Do all networks facilitate international commerce?

The case of US law firms and the mergers and acquisitions wave of the late 1990s

Simon J. Evenett

December 2001

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The World Bank, The Brookings Institution, and CEPR

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Abstract:
Unlike prior research, which has tended to focus on the effects of business networks on the international flow of goods and services, this paper examines the extent to which the international presence of US law firms stimulated or retarded overseas mergers and acquisitions (M&A) activity by American corporations in 1999. In a world of merger notification requirements and reviews, these law firms can help clients overcome regulatory hurdles abroad, adding grease to the international market for corporate assets. These law firms can also oppose transactions that are inimical to their US clients' interests, throwing sand into the wheels of this form of international commerce. Evidence is presented here to suggest that the US law firm with the greatest global reach (Baker & McKenzie) has facilitated such commerce, whereas the combined effect of five smaller US law firms with considerable global footprints appears to have reduced US outward M&A in 1999. The geographical distribution of these six law firms' offices around the world is such that, on net, many non-G7 nations have experienced US M&A transactions that are larger in total value and in average size that had those law firms not operated in these jurisdictions. This, in turn, suggests that these nations' own firms are now more exposed to pressures from the international market for corporate control. A byproduct of this study is the potentially provocative finding that the presence of national merger review procedures abroad tends to cut in half the amount of overseas M&A undertaken by US corporations.

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1. **Introduction**

In recent years there has been considerable interest in the ways in which groups of market participants interact so as to facilitate international trade. Particular emphasis has been given in this research program to mechanisms to locate potential buyers and sellers and to overcome contract enforcement problems (Rauch, forthcoming). Given the considerable growth in international trade flows since 1985, especially in the pan-Pacific region where Chinese business groups operate extensively, it is perhaps not surprising that research into such mechanisms has gathered pace (see, for example, Rauch and Trindale, forthcoming.) The late 1990s did, however, witness a surge in one form of international commerce that has received considerably less attention from international economists: a global wave of mergers and acquisitions (M&A). What is more, since the 1980s leading law firms have been expanding their presence outside their home jurisdictions, creating networks of legal professionals to advise multinational corporations as they take advantage of the opportunities presented by the current era of international market integration. This paper seeks to examine whether the formation of such global law firms has helped contribute to overseas US M&A activity during 1999, one of the boom years in this global wave of M&A.

The causal links between the presence of global legal networks and transactions in the international market for corporate assets are different from those traditionally emphasized in studies of international trade flows. The principal
difference is that the purchase and sale of firms often involves review and approval by national competition policy or antitrust authorities. Indeed, a merger of two firms may require the approval of many national authorities. For example, the merger between Price Waterhouse and Coopers and Lybrand, announced on September 17, 1997, required approval in the United States, by the European Commission, in Canada, Australia, New Zealand, and Switzerland—to name some, and by no means all, of the jurisdictions involved (Kolasky, 2000). Law firms with a global imprint can help clients obtain clearance from national antitrust authorities for mergers with, or takeovers of, foreign firms. Familiarity with both their clients needs and with overseas merger review procedures, which comes about in part by retaining skilled lawyers in offices abroad, can help add grease to the international market for corporate assets. Here, the impediments that networks help overcome are man-made, rather than the asymmetries of information emphasized in much of the literature on network formation and market outcomes.

Another feature of merger review is that some jurisdictions appear to give rival firms a greater role in presenting evidence against a proposed merger than others. It is often claimed that the European Commission’s merger review procedure gives opponents to a proposed merger a greater role than in comparable U.S. proceedings (Venit and Kolasky, 2000; Boeder, 2000). To the extent that this is true, global law firms can throw sand into the wheels of this form of global commerce, by presenting evidence against proposed transactions
that are inimical to their clients’ interests. *A priori*, then, it is unclear whether the spread of global legal networks has facilitated or retarded cross-border mergers and acquisitions.

A dataset detailing the overseas presence of 100 US law firms in 1997 is employed here to examine whether their geographical spread correlates with the pattern of overseas M&A by US corporations in 1999. Controlling for the other plausible determinants of international M&A activity (such as distance from the United States, and the national income and corporate tax rates of the overseas jurisdiction), I examine whether the presence of six US law firms, which together account for 60 percent of the employment of US lawyers abroad in the countries considered in my sample, have contributed to the observed level of overseas M&A activity by American corporations in 1999. In addition, as merger notification requirements and reviews tend to apply more strictly to relatively larger M&A transactions, I examine whether the presence of these six US law firms increases or decreases the mean size of recorded M&A transactions abroad. The principal finding is that presence in a country of the US law firm with the greatest footprint overseas (Baker & McKenzie) substantially raises the total value and mean value of US M&A activity in that country. In contrast, the presence in an economy of five other US law firms with large overseas operations tends to reduce the total value and mean size of M&A transactions in that economy. On net, however, the geographical distribution of these six law firms’ offices around the globe is such that US M&A activity into many non-G7 economies, including several relatively
fast growing developing economies, is double what would have otherwise occurred. This implies that the global spread of at least one US law firm has done much to bring additional pressure on (in particular publicly traded) firms in developing economies to improve the latters’ performance. In the course of my empirical analysis I also found that, after controlling for other factors, those nations with merger review procedures receive half the amount of US overseas M&A than nations without such procedures. Multi-jurisdictional merger review appears, then, to be a substantial constraint on the overseas expansion of US firms.

