Import to invest: Impact of cultural goods on cross-border mergers and acquisitions

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ABSTRACT

Existing studies have demonstrated the necessities of formal institutions and negativity of cultural distance in international investments. Surprisingly, China's exponential increase of cross-border mergers and acquisitions (M&As) and its low-quality institutions and distinct cultural norms contradict these studies. This paper aims to tackle this puzzle by examining the role of cultural imports in cross-border M&As. Our empirical evidence suggests that the trade of cultural goods significantly increases the volume and realized economic gains of M&As from importing to exporting countries. Our results are robust to alternative measures and an instrumental variable approach. On exploring potential channels, we find that imported cultural goods could drive cultural convergence between countries and also mitigate the adverse effect of cultural distance on merger outcomes. We further show that cultural imports could help firms in overcoming contractual barriers at target countries. This paper provides practical implications for cross-border investments in the current world with intensified cultural conflicts.

1. Introduction

Cross-border mergers and acquisitions (M&As) represent approximately 40% of all M&A deals and have become a crucial form of globalization over the past few decades (Frésard et al., 2017). Firms can profitably expand their comparative advantages overseas and create substantial value via cross-border M&As (Hymer, 1976; Neary, 2007). Thus, one of the fundamental research questions is what factors direct merger activities and improve investment efficiency. Prior studies have shown the necessities of sufficient financial resources and strong institutional frameworks for outward M&As (e.g., Di Giovanni, 2005; Bris and Cabolis, 2010). In particular, cultural distance impressively impedes foreign investment between two countries (Portes and Rey, 2005; Ahern et al., 2015). For example, Siegel et al. (2011) show that different attitudes toward egalitarianism decrease the volume of security issues, bank loans, and M&As for a country-pair.

At first glimpse, the academic findings do not correspond with the M&A experience of China over the past 20 years. For the period of 1996–2016, the total transaction value of cross-border M&As initiated by Chinese firms reached $950 billion, making China the sixth ranked in the world.[1] China even took second place in 2016, after only the United States. However, the levels of China's financial development and institutional quality are rather below average by standard measures (e.g., La Porta et al., 1998; Ding et al., 2018). China's cultural norms, such as a kinship-based clan culture or the collectivism of emphasizing group goals, are far away from Western beliefs (Greif and Tabellini, 2010). Common language, a proxy for cultural distance (Rossi and Volpin, 2004), is also rarely applicable to China and its investment partners, as only five countries and regions in the world speak Mandarin as an official language.[2]

Nonetheless, last twenty years witness an explosive increase in outward M&As from China, even toward culturally distant countries. According to the World Value Survey (WVS), the levels of trust are at the 25th and 85th percentiles, respectively, for China and Germany in comparison to all surveyed countries, implying distinct social norms in these two countries.[3] Meanwhile, the value of China's merger activities

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[1] This is the authors' calculation, based on data from the SDC Platinum.
[2] We extract the language information from the CEPII database. The five countries and regions that share a common language with China are Singapore, Malaysia, Hong Kong, Taiwan, and Macau.
[3] The information on trust is from the following survey question of the WVS: "How much you trust: People of another nationality." Ahern et al. (2015) employs trust to measure country-pair cultural distance.

in Germany increased approximately 33 times from 2007/2008 (the peaking years of global M&As before the 2008 financial crisis) to 2014. Also, China's M&A activities in Brazil, whose official language is Portuguese, that is, not either Mandarin or English, increased more than 20 times over the past 10 years. The coexistence of fast M&A growth and a fairly large cultural distance between China and its target countries seems to be puzzling. Therefore, our paper aims to reconcile this contradiction by investigating the effect of a dynamic form of cultural relation that is new to the literature.

Cultural distance is not static. Firms can build trust and learn about the work ethic of their trade partners from repeated interactions (Araujo et al., 2016). Imported media, like Hollywood movies, can enormously enhance how local people understand U.S. social norms and business ethics (Quinn, 2009). Also, Olivier et al. (2008) point out that goods integration and social integration are related to the dynamics of cultural identity. However, most of the proxies for cultural distance in studies on cross-border investments, for example, language, geography distance, Schwartz's survey data (1999), Hofstede's (2001) cultural dimensions, and WVS, exhibit few variations over a restricted sample period (see, e.g. Lee et al., 2008; Ahern et al., 2015).

To fill the void, this paper examines the role of cultural imports, a product-based cultural relation, in the process of cross-border M&As. Cultural imports refer to the imports of cultural goods that are defined by UNESCO Framework for Cultural Statistics.[4] Books, software, films, and audiovisuals are typical cultural goods. Unlike common commodities, cultural goods convey the cultural values of exporting countries and provide heterogeneous valuation among consumers in different countries (Francois and Ypersele, 2002). The United Nations' *Universal Declaration on Cultural Diversity* declares that "cultural goods and services which, as vectors of identity, values and meaning, must not be treated as mere commodities or consumer goods."[5] A nascent literature demonstrates that the trade of cultural goods is relevant to changing cultural values. Richardson (2006) argues that broadcasting from dominant countries (e.g., the United States) threatens local culture. Disdier et al. (2010) show that the import of audiovisual services affects parents' choice of baby names. More recently, Maystre et al. (2014) and Masood (2019) show that cultural imports might erode the traditional norms of importing countries and the exchange of cultural goods drives cultures to converge on a global basis. In this way, cultural imports could be viewed as a channel of bridging cultural distance between trade partners.

To empirically explore whether and how cultural imports play a role in the unprecedented development of China's outbound M&As, we first estimate the effect on the volume of M&As at the country-pair level. Drawing on the data of M&A deals from the SDC database and cultural imports from UN Comtrade Database over the period of 1996–2016, we find that importing more cultural goods from a specific country significantly leads to a larger volume of cross-border M&As toward that country. The positive effect of cultural imports strongly holds after the inclusion of additional country controls and stringent fixed effects. To address endogeneity concerns, we employ the genetic difference for a given country-pair to instrument for bilateral cultural imports, and our results are virtually unchanged from the instrumental variable (IV) regressions.

We also examine cross-border M&As at the firm level, as it is a typical form of firm expansion. Using stock price and financial statement information, we find that the realized economic gains of acquirers are positively and significantly related to the volume of cultural goods imported from target countries. The results show that cumulative abnormal returns around deal announcements are higher when the amount of cultural goods imported from target countries is larger. Moreover, we find that

acquirers experience significantly better accounting performance when target countries export a substantial amount of cultural goods to China.

We then explore several potential channels by which cultural imports dramatically increase China's outbound M&As. Consistent with the notion that the exchange of cultural goods reduces cultural diversity (Masood, 2019), we find that the volume of cultural imports is significantly and negatively associated with cultural distance measured by the attitudes towards hierarchy, social trust, and attitudes towards children. Moreover, we show that cultural imports could significantly alleviate the adverse effect of cultural distance on merger outcomes. We also show that the positive relation between cultural imports and merger performance becomes much stronger when target countries have a weak institutional framework. The evidence collaborates the argument that alternative institutions come in to deal with investment obstacles when strong formal institutions are absent. Given these results, we conclude that cultural imports lead to better merger outcomes by bridging the cultural distance between countries and alleviating contractual barriers in cross-border M&As.

