

The Hidden Costs of Being Public Evidence from Multinational Firms operating in Emerging Markets

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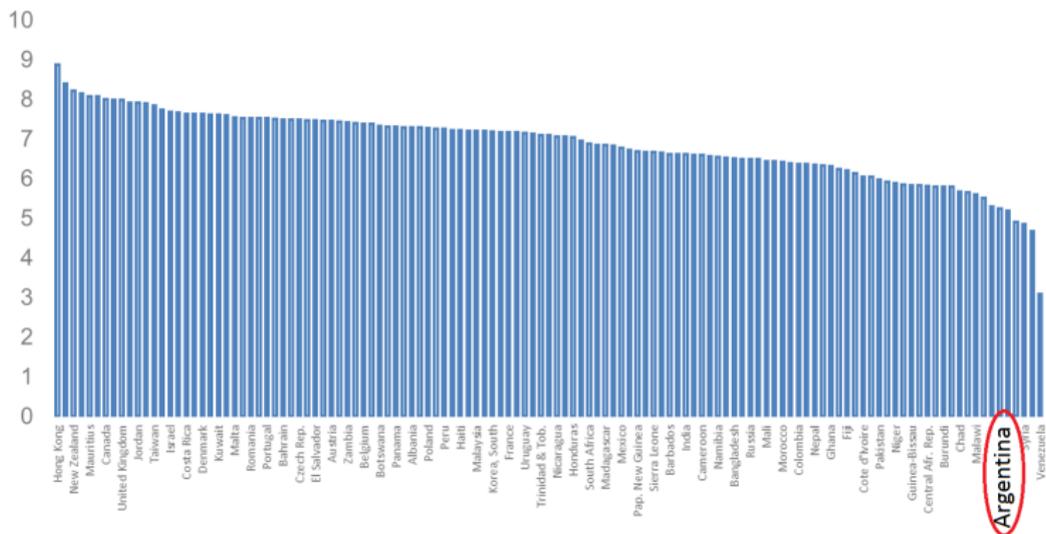
AFA Annual Meeting - January 2019

Business in Emerging Markets - Relevance

- 1 EM account for more than 50% of global GDP (IMF, 2014)
- 2 EM account for over 70% of global GDP growth (IMF, 2016)

Business in Emerging Markets - Issues

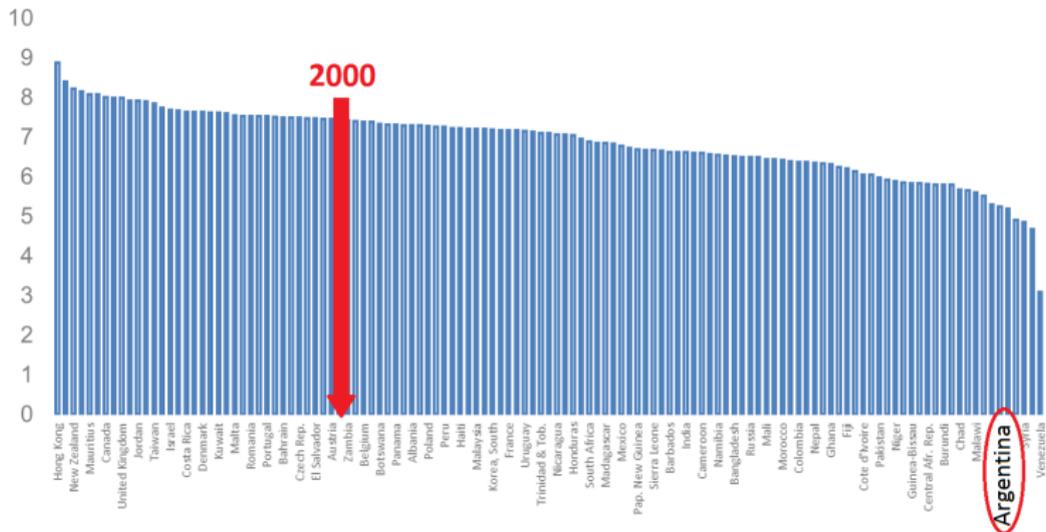
Doing Business in Emerging Markets



Economic Freedom of The World Index (2015)

Business in Emerging Markets - Issues

Doing Business in Emerging Markets



Economic Freedom of The World Index (2015)

Question 1

- 1 What do firms do in response to regulations that limit their operations?