This paper is organized as follows. In the next section I summarize several aspects of the boom in global M&A activity in the mid-to-late 1990s, and the growth of US law firms’ overseas operations since 1985. In section three, the econometric strategy and data employed are described, as are the estimation results. A discussion of these findings, their potential policy relevance, and suggestions for future research, is presented in section four.

2. The late 1990s boom in cross-border mergers and acquisitions and the international expansion of US law firms

The 1990s saw a ten-fold increase in the value of cross-border mergers and acquisitions. According to OECD (2001), over a trillion US dollars of corporate assets were involved in cross-border M&A in the year 2000. Unlike the surge in
cross-border M&A in the late 1980s, the latest wave was not confined principally to transactions between British and American firms. Continental European, Japanese, Korean, Latin American, and South East Asian firms played significant roles in what has been termed by some as the first truly global wave of mergers and acquisitions (Black, 2000). Figure 1 provides evidence on the extent of US outward M&A activity, and shows that US purchases of corporate assets abroad trebled in real terms between 1995 and 1999.

Many factors are said to be responsible for this global wave of M&A. Deregulation and privatization (especially in the utilities sectors) are important explanations in Europe and in many developing economies (UNCTAD, 2000; OECD, 2001). Changes in corporate strategies, that emphasize both concentration on so-called core competencies and on attaining global reach, are also a contributing factor in manufacturing industries, in particular (OECD, 2001). And liberalization of foreign direct investment regimes has no doubt played a role in facilitating overseas acquisitions of corporate assets, as has the ease with which firms were able to raise funds cheaply on stockmarkets in the late 1990s.

These developments have, of course, not gone unnoticed by antitrust officials around the world. As Table 1 makes clear, an increasing share of overseas US M&A activity involved the acquisition of a majority controlling interest in foreign firms. In fact, in 1999 nearly two thirds of such M&A transactions involved acquiring such a controlling stake. To the extent that these transactions reduce
the number of competitors in a given market, antitrust officials may be concerned about the potential exercise of monopoly power by the remaining firms. This has undoubtedly contributed to an increase in the number of nations with active programs for merger notification or review. According to an advisory committee to the US government on international competition policy matters, by 2000 sixty jurisdictions had some form of mandatory merger notification scheme (ICPAC, 2000, Annex 2-C). Such schemes are often complemented by review procedures to assess the likely impact on a nation’s markets of a proposed or actual M&A transaction. In principle, therefore, a cross-border merger could be reviewed by many national antitrust authorities; and depending on the statutes governing these authorities’ actions, the latter can reject such a proposed merger outright or can demand divestitures or other commitments from the parties involved. In some countries, in particular those with federal constitutions such as the United States, sub-national antitrust authorities may add to the number of reviewing entities. One might suspect that the cumulative effect of these reviews is to erect a considerable barrier to international mergers and acquisitions, that is, to the international trade in corporate assets.

Multi-jurisdictional merger review has considerably expanded the demand for legal services on two accounts. First, firms seeking approval for their proposed M&A transactions need specialized counsel in (at least) each of the major jurisdictions, and need to coordinate their counsel’s responses so that any concessions (or agreements reached with antitrust authorities) do not jeopardize
the overall commercial viability of the transaction. Second, firms opposed to a rivals’ announced plans to merge or to acquire assets abroad can hire legal counsel to present evidence to antitrust authorities that casts the proposed transaction in a poor light. Again, such actions need to be coordinated so as to maximize the probability that leading antitrust authorities take steps to oppose enough components of a proposed deal that it is eventually abandoned. As noted earlier, the receptiveness of antitrust authorities to evidence presented by rivals varies considerably across jurisdictions and may be greater in jurisdictions with nascent or younger merger review procedures.

The supply side response to this increased demand for specialist antitrust counsel in many jurisdictions has included the formation of global law firms. Such firms almost always started out serving either the US or the British national market. As far as US law firms are concerned, Spar (1997) identifies two waves of overseas expansion: 1965-85 and after 1985. The first wave saw US law firms follow their multinational clients abroad. For example, Shearman & Sterling opened a Paris office in 1967 just as its client Citibank was expanding vigorously overseas. Spar argues that:

“Some of the US firms that went abroad matured past their initial clients, building sizeable independent practices in their new found locations. Most of them, though, did not, and left their overseas posts once their clients’ work was completed.” (Spar, 1997 page 13)