Our analysis provides new insight into the explosive increase of M&A outflows from China and also, the active participation in foreign investments of several emerging economies characterized by a large cultural distance from the rest of the world. To the best of our knowledge, our paper is among the first wave of papers relating cultural trade to foreign investments. This paper contributes in several ways to the literature on the relation between culture and international flows of capital and goods. Studies on international investments suggest that firms and individuals are more likely to make either finance or real investments in culturally proximate countries (e.g., Sarkissian; Schill, 2004; Siegel et al., 2011; Giannetti; Yafeh, 2012; Ahern et al., 2015). However, most of these papers consider culture proximity to be static. The present study, by way of contrast, examine the issue from the dynamic perspective on the product-based cultural relation. Also, our exploration provides new empirical evidence for an expanding literature that derives a relation between goods integration and culture evolvement (e.g., Olivier et al., 2008; Maystre et al., 2014).

Our paper also contributes to the literature on the interplay between informal and formal institutions and their impacts on economics. A set of the literature, for example, Acemoglu et al. (2001) and Acemoglu and Johnson (2005), emphasizes the long-run effect of formal institutions, such as juridical and contractual environments, whereas some other studies (e.g., Guiso et al., 2006; Tabellini, 2008) think of deeply held values as primary persistent factors for economic outcomes. Recent work finds that cultural and formal institutions tend to move together and could mutually affect firm investments (e.g., Tabellini, 2010; Guiso et al., 2016). The present paper supplements these studies by showing that cultural relations act as a potent factor in cross-border M&As when formal institutions are underdeveloped.

Third, our work complements an extensive set of studies that investigates the relation between foreign direct investment (FDI) and trade. Prior studies have mainly aimed to examine whether these two forms of globalization are complements or substitutes at the country, firm, or product level (see, e.g., Mundell, 1957; Lipsey and Weiss, 1984; Goh et al., 2013; Conconi et al., 2016). However, these studies fail to differentiate goods embedded with cultural values from common commodities with homogeneous consumption values, which may affect firms' foreign entry decisions through different channels. We fill the gap by primarily focusing on the exchange of cultural goods in cross-border investments.

Finally, our work provides policy implications for the governments of emerging economies who aim to promote efficient foreign investments. Certain export-oriented policies, such as easing restrictions on foreign financing, can intensify the exchange of goods (Bose et al., 2020), and hence may impose a second order effect on foreign investments. Great cultural diversity is well recognized in our world, and the recent coronavirus pandemic (COVID-19) highlights how differing cultural values between countries can exacerbate conflict. Within this context, the exchange of cultural goods may act as an effective way to drive a

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[4] See the term definition on the website of http://uis.unesco.org/en/glossary-term/cultural-goods.

[5] See details on the website of http://www.unesco.org/new/fileadmin/MULTIMEDIA/HQ/CLT/pdf/5_Cultural_Diversity_EN.pdf.

convergence and increase resource allocation efficiency on a global basis.

The rest of this paper is as follows. Section 2 discusses the relation between investment obstacles and cultural imports. Section 3 describes the data. Section 4 presents the empirical evidence. Section 5 explores potential mechanisms how cultural imports affect cross-border M&As. Section 6 concludes.

2. Cultural imports and investment obstacles in cross-border M&As

Cross-border investments are plagued with both formal and informal barriers. Long geographic distance implies substantial transportation and communication costs, either in the process of negotiation or in ex post coordination between subsidiaries and headquarters (Portes and Rey, 2005). Harsh tariff increases trade costs of importing specialized inputs and exporting outputs for the merged entity. Also, M&As are often viewed as one form of resource allocation across countries and industries, and poor investor protection impedes efficient allocation (Burkart et al., 2014). Generally, firms encounter two main obstacles when investing abroad: information asymmetry and contract enforcement (Gelos and Wei, 2005; Javorcik et al., 2011). We posit that cultural imports, either as a vector of cultural identity or as one form of bilateral trade, may alleviate these two problems.

Cultural factors are potential sources of information asymmetry in cross-border investments (e.g., Sarkissian and Schill, 2004; Siegel et al., 2011). An M&A deal, especially a successful deal, demands sufficient information on the target country's work ethic, tastes, and beliefs. Halkos and Tzeremes (2011) and Chen et al. (2018) demonstrate that cultural conflicts increase the integration costs and agency costs required to manage foreign subsidiaries; Guiso et al. (2013) find that frequent cultural flows promote cooperation among employees from different countries and enhance synergy gains. The likelihood of a merger's success can be inferred by the extent of information asymmetry generated by cultural distance.

In this sense, we conjecture that cultural imports could reduce information asymmetry by lessening the cultural gap between two countries and increasing a country's familiarity with exporting countries. First, cultural imports have been proven to drive product-based cultural convergence (Disdier et al., 2010; Maystre et al., 2014; Masood, 2019). A country's exposure to imports also increases local media slant throughout the country toward the exporting country (Lu et al., 2018). Thus, cultural imports may erode the inherent beliefs and habits of the local people and make them more willing to accept the ethics and values of exporting countries. Second, enhanced familiarity with exporting countries may breed investment. In fact, the phenomenon that "familiarity breeds investment" is well documented in the literature as a reflection of either irrational psychological bias or information advantage (Huberman, 2001). Javorcik et al. (2011) show that ethnic network promotes FDI by reducing the costs of information gathering, and Santana-Gallego et al. (2016) find that tourism increases trade volume as a source of information on customer preference. Following similar arguments, cultural imports, by facilitating the exchange of information and increasing familiarity between countries, should promote cross-border M&As from importing to exporting countries.

Cultural imports may also alleviate contractual barriers in cross-border M&As. The quality of governance and contractual environment are found to be crucial to the volume and economic gains of cross-border M&As (Bris and Cabolis, 2008; Frésard et al., 2017). While, in reality, many countries with poor investor protection actively participate in international investments and trade, the existing literature demonstrates that alternative institutions play a role when formal institutional framework is underdeveloped. Rauch and Trindade (2002) show that ethics networks act as one contractual enforcement mechanism in international trade. Conconi et al. (2016) show that exporting experience reduces uncertainties and expropriation risks in the internalization process. Araujo et al. (2016) suggest that repeated interactions shape the

dynamics of exporting. Likewise, in the context of cultural trade, Chinese firms may learn about the reliability of exporters and even about the whole business environment of countries that are selling cultural goods. The trade relation may strengthen bilateral trust, a notable determinant in cross-border investments, and helps capture suitable target firms that are less likely to engage in disputes. Through this lens, cultural imports, as an alternative institution, are expected to reduce the difficulties firms face in enforcing contracts across national borders.

Summarizing our discussion, we argue that cultural imports could lessen cultural distance and alleviate contractual barriers and, as a result, increase the economic gains of cross-border M&As. We will explore the cross-sectional variations based on country-pair cultural distance and the quality of investor protection to test the abovementioned predictions.