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- 1 What do firms do in response to regulations that limit their operations?
 - Construct a new measure of compliance with a ban on profits repatriation
 - Use a novel and confidential database to show that my measure provides strong evidence that some firms bypass the ban
 - Show that listing status affects decision to comply with the ban

Private firms bypass ban and repatriate up to 46% of their profits, while listed firms mostly comply with the ban

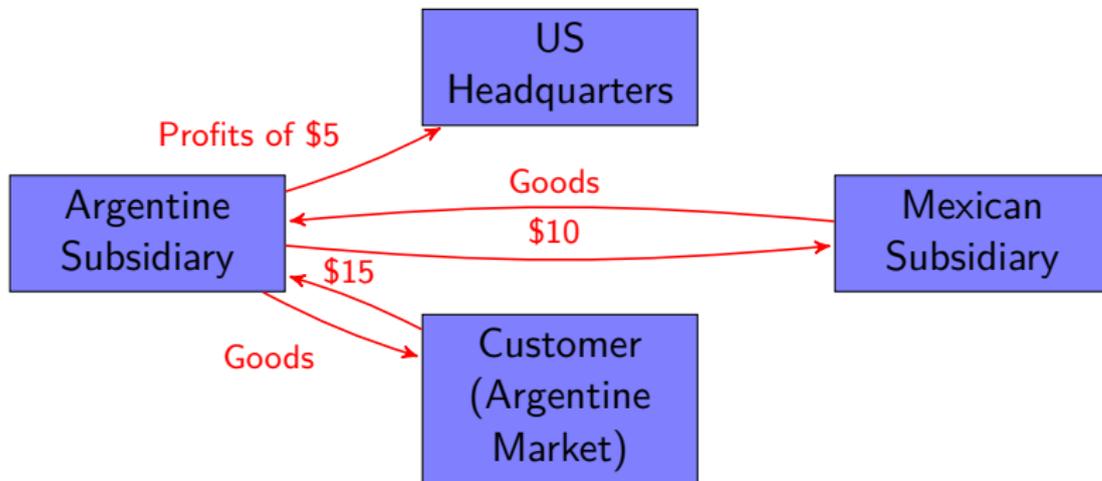
Question II

- 2 Does the ability to bypass regulations create corporate value?

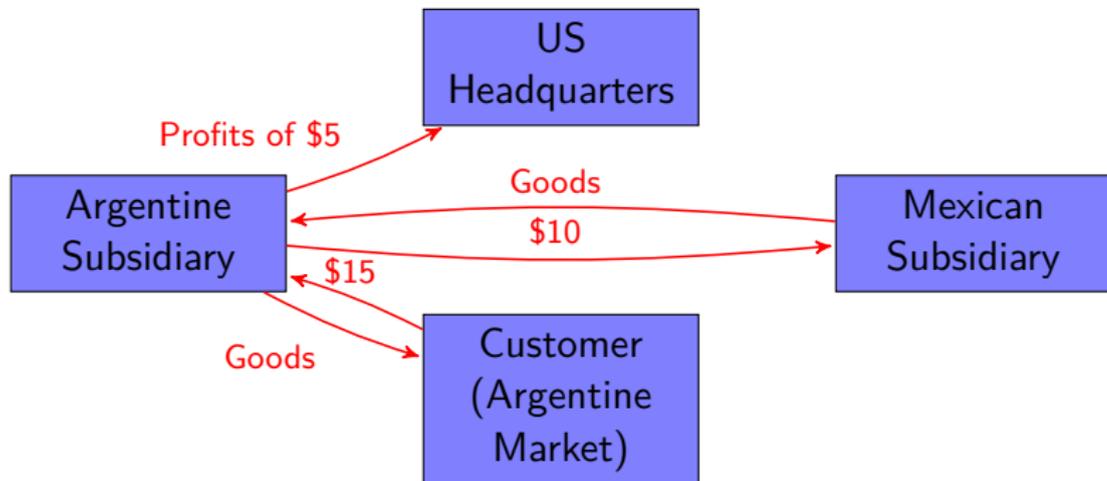
Question II

- 2 Does the ability to bypass regulations create corporate value?
- Show that after ban, M&A patterns consistent with value creation
 - Provide suggestive evidence that the results can be extended to other emerging markets and regulatory changes
- Less friendly: % tx private firms acquire listed firms **increases** by 22.8 pp
- More friendly: % tx private firms acquire listed firms **decreases** by 12 pp