The second wave was, however, on a different scale and at the initiative of the law firms themselves. For example, Morrison & Forrester, a San-Francisco-
based US law firm, opened a practice in Hong Kong in 1982 without having a single client in the region (Spar, 1997). In this wave, supply tended to lead demand, as Spar notes:

“Once a few firms established sizeable international practices, they achieved a critical mass that made them attractive to multinational clients. Rather than asking multinationals to spread their legal advising among a number of far flung firms, multinational law firms could offer coordinated and consolidated service.” (Spar, 1997 page 14)

These large global law firms were in place well before the global merger wave took off in the late 1990s. By 1989, the 250 largest US law firms had 180 overseas offices (Spar, 1997). This growth continued through the 1990s. A recent analysis revealed that in 1997 the top 100 US law firms had 363 overseas offices employing 4214 lawyers (Beaverstock, Smith, and Taylor, 2000). One firm alone, Baker & McKenzie, accounted for 1802 of these lawyers and had 48 overseas offices, far exceeding (on these metrics) the global reach of any rival law firm.²

While accepting the argument that the overseas offices of US law firms have been established to supply a wide range of services, meeting clients needs for advice on mergers and acquisitions has been a prominent rationale for overseas expansion. For example, the law firms of Coudert Brothers; Shearman & Sterling; Jones, Day, Reavis & Pogue; Kaye, Scholer, Fierman, Hays & Handler; and

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² For an account of the growth of Baker & McKenzie see Bauman (1999).
White & Case are said to have established offices in China during 1993-2000 with mergers and acquisitions stated as important practice areas.³

To summarize some of the main arguments of this section: Global legal networks expanded before the latest wave of cross-border M&A. The presence of a man-made impediment to trade in corporate assets—merger review procedures—provides these networks with a means to hamper or to facilitate cross-border M&A, and distinguishes these networks from the existing literature on business networks which emphasizes the latter’s role in promoting international trade in goods and services. The remainder of this paper is devoted to examining whether there is any empirical evidence that the global footprint of several leading US law firms facilitated or reduced US overseas M&A activity in 1999, a year when the wave of global M&A was in full swing.

3. Econometric strategy and data employed

Given that many factors can influence the amount of US cross-border M&A received by a foreign country, one objective must be to adequately control for these factors and to examine how much of the remaining variation can be attributed to the presence of global legal networks. The first step taken was to assemble the largest possible dataset of economies which had received US cross-border M&A in 1999. Several financial companies track announcements of

proposed (and completed) US cross-border M&A, and here I used the data reported in the 2000 Mergerstat Review. This source reports that 52 overseas economies and territories received US cross-border M&A in 1999, with a total value of such transactions equaling $173.5 billion. Three smaller territories (Bermuda, St. Kitts and Nevis, and Puerto Rico) were excluded from the dataset assembled here because they were in fact either U.S. territories or where the reported M&A data may well be misreported financial transfers (with no corporate assets changing hands.)

I have modified the traditional gravity equation approach to estimating the determinants of international trade flows to quantify the factors responsible for US cross-border M&A in 1999. The gravity equation approach assumes that the value of the economic transactions between two entities depends on their economic mass and the distance between them (Anderson, 1979, Deardorff, 1998, and Evenett and Keller, forthcoming.) In the present context, this amounts to assuming that the distance between a foreign nation and the United States and the former’s national income are candidate determinants of the total value of US cross-border M&A received by that nation. The intuition is that a larger

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4 Eliminating these three territories leaves 49 economies in my dataset. The 49 economies are: Argentina, Australia, Austria, Bahrain, Belgium, Brazil, Canada, Chile, China, Costa Rica, the Czech Republic, Denmark, the Dominican Republic, Egypt, El Salvador, Finland, France, Germany, Ghana, Hong Kong PRC, Hungary, India, Indonesia, Ireland, Israel, Italy, Japan, Lithuania, Malaysia, Mexico, Netherlands, New Zealand, Norway, Pakistan, Peru, Philippines, Poland, Portugal, Romania, Singapore, South Africa, South Korea, Spain, Sweden, Switzerland, Taiwan, Thailand, and Venezuela.

5 Strictly speaking the gravity equation approach suggests that the level of US national income is a determinant too of the value of outward US cross-border M&A. However, the fact that my dataset contains information on such cross-border M&A transactions for one year (1999) means that the level of US national income cannot account for the variation in the value of M&A received
foreign market provides, other things being equal, greater opportunities for the US acquisition of foreign corporate assets; and that greater distance from the United States makes running a foreign subsidiary or acquisition more difficult and detracts from the desirability of buying or merging with that nation’s corporate assets. Data on the 49 economies’ gross domestic products was taken from the World Bank’s *World Development Indicators* CD-ROM. Following standard practice, the distance from Washington, D.C., to the administrative capital of each economy was used as the proxy for distance from the United States.