3. Data and estimation strategy

3.1. Data

The data used in this paper are drawn from several sources. We first collect data of cross-border M&As announced between 1996 and 2016 for all Chinese acquirers from the Securities Data Company (SDC) Platinum. We omit deals with target firms labeled as multinational or with an unknown location, and particularly we exclude deals targeted in tax heavens.[6] To start our analysis, we construct a sample of acquisitions as large as possible, including deals by listed and unlisted acquirers, as well as completed and uncompleted deals. Our M&A sample consists of 5518 deals covering 130 target countries, among which 3913 are successfully completed. For each M&A, we extract a set of items: acquirer name, announcement date, transaction value, primary industry code, target name, target nation, public status of target firms, deal status, and deal attitude. To conduct country-level analysis, we construct a balanced panel data consisting of 2730 (130 countries × 21 years) country-year observations by aggregating the deal-level data.

According to the Harmonised System (HS) 2007 code provided by the UNESCO Framework for Cultural Statistics (FCS), cultural goods are categorized into six main categories: cultural and natural heritage, performance and celebration, visual arts and crafts, books and press, audiovisual and interactive media, and design and creative services.[7] We obtain the bilateral trade data of 84 products in these six categories from UN Comtrade Database. Cultural imports are calculated as the sum of those cultural goods imported from a specific country.

Moreover, we extract the stock price information from the Wind database and the financial statement information from Compustat Global, so as to evaluate the stock market's reactions and post-acquisition profitability for acquirers.

3.2. Specifications

To empirically investigate the relation between cultural imports and cross-border mergers, we first estimate the following specification:

$$MA\ value\ (MA\ number)_{i,t} = \alpha + \beta\ cultural\ imports_{i,t-1} + \gamma_1 BIT_{i,t}$$
$$+ \gamma_2 rule_{i,t-1} + \gamma_3 GDPpc_{i,t-1} + \gamma_4 Exchrate_{i,t-1} \quad (1)$$
$$+ \delta_i + \sigma_t + \varepsilon_{i,t},$$

where the outcome variable is logarithm of the total transaction value or the frequency of M&A deals from China to country i at time t. The primary focus of this paper, $cultural\ imports_{i,t-1}$, is the total imports of cultural goods from target country i with a one-year lag (in log).

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[6] We take Andorra, Bermuda, British Virgin Islands, Cayman Islands, Isle of Man, Liechtenstein, Monaco, Netherlands Antilles, and Panama as tax heavens.

[7] The HS2007 code is only applicable to trade statistics after 2007, so we convert the HS1996 code to the HS2007 code for data over the period of 1996–2006.

As documented in the previous literature, several other country-level institutional and economic factors strongly affect the intensity and performance of cross-border deals. We first include $BIT_{i,t}$, which measures the duration of time since the target country has signed a bilateral investment treaty with China before year t; we gather the information from the UNCTAD's (category of International Investment Agreement) website. Bilateral investment treaties provide a formal framework for solving foreign business disputes, which is expected to strengthen foreign investor protection for multinational firms.

Next, to measure country governance, we employ the Worldwide Governance Indicators (WGI) constructed by World Bank (*rule*). Higher values of WGI represent better quality. To control for macroeconomic conditions, we obtain data on the annual GDP per capita from the World Development Indicator. Erel et al. (2012) show that the appreciation/depreciation of currency affects country-pair cross-border M&As, so we include the national exchange rate as an additional control. Though legal origins, language, geography distance, and religion all have been proven to play important roles in cross-border deals, the inclusion of country fixed effect omits the effect of these time-invariant variables.

To step further, we aim to examine the value creation effect at the deal level by regressing merger outcomes on cultural imports. The specification is written as follows:

$$
\begin{aligned}
Deal\ outcome_{d,i,t} = {} & \alpha + \beta\ cultural\ imports_{i,t-1} + \gamma_1 BIT_{i,t} + \gamma_2 rule_{i,t-1} \\
& + \gamma_3 GDPpc_{i,t-1} + \gamma_4 Exchrate_{i,t-1} + \gamma_5 private_{d,t} \\
& + \gamma_6 attitude_{d,t} + \delta_i + \sigma_t + \phi_{ind} + \varepsilon_{d,i,t},
\end{aligned}
\tag{2}
$$

where d, i, and t denote deal, target country, and year, respectively. The measures of deal outcome refer to announcement returns and post-acquisition profitability. In addition to country controls in model (1), we also include firm and deal controls in the estimation. We control for a private dummy indicating whether the target is an unlisted firm, as deals have distinguished performance when bidding listed and unlisted targets (Fuller et al., 2002). An attitude dummy, indicating either a friendly deal or unfriendly one, is also included. Country, industry, and year fixed effects are controlled in the deal regressions.

Table 1 presents the summary statistics of all variables used in our analyses, respectively.
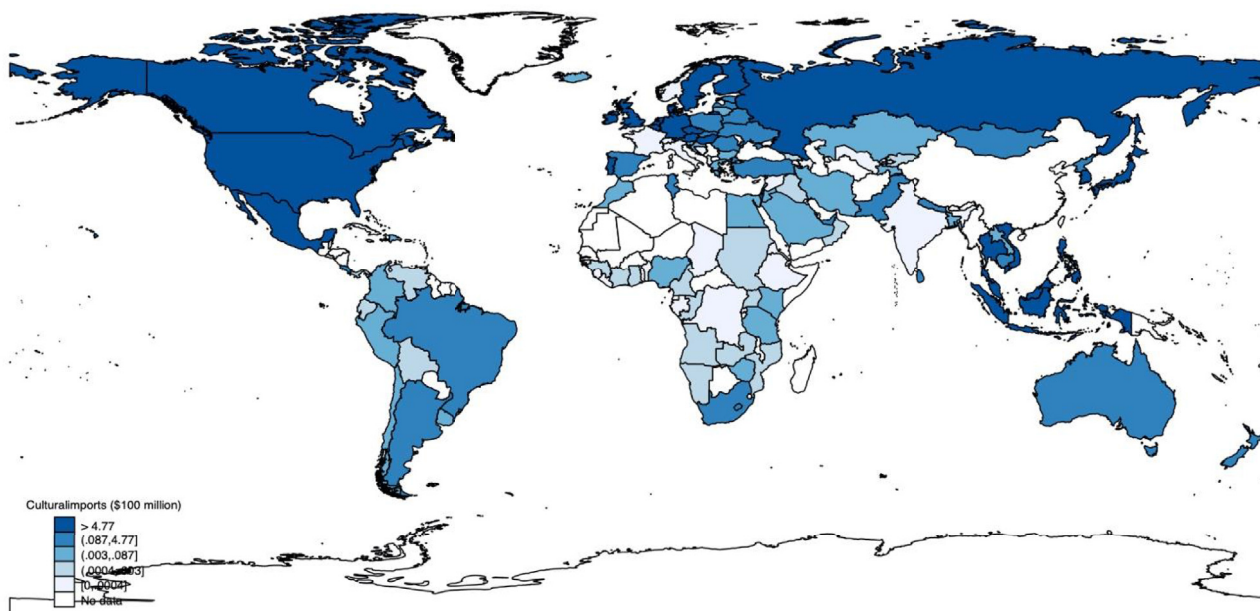
4. Empirical results

