Conflictive home-host country relations have a strong, negative effect on policy risk

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Policy risk negatively affects acquisition completion, but the strength of the effect is dependent on home-host country relations, according to new research published in *Global Strategy Journal*. The relationship between policy risk and cross-border acquisition completion is negative and strong under conflictive relations, weaker under cooperative relations, and weakest under ambivalent relations, the study authors found.

"In the recent decade, we are observing major shifts in the geopolitical environment and ever more dynamic intercountry relations that will likely continue to influence cross-border investments, which makes our research timely and relevant," says lead researcher Tsvetomira V. Bilgili, an assistant professor at Kansas State University.

The team used longitudinal event data on intercountry interactions to infer cooperative, conflictive, and ambivalent relations. Each event in the sample was assigned a score between -10 and +10 to indicate how positive or negative the event is. For example, the signing of a formal agreement was scored 8, while the imposition of an embargo, boycott, or sanctions received a ranking of -8.

To test the effect of home-host country relations on the relationship between policy risk and cross-border acquisition completion, the research team used logistic regression on a sample of 26,124 cross-border acquisitions by 14,568 unique acquirers.

The researchers found that for each unit increase in policy risk, the likelihood of completing a deal decreases by 2.2%, but that home-host country relations can change the effect. When the relationship between countries is conflictive, policy risk poses even greater challenges to deal completion because host governments may be more motivated to intervene in the deal.

Cooperative intercountry relations may offer a buffer, but the effect of policy risk isn't fully mitigated; however, ambivalent intercountry relations reduce the effect of policy risk to the greatest extent—possibly, the team hypothesized, because host governments may want to maintain relations with the home country by avoiding arbitrary and adverse actions toward acquirers.

"For instance, China and India have long had disputes over border security but have also collaborated in the economic realm," Bilgili says. "We argue that the state of intercountry relations can be indicative of the host country government's intentions and motivations to engage in arbitrary or opportunistic policy changes that can prevent the completion of cross-border acquisitions."

For executives, this underscores the importance of keeping an eye on intercountry relations to better assess the likelihood of policy changes that could have a negative effect on foreign acquisitions. Depending on the state of intercountry relations, some organizations will be better positioned to successfully pursue investment opportunities in high policy risk countries.

"Our findings suggest that in an increasingly complex global environment, understanding intercountry relations is critical to firms' ability to complete cross-border acquisitions in countries where policy risk is high," Bilgili says.

More information: Tsvetomira V. Bilgili et al, Friends, foes, or "frenemies": Intercountry relations and cross-border acquisitions, *Global Strategy Journal* (2022). DOI: 10.1002/gsj.1460

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