Three other control variables were employed. The first is a proxy for the retained corporate profit rate (that is, the proportion of its profits a firm can expect to keep after paying taxes and other government-assessed fees and levies.) Economies which have higher retained profit rates are hypothesized to be more desirable places to undertake cross-border M&A. I proxy for this rate with one minus the maximum corporate tax rate charged in an economy, data on which is available in the *World Development Indicators* database. The second control variable is the foreign economy’s tariff rate. The logic here is that higher tariffs reduce the profitability of exporting to an economy and enhance the attractiveness of establishing local subsidiaries. However, an alternative hypothesis is that national tariff rates proxy for the degree of policy-induced *internal* and external distortions to an economy, and to the extent that such internal distortions reduce the profitability of firms, this will discourage cross-border M&A. I took the average

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across different foreign economies. Consequently, I do not include US national income as an explanatory variable in my econometric analysis.
tariff rate as the proxy for the restrictiveness of a nation’s trade barriers, data which is also available on the *World Development Indicators* CD-ROM. The final control variable is whether an economy has a British colonial heritage. This is thought to be important for two reasons. First, in such economies English is more likely to be the language of business, making it easier for a US firm to run any firm it might acquire in these locales. Second, the likelihood that an economy employs a common law system is greater with if it was at some point a British colony—and this is precisely the system that operates in the United States and is familiar to US lawyers. Both conjectures suggest that having a British colonial heritage will raise the amount of US cross-border M&A. A dummy variable is introduced to capture this effect (taking the value of one if the economy has such a heritage.)

The first antitrust-related variable employed in the empirical analysis is whether the foreign economy has a merger notification scheme or merger review procedure. As argued in the last section, such schemes and reviews are likely to reduce the amount of cross-border M&A, especially for larger transactions. Although merger notification regimes and review procedures vary considerably across nations, I employ a dummy variable to indicate whether a nation has such a regime or not. The list of economies taken to have such regimes in 1999 was assembled from ICPAC (2000, Annex 2-C) and from evidence on the web pages of the U.S. Department of Justice’s Antitrust Division and the Competition Directorate-General of the European Commission. In our sample of 49
economies, the following were found not to have some form of merger review regime in 1999: Ghana, Pakistan, Egypt, El Salvador, China, Indonesia, Malaysia, the Dominican Republic, Singapore, and Hong Kong PRC.

Before describing the first econometric specification employed it will be helpful to introduce the following notation:

- **MA<sub>i</sub>**: Denotes the total value of US cross-border M&A into economy<i>i</i> in 1999.
- **ma<sub>i</sub>**: Denotes the mean value of US cross-border M&A transactions in economy<i>i</i> in 1999.
- **GDP<sub>i</sub>**: Denotes the value of gross domestic product of economy<i>i</i> in 1999, measured in US dollars.
- **DIST<sub>i</sub>**: Denotes the distance of economy<i>i</i>’s capital from the Washington, D.C., in kilometers.
- **π<sub>i</sub>**: Denotes the retained corporate profit rate in economy<i>i</i>.
- **(1+t<sub>i</sub>)**: Denotes one plus economy<i>i</i>’s average tariff rate on imported goods.
- **BRIT<sub>i</sub>**: Denotes a dummy variable which equals one if economy<i>i</i> has a British colonial heritage.
- **MN<sub>i</sub>**: Denotes a dummy variable which equals one if economy<i>i</i> has a mandatory merger notification regime or a merger review procedure in 1999.
- **e<sub>i</sub>**: Denotes a random error term, assumed to have zero mean and finite variance.
- **c**: Denotes a constant.

The first two specifications estimated were:

\[
\ln(MA_i) = c + \beta_1 \ln(GDP_i) + \beta_2 \ln(DIST_i) + \beta_3 \ln{\pi_i} + \beta_4 \ln(1 + t_i) + \beta_5 BRIT_i + \beta_6 MN_i + e_i
\]
\[
\ln(ma_i) = c + \beta_1 \ln(GDP_i) + \beta_2 \ln(DIST_i) + \beta_3 \ln{\pi_i} + \beta_4 \ln(1 + t_i) + \beta_5 BRIT_i + \beta_6 MN_i + e_i
\]

where \(\ln(\ldots)\) are natural logarithms and \(\beta_1, \ldots, \beta_6\) are parameters to be estimated.

The first specification takes the total value of US cross-border M&A as the
dependent variable, and the second specification takes the mean value of US cross-border M&A transactions as the dependent variable. Concerns about heteroskedacity, which are common in cross-sectional samples like the one used here, resulted in a two step estimation procedure being employed. In the first step, each specification was estimated using ordinary least squares and the absolute value of the regression residuals $|e_i|$ were recovered. The latter were used to weight each observation and the specifications were re-estimated. The full set of parameter estimates and their associated p-values are reported in Table 2 in for the regression with the total value of M&A activity as the dependent variable, and in Table 3 for the specification where the mean value of M&A transactions was the dependent variable.

