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

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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

Doing Business in Emerging Markets

Question 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?
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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
My contribution

1. Show that private firms have more flexibility when operating in emerging markets

2. Show that the value this flexibility creates is large enough as to shape M&A patterns in EM

3. Show that markets respond to reduce impact of regulations on corporate value
In February 2012, the government banned firms from transferring profits abroad.
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The Setting - After Regulation

US Headquarters

Argentine Subsidiary

Mexican Subsidiary

Customer (Argentine Market)

$15 (instead of $10)

Profits of $5

$15

Goods

Goods

What if the price has gone up for other reasons?
The Setting - After Regulation

What if the price has gone up for other reasons?
The Setting - Counterfactual

US Headquarters

- Argentine Subsidiary
- Mexican Subsidiary
- Domestic firm (non-related)

Goods
- $15 (before: $10)
- $10 (before: $10)

Profits of $5

Same product number ✓
Same manufacturer ✓
Same country ✓
Difference in differences:

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

Where \( i \): Good, \( j \): Importer, \( k \): Exporter, \( m \): Month, and \( t \): Time
## Results - Overpricing of Imports

<table>
<thead>
<tr>
<th>Price</th>
<th>(1) Private firms</th>
<th>(2) Listed firms</th>
<th>(3)</th>
<th>(4)</th>
<th>Difference (1) - (3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Post</td>
<td>0.00376 (0.020)</td>
<td>0.00172 (0.020)</td>
<td>0.00861 (0.017)</td>
<td>0.00810 (0.017)</td>
<td>-0.00485</td>
</tr>
<tr>
<td>Related</td>
<td>-0.0530*** (0.018)</td>
<td>-0.0548*** (0.017)</td>
<td>-0.0889** (0.039)</td>
<td>-0.0892** (0.039)</td>
<td>0.0359</td>
</tr>
<tr>
<td>Post × Related</td>
<td>0.0996*** (0.031)</td>
<td>0.0990*** (0.031)</td>
<td>0.0134 (0.017)</td>
<td>0.0133 (0.018)</td>
<td>0.0862***</td>
</tr>
</tbody>
</table>

Product FE: Yes; Month FE: No; N: 430,846

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

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

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

M&A Transactions by type
Argentina

- Private acquirer and listed target
- Listed acquirer and private target
Patterns in M&A Transactions - Further Evidence

\[ Sell_{s,l,t} = \alpha + HighExposure_s + Post_t + Listed + \]
\[ HighExposure_s \times Post_t + HighExposure_s \times Listed + Post_t \times Listed + \]
\[ \text{HighExposure}_s \times \text{Post}_t \times \text{Listed} + \epsilon_{s,l,t} \]  \hspace{1cm} (2)

| \text{HighExposure}_s \times \text{Post}_t \times \text{Listed} | 0.1706** \\
| \hspace{1cm} \text{(0.07311)} |

| \text{N} | 288 |
| \text{R-Squared} | 0.345 |
Roadmap

- Natural experiment in Argentina
- M&A in Argentina
- M&A in 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**

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<tr>
<th>Regulatory change</th>
<th>Private acquiring listed</th>
<th>Listed acquiring private</th>
</tr>
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<tbody>
<tr>
<td>More business-unfriendly</td>
<td>↑</td>
<td>↓</td>
</tr>
<tr>
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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

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</thead>
<tbody>
<tr>
<td>More business-unfriendly</td>
<td>↑ 22.8pp</td>
<td>↓ 11.8pp</td>
</tr>
<tr>
<td>Less business-unfriendly</td>
<td>↓ 12pp</td>
<td>↑ 5pp</td>
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Is it Stricter Auditing and Enforcement Standards?

Firms listed in markets with **strict** auditing and enforcement standards

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Firms listed in markets with **more lenient** auditing and enforcement standards

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<td>=</td>
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<tr>
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<td>=</td>
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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!