities, changes in purchasing authorities, reductions in head

**Buyers should limit interest costs, be prepared for possible slowing economies and have liquidity to support their purchase through any possible slowdowns that might occur post-acquisition.**

counts and divisional realignments than to live with the long term agony of postponing such decisions. The post-acquisition integration plan should be finalized before the transaction closes and the implementation strategy launched immediately upon takeover.

### Summary

In reality, the elements necessary to ensure success in a cross-border transaction are not much different than those required for success in a domestic acquisition. Differences arise due to the variety of scenarios that may come into play in cross-border acquisitions associated with language, culture, disclosure, legal protection and seller expectations. Knowledgeable buyers will carefully evaluate all of these issues before finalizing their cross-border purchase. It is important that companies have professional advisors before initiating a cross-border purchase. Unlike on some domestic acquisitions, our clients prefer that both sides have advisors on cross-border transactions. This ensures that the commercial focus of the project does not get lost in the myriad of issues associated with buying a company in a foreign jurisdiction.

---

*Oddbjorn Skredderberget is currently chairman of IMAP and president of Nordic Merger A.S. in Oslo, Norway. Nordic Merger is a leading Norwegian corporate finance and M&A advisory firm focusing on cross-border transactions. Skredderberget can be reached at [oddbjorn@nordicmerger.no](mailto:oddbjorn@nordicmerger.no).*

*Mark Esbeck is currently president of IMAP and chairman of Business Capital Corporation in Des Moines, Iowa. Business Capital provides investment banking services of valuation, corporate finance and M&A advisory to the middle market. Esbeck can be reached at [mark@businesscapitalcorp.com](mailto:mark@businesscapitalcorp.com).*