Examining the two tables it is clear that the controls have, almost always, their expected signs. Richer economies that are closer to the United States, which have lower corporate tax rates and a British colonial heritage, tend to attract more US M&A. The large negative estimated parameter on the tariff terms suggests that they are indeed proxying for the extent of internal as well as external distortions to an economy and, on net, repel US M&A. As these control variables have little bearing on the main question at hand, and because their estimated parameters do not vary much across the specifications discussed below, I shall not discuss them further. In specification 1, the presence of a merger notification regime does not appear to influence the total value and mean value of US cross-border M&A. I will return to this finding later.
To examine the effect of US legal networks on US cross-border M&A in 1999, I made use of Beaverstock, Smith, and Taylor’s (2000) detailed dataset on the overseas presence of the largest 100 US law firms in 1997. Their database indicates that there were 4066 lawyers working overseas for these law firms in the 49 economies in my sample. Further analysis revealed that 60 percent of those lawyers worked for just six US law firms: Skadden, Arps, Slate, Meagher & Flom; Jones, Day, Reavis & Pogue; Shearman & Sterling; Coudert Brothers; White & Case; and Baker & McKenzie (see Table 4.) Again, the scale of Baker & McKenzie’s overseas operations is apparent—this US law firm operates in 30 of the 49 economies in my sample and employs 1743 lawyers (see Table 4 and Figure 2). For the purposes of exposition I refer to these six US law firms as the “Big 6” firms, and the goal of the remaining empirical analysis is to estimate what the contribution to an economy’s receipt of US cross-border M&A is due to the presence of these six legal networks within its jurisdiction.

It is important to differentiate between the presence of these six law firms and the number of lawyers employed by US firms in a foreign economy. Although there may be a positive correlation between the former and the latter, the latter may not be a good proxy for the former as many lawyers may be hired by smaller US law firms that do not have the global footprint of the Big Six. To sort out the independent contribution of the Big Six, I proceeded as follows. First, I computed the total number of lawyers hired by US firms in each of the 49 economies in my
sample, and the number of Big Six firms that had offices with over 10 lawyers in any given economy. (Requiring that there be 10 or more lawyers hopefully rules our smaller overseas offices which are unlikely to have sizeable M&A practice areas.\textsuperscript{6}) Specifications 2 and 3 in Table 2 and 3 report the parameter estimates when the (natural logarithm) of the number of US lawyers and the number of Big Six firms are included as independent variables. And consistent with the hypothesis that the effect of such lawyers and legal networks on cross-border M&A is only due to the presence of merger notification requirements and review procedures, I interact these two new independent variables with the dummy variable indicating the presence of a merger notification regime (MN\textsubscript{i}). Including the number of Big Six firms causes the estimated parameter on the number of US lawyers to turn negative and statistically significant (at the 10 percent level)—suggesting that the net effect of having more lawyers employed by US firms in a foreign economy is to reduce the sale of that economies’ commercial assets to American corporations. As both tables makes clear, the number of Big Six firms in an economy does not appear to influence (in a statistically significant manner) either the total value or the mean value of US cross-border M&A.

One objection to specification 3, which included both the number of US lawyers and Big Six firms as independent variables, is that the former is likely to be larger in precisely those economies where the Big Six firms are present. And so the independent variable for the number of US lawyers may well be absorbing some

\textsuperscript{6} I relaxed this requirement to five lawyers with no substantial bearing on the estimated results or qualitative findings.
of the explanatory power of the variable measuring the number of Big Six firms present. To address this problem, I purged the former variable of any variation accounted for by the latter, effectively creating an instrument for the number of US lawyers in an economy that is, by construction, orthogonal to the number of Big Six legal firms. Specification 4 reports the parameter estimates which result from doing so. Interestingly, the number of US lawyers still has a negative and statistically significant effect on the amount of US cross-border M&A received. The number of the Big Six law firms in an economy is found to depress the mean value of cross-border M&A but not the total value of such M&A—suggesting that these firms are successful in blocking larger cross-border M&A transactions (or deterring their announcement in the first place) and in facilitating the approval of smaller transactions. Another interesting finding in specification 4 is that—once one starts to control adequately for the presence of US lawyers and law firms overseas—the estimated coefficient for the presence of a merger notification regime turns negative (but is not statistically significant at any recognized level.)

Given the difference in scale of Baker & McKenzie’s global network from the other members of the Big Six, a question arises as to whether the effect of the former’s network differs from that of the other five networks that I have identified. To investigate this I then dropped the number of Big Six firms as an independent variable, and included a separate dummy variable for the presence of a Baker & McKenzie office in an economy (again with 10 or more lawyers) and an
independent variable for the number of the other Big Six firms in an economy. The results are reported as specification 5 in Tables 2 and 3. Interestingly, the controlling for the presence of these different legal networks also produces—for the first time in this study—negative and statistically significant estimates of the effects of merger notification schemes on US cross-border M&A. The relevant parameter estimate in Table 2 implies that national merger review schemes and procedures tend to cut inflows of US cross-border M&A in half—a sizeable reduction, which suggests that merger enforcement around the world had reached the point in 1999 whereby it acted as a substantial constraint on the overseas expansion plans of US corporations.

