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TROIS ESSAIS SUR LA CORRUPTION

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RÉSUMÉ

La corruption est l'un des plus anciens problèmes de l'humanité. Elle a des effets dans de nombreux domaines tels que politique, économique, social et environnemental. Se définissant comme un détournement du pouvoir public à des fins de profits privés, elle est l'un des plus sérieux problèmes auxquels font face les pays en voie de développement, mais constitue aussi un défi pour les pays développés. La lutte contre la corruption a suscité une attention considérable au cours de la décennie passée, et des organisations internationales comme l'ONU, le FMI et l'OCDE ont démontré un intérêt particulier pour les mouvements anticorruptions. Le bon sens voit la corruption comme une entrave à la croissance, au développement et surtout à l'investissement. La littérature qui examine les conséquences de la corruption soutient ce point de vue et associe de manière empirique un haut niveau de corruption dans le pays hôte à une croissance économique lente ainsi qu'à de faibles afflux d'investissement. Pour les investisseurs étrangers, la corruption agit comme une barrière au marché et augmente les coûts d'entrée dans un pays. Cette thèse a pour but d'étudier la relation entre corruption et investissement sous trois perspectives différentes.

L'essai 1 cherche le lien entre l'activité de Fusions et Acquisitions (F&A) et le niveau de corruption dans le pays hôte. J'émets l'hypothèse selon laquelle une activité transfrontalière de F&A plus élevée peut accroître la concurrence et introduire de nouvelles normes et politiques qui peuvent à tour de rôle réduire le niveau de corruption du pays hôte. L'analyse empirique soutient ces hypothèses.

L'essai 2 analyse les effets de la distance de corruption sur l'activité de F&A. Les compagnies de pays ayant un faible niveau de corruption n'ont aucune expérience dans la gestion de la corruption et sont donc réticentes à investir dans un pays corrompu. Or, l'exposition à la corruption domestique prépare les compagnies à faire face à la corruption à l'étranger. Par conséquent, les compagnies préfèrent investir dans des pays ayant un niveau de corruption similaire au leur. Ces hypothèses sont appuyées de manière empirique dans l'essai.

L'essai 3 examine l'effet de perception de la corruption par les médias américains sur les investissements directs à l'étranger (IDE) des États-Unis. Les médias américains rapportent des faits sur la corruption dans d'autres pays. Cet essai étudie l'effet de tels faits négatifs sur le niveau d'IDE américain en direction ces pays et constate que la

perception de la corruption par les médias est un déterminant important de l'IDE sortant des États-Unis.
Cette thèse peut apporter un nouveau regard sur notre compréhension de la relation entre la corruption et l'investissement étranger.
Mots clés : Corruption, investissement, fusions et acquisitions, l'investissement direct à l'étranger, média, intégrité financière.

ABSTRACT

Corruption is one of humanity's most ancient problems. Corruption has effects on many different domains such as the political, economic, social and environmental spheres. Defined as the misuse of public power for private gains, corruption is one of the most serious problems faced by developing countries but is also a challenge for many developed countries. The fight against corruption has raised considerable attention in the last decade, and international organizations such as the UN, the IMF and the OECD have taken a special interest in anti-corruption movements. Common sense views corruption as an impediment to growth, development and, more importantly, investment. The literature that investigates the consequences of corruption supports this point of view and empirically associates high levels of host-country corruption with slow economic growth and low investment inflows. For foreign investors, corruption acts as a market barrier to entry and increases the costs of entering a country. This thesis aims to study the mutual relationship between corruption and investment from three different perspectives.

Essay one investigates the link between Mergers and Acquisitions (M&A) activity and the level of corruption in the host country. I hypothesize that higher cross-border M&A activity can increase competition and introduce new norms and policies, which in turn can reduce the host country's level of corruption. Empirical analysis supports the hypotheses.

Essay two analyzes the effects of corruption distance on M&A activity. Companies from low corruption countries have no experience in dealing with corruption, so they are reluctant to invest in a corrupt country. However, exposure to corruption at home provides a learning experience preparing the companies to handle corruption abroad. Therefore, companies prefer to invest in similarly corrupt countries. The hypotheses are empirically supported in the Essay.

Essay three examines the effects of media corruption perceptions (MCP) on US foreign direct investment (FDI) outflows. The US media cover many stories about corruption in other countries. This essay studies the effects of such negative stories on the level of US FDI outflow towards these countries and finds that MCP is a strong determinant of US outward FDI.

This thesis aims to shed new light on our understanding of the relationship between corruption and foreign investment.

Keywords: Corruption, investment, mergers and acquisitions, foreign direct investment, media, financial integrity.