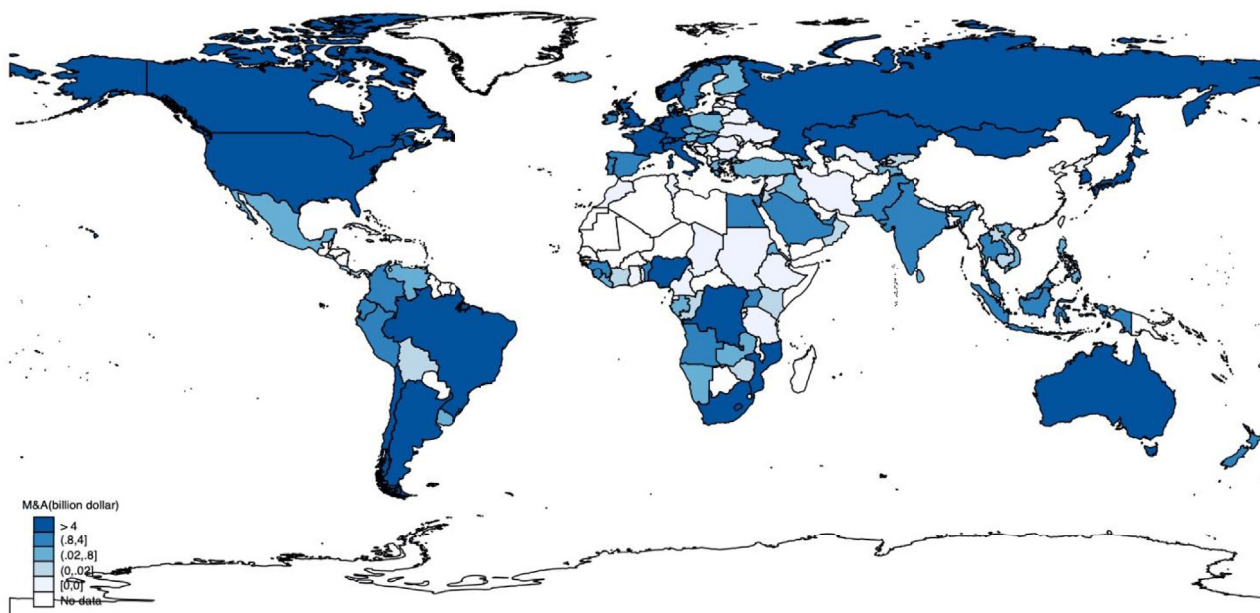### 4.1. Country-level evidence: cultural imports and the volume of M&As

We first provide some suggestive evidence. In spite of its distinct traditional culture, China imports substantial amounts of cultural good from many countries. Fig. 1(a) depicts the worldwide geographical distribution of China's cultural imports over the period of 1996–2016. In addition to East and Southeast Asian countries (e.g., South Korea and Malaysia) that are well recognized to historically and culturally relate to China, the United States, India, Germany, Israel, and Russia most contribute to China's cultural imports. Fig. 1(b) shows that these countries are also important target countries for Chinese firms. Fig. 2 further charts co-movement between outbound M&As and cultural imports during our sample period.

Table 2 reports the benchmark estimations of model (1) across 2730 bidirectional country-year observations. The dependent variables are total transaction value of outbound M&As in first three columns. We observe that the strong trade relation along the dimension of cultural domains is significantly and positively related to the volume of M&As for a specific country-pair. The positive effect has a large economic significance: in Column (1), a 1% increase in the volume of cultural imports is associated with a 23.76% increase in the volume of cross-border acquisition in the subsequent year. The results are virtually unchanged if we include country controls and country and time fixed effects: merger activity increases by 9.7% for the same magnitude of change in cultural imports. The positive role of cultural imports remains statistically and economically significant when we measure the intensity of M&As by counting the number of announced deals in Columns (4)–(6).

Furthermore, in Columns (7) and (8), we confine our sample to completed deals and continue to yield significantly positive coefficients on cultural imports. Combining the results, we conclude that imports of cultural goods not only increase the tendency of Chinese firms to acquire

Table 1
Descriptive statistics.

Panel A. Country-year data set						
Variable	Obs.	Median	Mean	SD	Min	Max
M&A value	2730	0	0.2382	0.7806	0	6.5553
M&A number	2730	0	0.3233	0.7295	0	5.0434
Num_succ	2730	0	0.1994	0.6885	0	6.1115
Value_succ	2730	0	0.2511	0.6315	0	4.6546
Cultural imports	2730	0.0001	0.2532	0.7434	0	4.6467
BIT	2730	6	7.8441	8.1804	0	32
Rule	2730	0	0.3393	5.2592	−12.6025	11.8234
GDPpc	2730	8.7437	8.4724	2.1032	0	11.4245
Exchrate	2730	66.9903	52.0953	55.2432	0	740.6567
Gene diff	2268	0.1152	0.1302	0.0710	0	0.2963

Panel B. Deal data set						
Variable	Obs.	Median	Mean	SD	Min	Max
Cultural imports	3913	0.7211	1.1012	1.1946	0	4.6462
BIT	3913	0	8.4781	10.7084	0	32
Rule	3913	8.3702	6.3703	4.2748	−9.9863	11.3342
GDPpc	3913	10.5362	10.2343	1.0107	0	11.4234
Exchrate	3913	100.4469	95.8034	33.406	0	275.3797
Attitude	3913	1	0.8924	0.3115	0	1
Private	3913	1	0.7064	0.4564	0	1
CAR (-1, 1)	512	0.0002	−0.0054	0.1342	−1.0195	0.5602
CAR (-2, 2)	512	0.0035	−0.0079	0.1493	−1.0373	0.6113
CAR (-3, 3)	512	0.0019	−0.0079	0.1574	−1.0985	0.7324
Post1_ROA	821	0.0453	−0.0001	0.9425	−25.974	0.3435
Post2_ROA	639	0.0434	0.0373	0.1903	−3.8623	0.3186
Post3_ROA	522	0.0368	−0.0002	0.3325	−4.2621	0.4134

Notes. Refer to Table A1 in the appendix for variable descriptions.

(a) cultural imports

(b) cross-border M&As

Fig. 1. Spatial distributions of China's cultural imports and outbound M&As over the period of 1996–2016. A country receiving more (less) M&As or exporting more (less) cultural goods is shed in darker (lighter) blue. (For interpretation of the references to colour in this figure legend, the reader is referred to the Web version of this article.)

firms in the exporting countries of goods but also enhance the intensity of successful deals. The results of other controls are consistent with the previous literature. Both the bilateral investment treaty and strong country governance increase the likelihood of the merger, as they could provide formal frameworks that protect multinationals. In unreported estimations.

we confirm the benchmark results by using the measures of cultural imports with 2- and 3-year lags.[8] The patterns remain robust.