Another way to gauge the restrictive effect of national merger review procedure is to consider what changes in the control variables would reduce US cross-border M&A by the same amount—that is, by approximately 50 percent. According to the estimates in Specification 5 in Table 2, an equivalent reduction in inward US M&A would require either a 49 per cent reduction in the recipient nation’s GDP, or an increase in the corporate tax rate from 30 percent to 37 percent, or an across-the-border increase in national tariffs of 3.5 percent. In other words, one would have to see some large changes in the fundamental determinants of

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7 One alternative approach I considered was to include separate dummy variables for the presence of each of the Big Six firms. It turns out that there is significant collinearity between the dummy variables for the five smaller members of the Big Six, which means the estimated effect for each dummy variable would have been identified off at most a handful of countries—a highly unsatisfactory basis upon which to make inferences.

8 In my sample of 49 economies the mean corporate tax rate was 30.5 percent.

9 For comparison’s sake, the Uruguay Round of trade negotiations resulted in cut tariffs by industrial economies on manufactured goods by 2.1 percent.
cross-border M&A to compensate for the introduction of a merger review procedure.

The inclusion of these two network terms in specification 5 does suggest that these global legal networks significantly affect the extent of US cross-border M&A. It appears that having a large Baker & McKenzie office in a country substantially boosts the total value of US cross-border M&A in that country, and goes a long way (if not entirely) to offset the effect of the presence of the other Big Six firms. The regression results imply that the incremental effect in an economy of establishing an additional office from the five smaller Big Six firms is to reduce the inflow of US cross-border M&A received by 32 percent. One interpretation of this finding is that a principal component of the smaller Big Six firms’ global strategies has been to earn their spurs by frustrating the overseas expansion plans of the rivals to their US corporate clients. An alternative explanation is that in order to sustain their large overseas offices, these US firms have begun to defend local firms against takeovers by US corporations. In unreported results, these findings appear to be robust for other corrections for heteroskedasticity and to sample composition (outliers.)

A better sense of the net effect of these six legal networks on US cross-border M&A can be found in Table 5. Using the estimated parameters in specification 5, and taking account of the appropriate covariances, I recovered the combined effect on each economy’s receipt of US cross-border M&A of the presence of all
six legal networks. At the 10 percent level (with one tailed tests), I found that all of the statistically significant estimates are positive—suggesting that on net these networks grease international transactions in corporate assets. What is more, the effects to be particularly pronounced in non-G7 economies, including developing economies such as Brazil, Chile, Hungary, the Philippines, Thailand, and Venezuela—and reflects the fact that such nations have Baker & McKenzie offices and few (or no) large offices from the other Big Six firms. To the extent that such overseas M&A brings pressure to improve performance on domestic firms in these economies, then this may well be a positive development. Of course, to the extent that such M&A reduces competition in those nations’ markets then the effects may not be so benign.

4. Summary and implications for future research

Much of the existing literature on the effects of networks on trade has emphasized the trade-facilitating aspects of network formation. In this paper I have considered the growth of legal networks where a proiri one cannot be certain that their spread has greased the wheel of one prominent form of international commerce, cross-border mergers and acquisitions. The existence of merger notification requirements and merger reviews provides law firms with an opportunity to present evidence that might go some way to convince antitrust authorities to oppose or demand changes to a transaction proposed by a rival to

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10 And, incidentally, would reinforce the case for liberalizing any restrictions on the entry of foreign legal firms.
the law firms’ US clients. I have presented evidence to suggest that for five US law firms with sizeable global reach this is, on net, exactly the consequence of their overseas operations.

This paper’s findings may have some implications for ongoing discussions between government officials, practitioners, and academics on international competition policy. The estimated parameters in specification 5, where I examined the differential effects of the Big Six firm’s global networks and which is the specification that—in my view—best addresses the questions raised in this paper, suggest that national merger review regimes around the globe have now developed to such an extent that they have considerable bite. Specifically, my results imply that such regimes cut the total value of US overseas M&A in half. In the light of these results, one has to wonder whether the independent exercise of merger review by multiple jurisdictions is best serving US overseas commercial interests. Indeed, could it be the case that some US overseas M&A deals are being abandoned (or not even proposed in the first place) even when the anticipated adverse effects in a small number of jurisdictions are more than compensated by benefits—generated perhaps by efficiencies—in other jurisdictions? The lack of any formal or informal mechanism to balance the gains in one jurisdiction against losses in others could in part account for the large estimated effects of national merger regimes on overseas US M&A reported here. Given that national authorities are likely to vigorously guard their prerogatives and the current lack of sympathy towards creating such cross-
jurisdictional mechanisms, the large M&A-reducing effects of national merger reviews found here suggest that—at a minimum—a thorough discussion of the appropriate substantive standards for merger reviews seems all the more urgent.