The Setting - Before Regulation

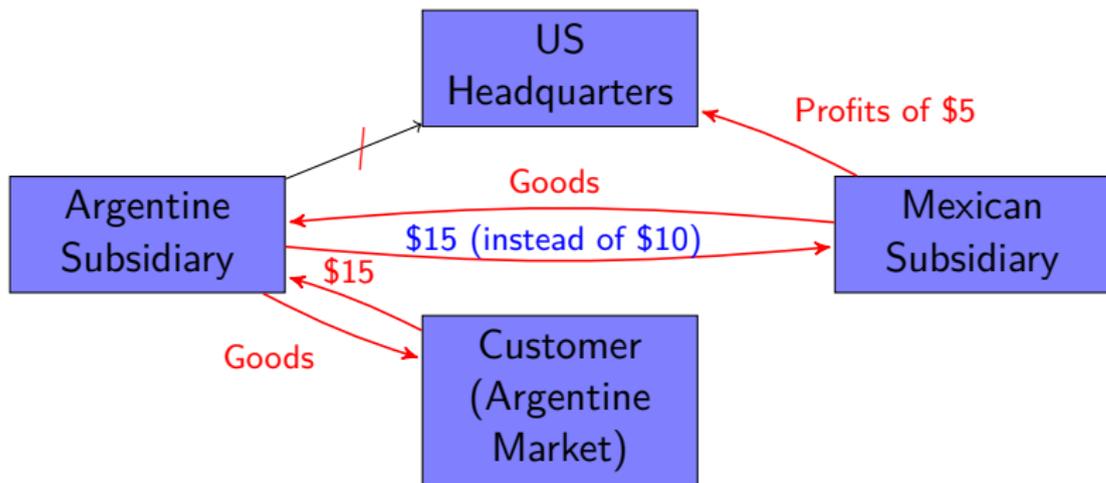


The Setting - Before Regulation

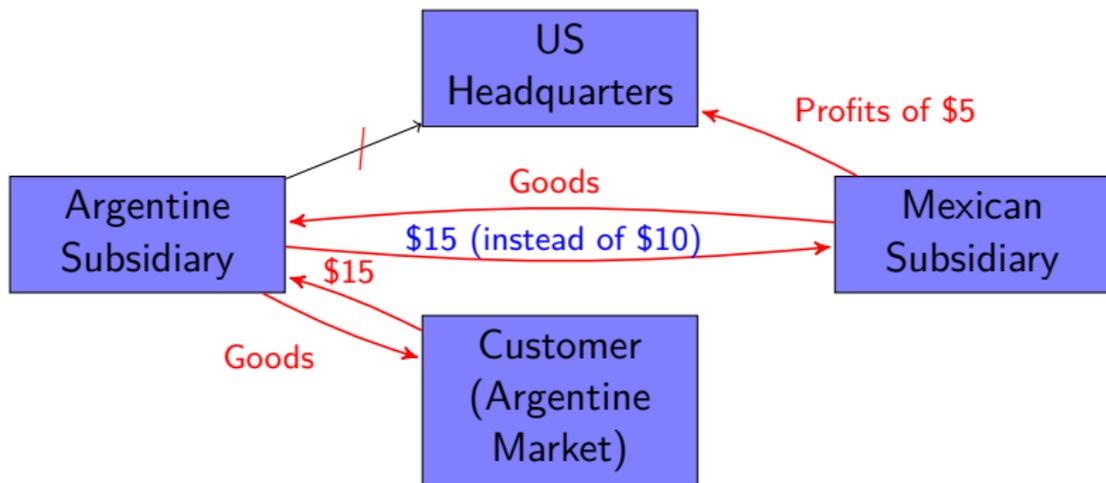


In February 2012, the government banned firms from transferring profits abroad

The Setting - After Regulation

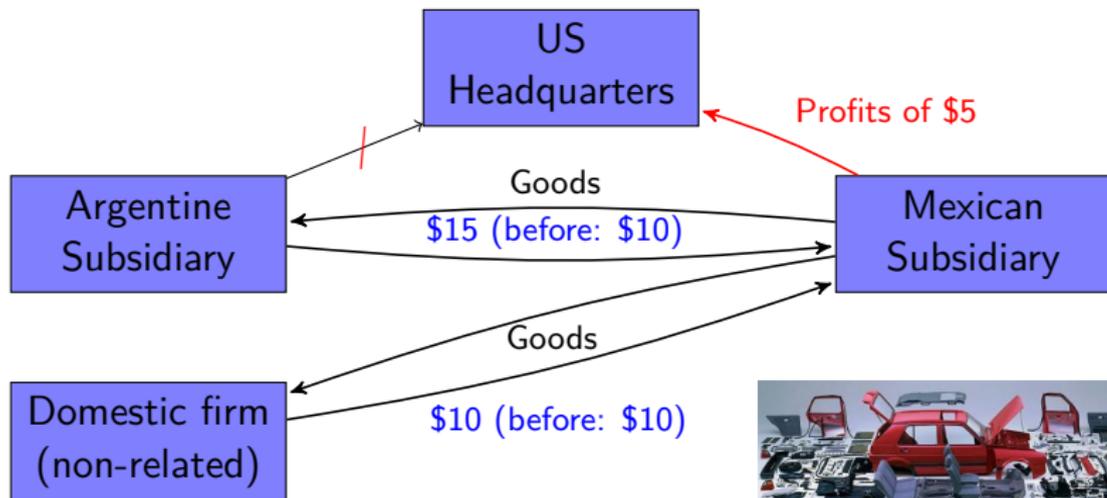


The Setting - After Regulation



What if the price has gone up for other reasons?

The Setting - Counterfactual



Same product number ✓
Same manufacturer ✓
Same country ✓

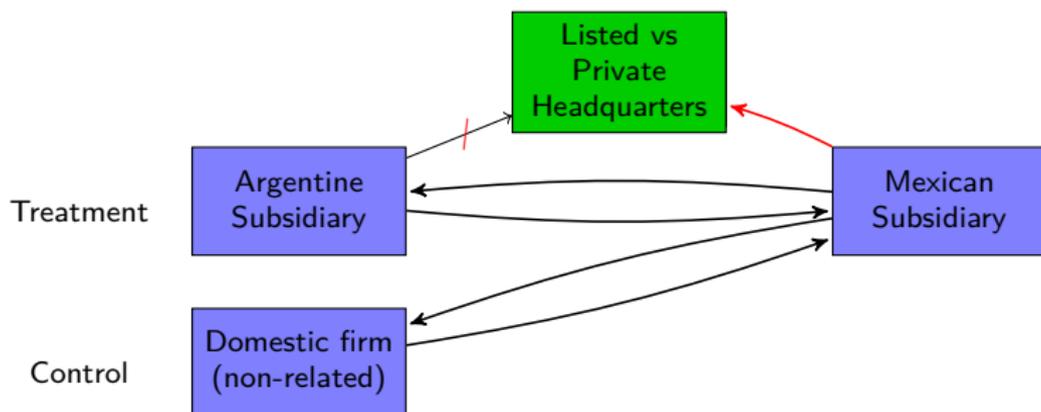


Empirical Specification

Difference in differences:

$$P_{ijkt} = \alpha_i + \alpha_m + \beta_p \times Post_t + \beta_r \times Related_{jk} + \beta_{pr} \times Post_t \times Related_{jk} + \epsilon_{ijkt} \quad (1)$$

Where i : Good, j : Importer, k : Exporter, m : Month, and t : Time



Results - Overpricing of Imports

Price	(1) Private firms	(2)	(3) Listed firms	(4)	(5) Difference (1) - (3)
Post	0.00376 (0.020)	0.00172 (0.020)	0.00861 (0.017)	0.00810 (0.017)	-0.00485
Related	-0.0530*** (0.018)	-0.0548*** (0.017)	-0.0889** (0.039)	-0.0892** (0.039)	0.0359
Post × Related	0.0996*** (0.031)	0.0990*** (0.031)	0.0134 (0.017)	0.0133 (0.018)	0.0862***
Product FE	Yes	Yes	Yes	Yes	
Month FE	No	Yes	No	Yes	
N	430,846	430,846	787,591	787,591	