These results provide strong evidence that the consumption of cultural goods substantially increases the volume of cross-border acquisitions in the exporting countries. However, the relation might be interpreted in the reverse direction. The ex-ante large volume of cross-border M&As strengthens the economic relation between two countries and drives more frequent trade activities, including cultural trade. Moreover, cultural imports are correlated with some other omitted variables that may also influence firm decision-making about M&As. For example, countries with favorable tariff policies attract more imports of cultural goods and also increase the competition of domestic markets and a tendency to invest abroad. In this sense, tariff policies could jointly affect the volume of imports and merger activities.
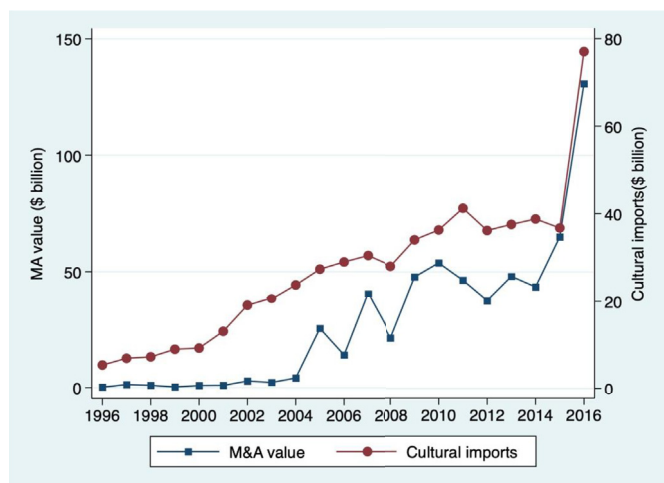
[8] For brevity, we do not tabulate the results here, but they can be provided on request.

Fig. 2. China's cultural imports and cross-border M&As. Red and blue lines represent the aggregated value of imported cultural goods (with a one-year lag) and outbound M&As in our sample, respectively, over the period of 1996–2016. (For interpretation of the references to colour in this figure legend, the reader is referred to the Web version of this article.)

To alleviate these endogeneity problems, we employ an instrumental variable (IV) approach using the country-pair genetic difference as an instrument for cultural imports. Genetic distance initially measured the difference in the distribution of allelic frequencies across populations, and economists extended the measure to the difference at the country level. Several studies have documented that genetic distance is closely related to cultural dimensions, providing a precedence of the relevance condition for our instruments (Giuliano et al., 2014; Ahern et al., 2015). We accordingly collect the data of weighted genetic distance between countries from Spolaore and Wacziarg (2009). The divergence of a gene for a country-pair represents an inherent cultural divergence, which is hypothesized to impose additional barriers in the exchange of cultural goods.

Panel A in Table 3 summarizes second-stage results of IV estimations. Consistent with Table 2, we use the total transaction value of announced M&As in each country-pair, the frequency of announced M&As, the total transaction value of completed M&As, and the frequency of completed

M&As as dependent variables through Columns (1) to (4), respectively. The results consistently show that cultural imports are significantly and positively associated with the volume of cross-border mergers. The size of coefficients in the IV estimations are close to those in the benchmark results in Table 2. Panel B presents first-stage estimations corresponding to each column of Panel A. As expected, we find that genetic difference negatively affects the volume of cultural imports. The significance of the estimated coefficients clarifies the validity of the instrument. Also, the statistics show that our instrument passes both weak instrument and under-identification tests. Consequently, the IV results assure that our benchmark patterns do not mainly stem from reverse causality or omitted variables.

4.2. Deal-level evidence: cultural imports and merger outcomes

The abovementioned analysis provides robust evidence that the intense inflows of cultural goods promote firms from importing countries to engage in merger activities in the exporting countries. However, whether these firms are more successful in negotiations and their integration process is unsolved. If firms exploit their information advantage from such cultural trade relation—a strategy that may reduce substantial costs embedded in ex ante searching and ex post operations—we conjecture that such firms should receive favorable stock market reactions around announcements and experience better long-term operating performance, that is, mergers with more economic gains. There is, however, an alternative hypothesis associated with the familiarity bias. Several studies show that people prefer status quo choices, and their investment decisions are kidnapped by familiarity, leading to less successful outcomes (Seasholes and Zhu, 2010; Jiang et al., 2019). In this sense, we should expect that the intensity of cultural imports results in inferior M&As. These two hypotheses both predict a positive influence of cultural imports on the volume of M&As but unambiguous directions on value creation.

To disentangle two competing hypotheses and capture a wealth effect, we directly concentrate on the short-run and long-run deal performance in Table 4. By drawing on a reduced sample of deals initiated by listed firms, we first examine the reactions of stock market participants to deal announcements. Following a standard event study methodology, we estimate the daily abnormal returns using a market model in which Shanghai Composite index and Shenzhen Component index are taken as the market returns and the estimation window is from 200 days to 20

Table 2
Benchmark results.

	M&A value			M&A number			Value_succ	Num_succ
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Cultural imports	0.2376***	0.1329***	0.0970**	0.3655***	0.2508***	0.2234***	0.0840**	0.1951***
	(6.14)	(3.43)	(2.53)	(13.00)	(9.24)	(8.44)	(2.45)	(8.27)
BIT		0.0292***	−0.0121***		0.0328***	−0.0036	−0.0110***	−0.0049*
		(10.93)	(-2.62)		(17.51)	(-1.14)	(-2.66)	(-1.72)
Rule		0.0273***	0.0249***		0.0239***	0.0216***	0.0217***	0.0183***
		(4.87)	(4.54)		(6.07)	(5.72)	(4.42)	(5.43)
GDPpc		−0.0084	−0.0349*		−0.0194	−0.0400***	−0.0328*	−0.0380***
		(-0.44)	(-1.84)		(-1.45)	(-3.06)	(-1.94)	(-3.26)
Exchrate		−0.0008	−0.0008		−0.0006	−0.0007	−0.0006	−0.0005
		(-1.34)	(-1.34)		(-1.47)	(-1.59)	(-1.14)	(-1.45)
Country FE	No	No	Yes	No	No	Yes	Yes	Yes
Year FE	No	No	Yes	No	No	Yes	Yes	Yes
N	2730	2730	2730	2730	2730	2730	2730	2730
R^2	0.0143	0.0681	0.1199	0.0611	0.1735	0.2456	0.1071	0.2047

Notes. This table presents the estimations of model (1). We take the total transaction value and the number of announced M&As as dependent variables in Columns (1)–(3) and Columns (4)–(6), respectively. The dependent variables are the total transaction value and the frequency of completed deals in Columns (7) and (8), respectively. Refer to Table A1 in the appendix for variable descriptions. Heteroskedastic-corrected *t*-statistics are in parentheses. *$p < 0.1$; **$p < 0.05$; ***$p < 0.01$.