There are a number of important caveats to my analysis which should be borne in mind when interpreting these results. First, I am dissatisfied with the use of a single dummy variable to estimate the effects of merger reviews and notification procedures. Obviously these procedures differ across economies and, in future research, it would be desirable to explore which attributes of such reviews have the greatest effect on cross-border M&A. Second, given that not every overseas office (even those with 10 or more lawyers) of a US law firm is likely to be engaged in advising clients on cross-border M&A, my measure of each of the Big Six’s global reach could probably be improved upon. Third, the cross-sectional analysis presented does not shed any light on how the impact of these global legal networks has changed over time—a deficiency that too could be remedied by future research. Finally, it is worth reiterating that there is no clear relationship between the value of US M&A that a nation receives and its economic well-being. As discussed at the end of the last section, cross-border M&A can enhance or worsen the allocation of a nation’s resources. The goal of this paper was, however, far more modest—to examine the positive (rather than normative) impact of the presence of six large US legal networks.
References


Figure 1: US overseas M&A transactions 1985-1999

![Graph showing billions of US dollars (constant 1999 US dollars) for each year from 1985 to 1999.](image)

Figure 2: The Big 6 law firms dominate overseas activities by US law firms, measured by number of lawyers in 1998

![Pie chart showing the distribution of lawyers among Big 6 and non-Big 6 firms.](image)
Table 1: Types of U.S. overseas mergers and acquisitions

<table>
<thead>
<tr>
<th>Year</th>
<th>Acquisition of controlling interests</th>
<th>Acquisition of minority interests</th>
<th>Divestitures of foreign-based units</th>
<th>Diverstitures of US-based units</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>128</td>
<td>23</td>
<td>57</td>
<td>58</td>
<td>266</td>
</tr>
<tr>
<td>1995</td>
<td>254</td>
<td>54</td>
<td>94</td>
<td>81</td>
<td>483</td>
</tr>
<tr>
<td>1999</td>
<td>882</td>
<td>48</td>
<td>309</td>
<td>159</td>
<td>1398</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of deals</th>
<th>Percentage of deals</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>100.0</td>
<td>48.1 8.6 21.4 21.8</td>
</tr>
<tr>
<td>1995</td>
<td>100.0</td>
<td>52.6 11.2 19.5 16.8</td>
</tr>
<tr>
<td>1999</td>
<td>100.0</td>
<td>63.1 3.4 22.1 11.4</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Independent variable</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Constant</td>
<td>?</td>
<td>0.151</td>
<td>0.460</td>
<td>0.155</td>
<td>0.436</td>
</tr>
<tr>
<td>National Income</td>
<td>+</td>
<td>1.023</td>
<td>0.000</td>
<td>1.023</td>
<td>0.000</td>
</tr>
<tr>
<td>Distance from U.S.</td>
<td>-</td>
<td>-0.424</td>
<td>0.000</td>
<td>-0.477</td>
<td>0.000</td>
</tr>
<tr>
<td>Retained profit rate</td>
<td>+</td>
<td>5.292</td>
<td>0.000</td>
<td>5.250</td>
<td>0.000</td>
</tr>
<tr>
<td>Tariff rate</td>
<td>?</td>
<td>-13.142</td>
<td>0.000</td>
<td>-13.630</td>
<td>0.000</td>
</tr>
<tr>
<td>British colonial heritage</td>
<td>+</td>
<td>1.681</td>
<td>0.000</td>
<td>1.638</td>
<td>0.000</td>
</tr>
<tr>
<td>Merger notification regime</td>
<td>-</td>
<td>-0.025</td>
<td>0.758</td>
<td>0.044</td>
<td>0.686</td>
</tr>
<tr>
<td>Number of lawyers in US legal firms</td>
<td>?</td>
<td>0.039</td>
<td>0.123</td>
<td>-0.137</td>
<td>0.060</td>
</tr>
<tr>
<td>Number of Big Six US law firms</td>
<td>?</td>
<td></td>
<td>0.204</td>
<td>0.578</td>
<td>0.047</td>
</tr>
<tr>
<td>Instrument for number of lawyers in US legal firms</td>
<td>?</td>
<td></td>
<td></td>
<td>-0.137</td>
<td>0.060</td>
</tr>
<tr>
<td>Presence of Baker &amp; McKenzie</td>
<td>?</td>
<td></td>
<td></td>
<td></td>
<td>1.601</td>
</tr>
<tr>
<td>Number of Big Six US law firms, other than Baker &amp; McKenzie</td>
<td>?</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>R-squared</td>
<td>0.752</td>
<td>0.750</td>
<td>0.742</td>
<td>0.742</td>
<td>0.723</td>
</tr>
</tbody>
</table>
### Table 3: Estimation results when mean value of bilateral U.S. M&A transactions is the dependent variable.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>?</td>
<td>0.52 0.137</td>
<td>0.383 0.101</td>
<td>0.307 0.200</td>
<td>0.307 0.200</td>
</tr>
<tr>
<td>National Income</td>
<td>+</td>
<td>0.706 0.000</td>
<td>0.792 0.000</td>
<td>0.792 0.000</td>
<td>0.792 0.000</td>
</tr>
<tr>
<td>Distance from U.S.</td>
<td>-</td>
<td>0.150 0.052</td>
<td>0.034 0.656</td>
<td>0.073 0.371</td>
<td>0.073 0.371</td>
</tr>
<tr>
<td>Retained profit rate</td>
<td>+</td>
<td>3.324 0.016</td>
<td>3.838 0.000</td>
<td>4.501 0.000</td>
<td>4.501 0.000</td>
</tr>
<tr>
<td>Tariff rate</td>
<td>?</td>
<td>-5.292 0.000</td>
<td>-9.588 0.000</td>
<td>-9.783 0.000</td>
<td>-9.783 0.000</td>
</tr>
<tr>
<td>British colonial heritage</td>
<td>+</td>
<td>0.623 0.000</td>
<td>0.662 0.000</td>
<td>0.708 0.000</td>
<td>0.708 0.000</td>
</tr>
<tr>
<td>Merger notification regime</td>
<td>-</td>
<td>0.190 0.527</td>
<td>-0.025 0.896</td>
<td>-0.087 0.696</td>
<td>-0.337 0.114</td>
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<tr>
<td>Number of lawyers in US legal firms</td>
<td>?</td>
<td>-0.172 0.000</td>
<td>-0.157 0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of Big Six US law firms</td>
<td>?</td>
<td>-0.046 0.230</td>
<td>-0.226 0.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Instrument for number of lawyers in US legal firms</td>
<td>?</td>
<td>-0.157 0.000</td>
<td>-0.474 0.011</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Presence of Baker &amp; McKenzie</td>
<td>?</td>
<td>0.806 0.154</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of Big Six US law firms, other than Baker &amp; McKenzie</td>
<td>?</td>
<td>-0.459 0.002</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>R-squared</td>
<td>0.942</td>
<td>0.810</td>
<td>0.801</td>
<td>0.801</td>
<td>0.803</td>
</tr>
</tbody>
</table>
Table 4: The Big Six US law firms in the sample