Standard errors in parentheses, clustered at the importer-exporter pair level

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

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Increase in transfer prices allows firms to repatriate up to 46% of their profits

Results - Overpricing of Imports



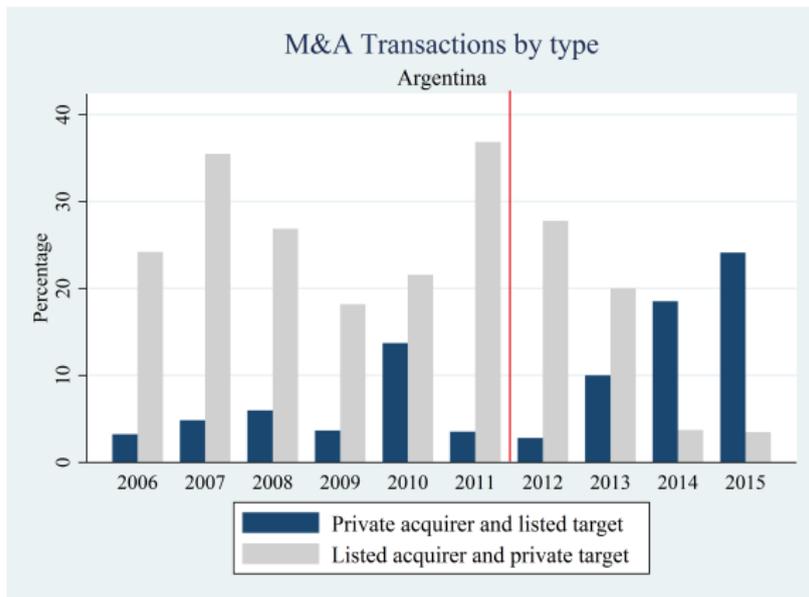
What about...?

- 1 Size
- 2 Concentrated Ownership
- 3 Visibility
- 4 Tax Minimization
- 5 Volumes
- 6 Others...

Roadmap

- Natural experiment in Argentina
- M&A in Argentina
- M&A in emerging markets

Patterns in M&A Transactions



Patterns in M&A Transactions - Further Evidence

$$\begin{aligned}
 Sell_{s,l,t} = & \alpha + HighExposure_s + Post_t + Listed + \\
 & HighExposure_s \times Post_t + HighExposure_s \times Listed + Post_t \times Listed + \\
 & \boxed{HighExposure_s \times Post_t \times Listed} + \epsilon_{s,l,t} \quad (2)
 \end{aligned}$$

	Sell
<i>HighExposure_s × Post_t × Listed</i>	0.1706** (0.07311)
N	288
R-Squared	0.345

Roadmap

- Natural experiment in Argentina
- M&A in Argentina
- M&A in emerging markets

Extending Results to Other Regulations/Emerging Markets

If results can be generalized, changes in the regulatory environment should shape M&A transactions

Panel of 59 emerging markets over 14 years

Regulatory change	Private acquiring listed	Listed acquiring private
More business-unfriendly	↑	↓
Less business-unfriendly	↓	↑

Extending Results to Other Regulations/Emerging Markets

If results can be generalized, changes in the regulatory environment should shape M&A transactions

Panel of 59 emerging markets over 14 years

Regulatory change	Private acquiring listed	Listed acquiring private
More business-unfriendly	↑ 22.8pp	↓ 11.8pp
Less business-unfriendly	↓ 12pp	↑ 5pp

Is it Bribery?

Firms in industries **more** prone to bribery

Regulatory change	Private acquiring listed	Listed acquiring private
More business-unfriendly	↑	↓
Less business-unfriendly	↓	↑

Firms in industries **less** prone to bribery

Regulatory change	Private acquiring listed	Listed acquiring private
More business-unfriendly	=	=
Less business-unfriendly	=	=

Concluding Remarks

- 1 Show that private firms have more flexibility when operating in emerging markets
Mitigate regulatory effect by 46%
- 2 Show that the value this flexibility creates is large enough as to shape M&A patterns in EM
Less friendly: % tx private firms acquire listed firms increases by 22.8 pp
More friendly: % tx private firms acquire listed firms decreases by 12 pp
- 3 Show that markets respond to reduce impact of regulations on corporate value
Business-unfriendly regulations attract firms that defy them

Thank you!