Table 3
An instrumental variable approach.

Panel A. Second-stage results

	M&A value	M&A number	Value_succ	Num_succ
	(1)	(2)	(3)	(4)
Cultural imports	0.1310**	0.2589***	0.1066**	0.2274***
	(2.45)	(6.83)	(2.21)	(6.67)
BIT	−0.0078	−0.0014	−0.0081*	−0.0038
	(-1.60)	(-0.42)	(-1.85)	(-1.24)
Rule	0.0208***	0.0183***	0.0183***	0.0150***
	(3.54)	(4.41)	(3.45)	(4.01)
GDPpc	−0.0199	−0.0344**	−0.0219	−0.0355**
	(-0.90)	(-2.18)	(-1.09)	(-2.50)
Exchrate	−0.0017**	−0.0012***	−0.0015**	−0.0012***
	(-2.54)	(-2.60)	(-2.49)	(-2.73)

Panel B. First-stage results

	Cultural imports			
Gene diff	−0.1008***	−0.1533***	−0.1038***	−0.1931***
	(-5.56)	(-3.14)	(-5.56)	(-3.14)
Kleibergen-Paap rk LM statistic	64.7890	55.4509	73.8092	86.8202
p-value	(0.03)	(0.04)	(0.03)	(0.02)
Kleibergen-Paap rk Wald F statistic	337.2012	689.5283	935.8104	706.6513
Country FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
N	2268	2268	2268	2268

Notes. Panel A presents the second-stage results: the dependent variables are the total transaction value of announced deals, the frequency of announced deals, the total value of completed deals, and the frequency of completed deals, for a country-pair, in Columns (1)–(4), respectively. For brevity, Panel B only presents the coefficients of the instrument, corresponding to each column of Panel A, in first-stage estimations. Refer to Table A1 in the appendix for variable descriptions. Heteroskedastic-corrected *t*-statistics are in parentheses. *$p < 0.1$; **$p < 0.05$; ***$p < 0.01$.

days preceding the announcement. Cumulative abnormal returns (CARs) over the event windows of $(-1, 1)$, $(-2, 2)$, and $(-3, 3)$ are taken as the dependent variables in Columns (1)–(3), respectively.[9] The public status of the target and deal attitude are also controlled in the estimations (e.g. Moeller and Schlingemann, 2005; Renneboog and Zhao, 2014; Field and Mkrtchyan, 2017). The significantly positive coefficients imply that market participants view cultural imports as one channel of enhancing M&A performance. Quantitatively, a 1% increase in the cultural imports from target country raises the acquirer's 3-day CAR by 111 basis points. The favorable market reaction squares with the hypothesis that the inflows of cultural goods help firms reduce information asymmetry and overcome contractual barriers.

It may be argued that market participants cannot fully understand the effect in the short run and thus conceivably underestimate or overestimate the value created by the imports of cultural goods. Therefore, we substantiate our analysis by examining the potential synergy gains in the long run. We calculate return on assets (ROAs) over horizons of 1, 2, and 3 years after the announcement and take them as the outcome variables in Columns (3)–(6) of Table 4. The results in those three columns consistently suggest that cultural imports could improve acquirers' operating performance: the estimated coefficients on cultural imports are all statistically and significantly positive. Overall, deal evidence supports the idea that cultural imports enhance acquiring firms' ability to identify suitable targets and achieve more synergy gains in the exporting countries.

5. Additional analysis

To better understand the potential mechanisms behind the positive effect of cultural imports on the performance of cross-border M&As, we next conduct cross-sectional analysis on several country characteristics that may provide variations in the relation. As discussed in Section 2, additional transaction costs and uncertainties are embedded in the process of international investments (Javorcik et al., 2011). Individuals and firms might have a poor understanding of a culture not their own, including business ethics or tastes of the people, and hence face high communication costs and severe information asymmetry. The weak protection for foreign investors at host countries also hampers corporate mergers and deteriorates the performance. Thus, we explore the cross-sectional variations with country-pair cultural distance and the extent of investor protection at target countries to explain our main results.

5.1. Cultural distance

Cultural factors are potential sources of information asymmetry in cross-border investments (Siegel et al., 2011). When two countries are culturally distant, the searching costs in pre-merger process and the integration and agency costs in post-merger process would be increased. As a result, firms are more likely to depend on the information transferred by the flows of cultural goods to lessen the cultural distance and reduce informational barriers in foreign markets. Also, the enhanced familiarity by cultural imports may "breed investment" (Huberman, 2001) more rigorously when merging entities are originally unfamiliar with the beliefs and values of their counterparties. Consistent with this idea, the positive effect of cultural imports on M&A performance should be more pronounced when the acquirer and target countries are more culturally distant.

To test the predictions, we use World Value Survey (WVS) to measure cultural values along several dimensions. Most of the proxies for cultural distance, such as language, geography distance, Schwartz's survey data (1999), Hofstede's (2001) cultural dimensions, are time-invariant. Therefore, the adoption of these measures cannot allow us to examine whether the flows of cultural goods drive a cultural convergence between two countries. WVS is the largest and up-to-date survey on cultural values and has been used in several studies (e.g., Ahern et al., 2015; Karolyi, 2016). It has carried out 7 waves of survey: 1981–1984, 1990–1991, 1995–1997, 1999–2001, 2005–2007, 2010–2014, and 2017–2018. Thus, we can match our trade and M&A data to the survey period to exploit the time variations of cultural distance. In this subsection, we focus on three dimensions of cultural values that have been documented to affect cross-border investments: hierarchy, trust, and attitudes towards children (See, e.g. Guiso et al., 2006; Siegel et al., 2011; Ahern et al., 2015).[10] A fairly large difference in cultural values of employees between acquirers and targets may impede them to effectively work together and make the coordination more difficult, which imposes additional costs of achieving a successful merger. For example, preference for overtime or family can affect the integration of corporate culture; the attitudes toward hierarchy and egalitarianism determine the interpersonal relationship between works and superiors, and egalitarian managers

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[9] The availability of stock price data over the event and the estimation windows is a necessity for the calculation of CAR, which reduces the size of our sample to 512 deals.

[10] To measure the attitudes toward hierarchy, we draw on the survey question: *People have different ideas about following instructions at work. Some say that one should follow one's superior's instructions even when one does not fully agree with them. Others say that one should follow one's superior's instructions only when one is convinced that they are right. With which of these two opinions do you agree? should follow instructions or must be convinced first.* To measure trust, we use the survey question in WVS: *Generally speaking, would you say that most people can be trusted or that you need to be very careful in dealing with people?* To measure the attitudes toward family and children, we focus on the question: *Do you have any children? (Code 0 if no, and respective number if yes).*

Table 4
Cultural imports and merger outcomes.