<table>
<thead>
<tr>
<th>Big 6 US law firm</th>
<th>Total number of lawyers based in overseas offices</th>
<th>Total number of overseas offices</th>
<th>Number of overseas offices with…</th>
<th>Overseas offices in…</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>0-4 lawyers</td>
<td>5-9 lawyers</td>
</tr>
<tr>
<td>Skadden, Arps, Slate, Meagher &amp; Flom</td>
<td>93</td>
<td>12</td>
<td>5</td>
<td>4</td>
</tr>
<tr>
<td>Jones, Day, Reavis &amp; Pogue</td>
<td>94</td>
<td>9</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td>Shearman &amp; Sterling</td>
<td>133</td>
<td>8</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Coudert Brothers</td>
<td>158</td>
<td>11</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td>White &amp; Case</td>
<td>203</td>
<td>12</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Baker &amp; McKenzie</td>
<td>1743</td>
<td>30</td>
<td>0</td>
<td>1</td>
</tr>
</tbody>
</table>

**Table 5: Implied combined effects of all six legal firm networks on cross-border M&A**

Parameter estimates from specification 5 in Tables 2 and 3 were used to calculate these forecasts.

<table>
<thead>
<tr>
<th>Economy</th>
<th>Change in mean value of bilateral US cross-border M&amp;A</th>
<th>Change in total value of bilateral US cross-border M&amp;A</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Implied percentage change</td>
<td>Point estimate</td>
</tr>
<tr>
<td>France</td>
<td>-77.472</td>
<td>-1.490</td>
</tr>
<tr>
<td>UK</td>
<td>-77.472</td>
<td>-1.490</td>
</tr>
<tr>
<td>Belgium</td>
<td>-10.640</td>
<td>-0.113</td>
</tr>
<tr>
<td>Germany</td>
<td>-10.640</td>
<td>-0.113</td>
</tr>
<tr>
<td>Japan</td>
<td>41.453</td>
<td>0.347</td>
</tr>
<tr>
<td>Mexico</td>
<td>41.453</td>
<td>0.347</td>
</tr>
<tr>
<td>Poland</td>
<td>41.453</td>
<td>0.347</td>
</tr>
<tr>
<td>Taiwan</td>
<td>41.453</td>
<td>0.347</td>
</tr>
<tr>
<td>Argentina</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Australia</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Brazil</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Canada</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Chile</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Hungary</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Italy</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Netherlands</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Philippines</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Spain</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Sweden</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Switzerland</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Thailand</td>
<td>123.916</td>
<td>0.806</td>
</tr>
<tr>
<td>Venezuela</td>
<td>123.916</td>
<td>0.806</td>
</tr>
</tbody>
</table>

- Implies estimate is positive and statistically significant (at 10 percent level, one tail test)
- Implies estimate is negative
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Malaysia).


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