	CAR (−1, 1)	CAR (−2, 2)	CAR (−3, 3)	Post1_ROA	Post2_ROA	Post3_ROA
	(1)	(2)	(3)	(4)	(5)	(6)
Cultural imports	0.0111*	0.0130*	0.0115	0.0711***	0.0146*	0.0692***
	(1.71)	(1.69)	(1.25)	(4.29)	(1.84)	(3.51)
BIT	0.0023	−0.0010	−0.0020	−0.0123	−0.0175	0.0165
	(0.30)	(-0.10)	(-0.17)	(-1.01)	(-1.31)	(0.80)
Rule	−0.0188	−0.0244	−0.0193	−0.0406	0.0149	0.0134
	(-0.52)	(-0.59)	(-0.45)	(-0.98)	(1.49)	(1.19)
GDPpc	0.2170	0.1360	0.2165	0.3260	−0.0060	−1.1275*
	(0.82)	(0.45)	(0.72)	(0.81)	(-0.03)	(-1.82)
Exchrate	−0.0006	−0.0003	−0.0007	0.0023	0.0020	−0.0031
	(-0.52)	(-0.20)	(-0.45)	(1.35)	(1.29)	(-1.19)
Attitude	0.0370	0.0316	0.0449	0.0002	0.0504	−0.0173
	(1.54)	(0.89)	(1.22)	(0.01)	(0.90)	(-0.49)
Private	−0.0123	−0.0317	−0.0353	0.1319**	−0.1903	−0.8732***
	(-0.23)	(-0.60)	(-0.66)	(2.07)	(-1.59)	(-3.72)
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes
Country FE	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes
N	512	512	512	814	631	517
R^2	0.6645	0.6502	0.6666	0.1000	0.3405	0.6228

Notes. This table summarizes the results of deal-level regressions. The dependent variables are 3-, 5-, and 7-day CARs; and ROAs 1, 2, and 3 years after M&A in Columns (1)–(6), respectively. Refer to Table A1 in the appendix for variable descriptions. Heteroskedastic-corrected *t*-statistics are in parentheses. *$p < 0.1$; **$p < 0.05$; ***$p < 0.01$.

(workers) cannot reach a coordination with hierarchical workers (managers).

To delineate the effect, we first examine the relation between the volume of cultural imports and cultural distance using the country-pair level data. The cultural distance is calculated as the difference in the average scores of individual responses to survey questions between two countries, i.e., *D_Hierarchy*, *D_Trust*, and *D_Children*. Column (1) of Table 5 shows that an intense flow of cultural goods significantly lessens the cultural distance measured by the attitudes towards hierarchy. Next, we relate the cultural distance with the acquirer returns. The results in Column (2) are in tandem with the arguments in previous studies that large cultural distance leads to poor merger performance (Ahern et al., 2015). Most importantly, we re-estimate our deal regressions by incorporating the interaction term between cultural imports and *D_Hierarchy*. Column (3) reports the results. The direct effect of cultural distance remains significant and negative as in Column (2); particularly, the estimated coefficient on the interaction term is significantly positive at the 1% level, implying that cultural imports could alleviate the adverse effect of cultural distance and increase the acquirer returns. Following similar procedures, we use the cultural distance in social trust and attitudes towards children to reinforce our predictions. The results are reported in Columns (4)–(9). We consistently find that, cultural imports drive a convergence of cultural values, and cultural distance directly imposes a negative effect on merger outcomes. Particularly, the interaction terms between cultural imports and cultural distance are all significant and positive, suggesting that cultural imports strongly weaken the negative influence of cultural distance on the economic gains of acquirers.

Overall, the results in Table 5 provide evidence that cultural imports could enhance the performance of acquisitions in the exporting countries by bridging the cultural gap between two countries.

5.2. Institutional environment

Another important factor in cross-border M&As is institutional environment, particularly protection for foreign investors, at target countries. Low-quality institutions create substantial obstacles for multinational firms (Gelos and Wei, 2005; Frésard et al., 2017), which may result in a sparing amount of cross-border M&As and unsuccessful integration. Therefore, we next examine whether the positive association between cultural imports and merger performance varies when acquiring firms face more contractual barriers in target countries. Prior studies show that

various informal institutions appear to deal with contractual issues when formal institutions are underdeveloped, such as culture, ethics networks and political connections (Rauch and Trindade, 2002; Ding et al., 2018). Thus, the imports of cultural goods, as a conduit of cultural values, are expected to play a more salient role when acquirers pursue firms in countries that cannot protect the interests of foreign investors well.

To test the nonlinearities, we employ a widely used indicator, namely, the index of *Enforcement Time,* from the World Bank Doing Business database (WBDB) to assess the quality of a country's judicial and contractual environments (e.g., Bae and Goyal, 2009; Frésard et al., 2017). High values of enforcement time represent poor contracting institutions. We then augment our deal regressions on announcement returns by introducing the enforcement index and its interaction with cultural imports. The inclusion of controls and fixed effects is analogous. The results are presented in Table 6. The coefficients on cultural imports per se are significantly positive, assuring that cultural imports have a general and positive impact on the merger outcomes. Also, the negative coefficients on *Enforcement Time* in all three columns suggest that long time necessary to enforce contract, i.e. a poor enforceability of contracts, deteriorates merger performance. More importantly, the positive and significant interaction terms between cultural imports and *Enforcement Time* imply that the beneficial effect of cultural imports becomes stronger when the quality of contracting institutions at the target country is relatively low. Thus, the dynamic flows of cultural goods can help multinationals in overcoming certain contractual barriers, and hence alleviate the negative effect of weak institutions on cross-border M&As.

Taken together, the analysis in this section echoes the discussion in Section 2 and provide some insight into potential channels for how inflows of cultural goods affect merger outcomes.

6. Conclusions

Prior studies have shown that cultural distance largely impedes cross-border investments by engendering frictions between entities with different cultural backgrounds. However, China's M&A experience in past decades contradicts these studies. China's deeply held values, e.g. Confucianism, are rarely acceptable and understandable for Western people, and the official language, Mandarin, is not a widely used language in the world. Nevertheless, the value of China's outbound M&As has increased more than 50 times during past twenty years. To tackle the puzzle, this paper introduces a dynamic product-based cultural relation

Table 5
Cultural distance, cultural imports, and deal performance.

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	D_Hierarchy	CAR (−1,1)	CAR (−1,1)	D_Trust	CAR (−1,1)	CAR (−1,1)	D_Children	CAR (−1,1)	CAR (−1,1)
Cultural imports	−0.0042*		0.0058***	−0.0259***		0.0364	−0.0566***		0.0202*
	(-1.96)		(2.81)	(-3.96)		(0.61)	(-5.55)		(1.87)
D_Hierarchy		−23.9290**	−24.4210**						
		(-2.31)	(-2.49)						
Cultural imports × D_Hierarchy			4.1069***						
			(3.98)						
D_Trust					−0.0468	−0.0478**			
					(-0.85)	(-2.53)			
Cultural imports × D_Trust						0.0028***			
						(3.51)			
D_Children								−0.0807***	−0.0679*
								(-4.75)	(-1.88)
Cultural imports × D_Children									0.0428*
									(1.97)
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Country FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
N	1970	234	234	1970	234	234	1970	234	234
R^2	0.5614	0.0716	0.0737	0.5654	0.0709	0.0528	0.8873	0.0757	0.0127

Notes. D_Hierarchy, D_Trust, and D_Children are measures of cultural distance between two countries, which are defined as the difference in average scores of individual responses to three survey questions in World Value Survey. To save space, the estimations of controls are not reported. Controls include *BIT*, *Rule*, *GDPpc*, *Exchrate*, *Attitude*, and *Private*. Refer to Table A1 in the appendix for variable descriptions. Heteroskedastic-corrected t-statistics are in parentheses. *p < 0.1; **p < 0.05; ***p < 0.01.

Table 6
Contracting institutions, cultural imports, and merger outcomes.

	CAR (−1, 1)	CAR (−2, 2)	CAR (−3, 3)
	(1)	(2)	(3)
Cultural imports	0.1699***	0.1571***	0.1534***
	(2.88)	(2.99)	(2.72)
Enforcement Time	−0.0003***	−0.0003***	−0.0003***
	(-2.89)	(-3.19)	(-3.15)
Cultural imports × Enforcement Time	0.0006**	0.0006*	0.0007*
	(2.09)	(1.73)	(1.80)
Controls	Yes	Yes	Yes
Country FE	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
N	440	440	440
R2	0.7073	0.6824	0.6951

Notes. This table presents estimation results by incorporating *Enforcement Time* and its interactions with cultural imports in model (2). High values of enforcement time represent poor contracting institutions. The dependent variables in Columns (1)–(3) are three-day, five-day, and seven-day CARs, respectively. To save space, the estimations of controls are not reported. Controls include *BIT*, *Rule*, *GDPpc*, *Exchrate*, *Attitude*, and *Private*. Refer to Table A1 in the appendix for variable descriptions. Heteroskedastic-corrected t-statistics are in parentheses. *p < 0.1; **p < 0.05; ***p < 0.01.

and examine its role in the cross-border M&As. Our central hypothesis is that substantial inflows of cultural goods help firms reduce information asymmetry generated from cultural distance and alleviate contractual barriers when investing across national boundaries. Our work concentrates on whether and how cultural imports affect the volume of country-pair cross-border M&As and deal performance.

By using the country-year dataset covering 130 target countries over the sample period of 1996–2016, we uncover that cultural imports are an important driver of outbound cross-border M&As. The volume of outbound M&As significantly increases following an intense inflow of cultural goods for a specific country-pair. The patterns remain unchanged when employing alternative specifications and an instrumental variable approach with genetic difference as the instrument. Deal-level evidence shows that the imports of cultural goods matter a lot for merger outcomes. Acquirers experience both favorable market reactions around

announcement dates and superior long-run operating performance when bidding targets in the countries that export substantial amount of cultural goods to China. The favorable gains suggest that the dynamic product-based cultural relation can reduce frictions and simplify post-acquisition integration in outbound M&As.

By exploring potential channels, we find that the intense flows of cultural goods could reduce the distance in cultural values between two countries and alleviate the adverse effect of cultural distance on the economic gains of acquirers. Furthermore, we find that the value creation effect of cultural imports is also much stronger for deals of which the acquirers receive poor investor protection in target countries. The cross-sectional variations provide insight into two potential channels through which cultural imports affect merger performance: lessening cultural gap and alleviating contractual barriers.

Our findings have several policy and managerial implications. Inherently cultural factors, like language, religion, or deeply held cultural values, are difficult to change. Policy makers should recognize that frequent cultural communications might shorten cultural distance created by cultural facts and thereby benefit economic integration. The relation between cultural imports and outbound M&As implies that governments could promote foreign investments toward a specific country by easing the imports of cultural goods from that country and, alternatively, attract more inward foreign investments by promoting the exports of domestic cultural goods. Managers of multinationals might incorporate the exchange of cultural goods when choosing a target country; also, the heterogenous effect from different levels of institutional quality underscores the necessity of firms understanding the interplay between cultural factors and contractual environments.

Overall, our findings illustrate that the imports of cultural goods matter across many aspects of cross-border M&As, and the magnitude largely depends on the extent of contractual and informational obstacles that firms encounter during the merger process. This paper complements the growing field of literature on culture and investments. Together with many other studies, it further emphasizes that international trade could attract investments from other countries. Cultural goods are only one of the dynamic cultural flows between countries, and it would be interesting to examine whether the trade of cultural services or labor mobility related to cultural sectors also substantially affect international investments.

Declaration of competing interest

The authors, Chang Li and Lianxing Yang, declare that they have no known competing financial interests or personal relationships that could have appeared to influence the work reported in this paper.

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Appendix A

Table A1
Variable descriptions

Variables	Descriptions	Data Source
Panel A. Country-year data set		
M&A value	Logarithm of the total transaction value of announced M&A deals plus one for a specific country-pair	SDC
M&A number	Logarithm of the number of announced M&A deals plus one for a specific country-pair	SDC
Value_succ	Logarithm of the total transaction value of completed M&A deals plus one for a specific country-pair	SDC
Num_succ	Logarithm of the number of completed M&A deals plus one for a specific country-pair	SDC
Cultural imports	Logarithm of the total value of cultural imports from a specific country plus one	UNCTAD
BIT	The duration of time since the target country has signed a bilateral investment treaty with China before acquisition year	UNCTAD
Rule	Worldwide Governance Indicators (WGI)	World Bank
GDPpc	Logarithm of gross domestic product per capita	WDI
Exchrate	Exchange rate	WDI
Gene diff	Genetic difference	Spolaore and Wacziarg (2009)
D_Hierarchy	The difference between two countries in the average scores of responses to the survey question: *People have different ideas about following instructions at work. Some say that one should follow one's superior's instructions even when one does not fully agree with them. Others say that one should follow one's superior's instructions only when one is convinced that they are right. With which of these two opinions do you agree? should follow instructions or must be convinced first.*	WVS
D_Trust	The difference between two countries in the average scores of responses to the survey question: *Generally speaking, would you say that most people can be trusted or that you need to be very careful in dealing with people?*	WVS
D_Children	The difference between two countries in the average scores of responses to the survey question: *Do you have any children? (Code 0 if no, and respective number if yes)*	WVS
Enforcement Time	An index to measure the time of enforcing contract	Doing Business
Panel B. Deal data set		
Cultural imports	Logarithm of one plus the total value of cultural imports at the target country	UNCTAD
Private	A dummy that equals one for an unlisted target and zero otherwise	SDC
Attitude	A dummy that equals one for a friendly deal and zero otherwise	SDC
CAR (-1, 1)	3-day cumulative abnormal returns	Wind
CAR (-2, 2)	5-day cumulative abnormal returns	Wind
CAR (-3, 3)	7-day cumulative abnormal returns	Wind
Post1_ROA	Return on assets one year after M&A	Compustat Global
Post2_ROA	Return on assets two years after M&A	Compustat Global
Post3_ROA	Return on assets three years after M&A	Compustat Global

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