GENERAL INTRODUCTION

Corruption is one of the most ancient problems of mankind. Corruption has effects on many different domains such as the political, economic, social and environmental spheres. In the political scope, corruption hinders democracy and the rule of law because public institutions and offices may lose their legitimacy. Corruption may also reduce political stability, political competition, and the transparency of political decision making. In the social sphere, corruption discourages people from working together for the common good and the request for and payment of bribes becomes a social norm. Corruption increases poverty, results in social inequality, and widens the gap between the rich and the poor, which leads to a weak civil society. The economic effects of corruption are even harsher. Corruption leads to the depletion of national wealth. Scarce public resources are squandered on high profile projects, while much needed projects such as schools, hospitals and roads, or the supply of potable water remains unfunded. In such environments, public wealth is converted to private and personal property, inflation is high, and unhealthy competition prevails.

In the perspective of finance, corruption is defined as the misuse of public power for private gains. It is an impediment to growth, economic development and, more importantly, investment. The literature on corruption empirically supports the detrimental effects of corruption on both investment and growth at the macro level (Mauro, 1995; Meon & Sekkat, 2005; Wei, 2000). This body of literature predicts that higher corruption levels lead to lower rates of growth and investment. Mauro (1995) observed a significant negative relationship between corruption and

investment that extended to growth. Brunetti and Weder (1998) and Mo (2001) confirmed Mauro's findings. Drabek and Payne (2002) argued that corruption has a detrimental effect on FDI attractiveness. Rock and Bonnett (2004) argue that corruption reduces investment in most developing countries and particularly in small open economies. This body of evidence proposes that corruption is harmful to economic growth, foreign investment, and the development of a country. As a result, the fight against corruption is a high priority for international organizations such as the IMF, the World Bank, the UN and the OECD.

The first paper that examines the link between corruption and investment is Mauro (1995), which reports empirical evidence for a negative correlation between corruption and the ratio of inward investment to gross domestic product (GDP) in a cross-section of 57 countries. Several consequent studies broaden his results and focus on the effects of host country corruption on investment and find that corruption is a deterrent to inward foreign direct investment (Hines, 1995; Henisz, 2000; Wei, 2000; Habib and Zurawicki, 2002). Habib and Zurawicki (2001) examine data on local and foreign direct investments (FDI) in 111 countries during 1994 to 1998 and find that host country corruption has more of a negative impact on foreign investments compared with local ones. According to them, local direct investment seems to be substantially (about 2 times) less affected by corruption than foreign direct investment.

FDI is defined as an investment involving a long-term relationship and reflecting a long-term interest and control of a resident entity in an economy other than that of the investor. Mergers and acquisitions, green-field investments, equity investments, etc. are all types of FDI. Grosse and Trevino (1996) and Chen and Chen (1998) classify the determinants of cross-border FDI into three categories: (1) firm-specific factors, (2) location-specific factors, and (3) measures of the relationship between the source

and host countries. Location factors such as market size, borrowing costs, unit labour costs, and institutional and political stability are critical for the firm's investment decision. Corruption is determined by a country's institutional and political environment, thus high levels of corruption reduce locational attractiveness and have a negative impact on investors' decision to invest. Habib and Zurawicki (2002) state that "....[bribe] payments to the host country officials do not have a market value and, hence, raise the cost of goods when compared to a competitive market. This can be a major disincentive for foreign investors" (p. 293). A distinctive feature of corruption is its "lock-in" effect. Once in the game, it is very difficult to get out of it. Firms opening their doors for corruption may find it difficult to resist demands for bribery payments in the future (Rose-Ackerman, 1999). Additionally, firms with a reputation for bribing are more likely to receive demands for higher bribe payments by corrupt officials, sometimes even for the services that are normally offered for free. Moreover, the threat of mutual denunciation ties the partners to each other even after the bribery transaction. This constant engagement in corrupt actions raises the barriers to entry and exit of corrupt markets for foreign investors. Host country corruption also raises the cost of a firm's foreign investment, since (1) firms are expected to pay bribes. Wei (2000) suggests that severe corruption has an effect similar to increasing the host country tax rate; (2) they are engaged in resource-wasting, rent-seeking activities (Murphy et al., 1991; Shleifer and Vishny, 1993); and (3) they have to accept additional contract-related risks, because corruption contracts are not enforceable in courts (Boycko et al., 1995). Likewise, Javorcik and Wei (2009) investigate the effects of host country corruption on FDI inflows and show that corruption increases the advantages of having a local partner to navigate bureaucratic issues. However, these advantages come at the cost of reducing the effective protection of a multinational firm's intangible assets. Also, corruption reduces the productivity of public inputs (e.g., infrastructure) which, in turn, decreases a country's locational attractiveness (Bardhan, 1997; Rose-Ackermann, 1999; Lambsdorff, 2003). Therefore, corruption in the host country increases the cost

of entry and acts as a barrier, reducing firm profits and therefore lowering a firm's incentives to invest in the corrupt country.

This thesis aims to study the link between foreign investment and corruption in three essays, each from a different perspective.

Essay one investigates the effects of investment on corruption. Although corruption has a negative impact on foreign investment, the opposite causality also holds. Foreign investment can also influence corruption. Many studies scrutinize the effects of FDI on host country corruption (Gerring and Thacker, 2005; Larrain and Tavares, 2004; Sandholtz and Gray, 2003) and find that higher FDI inflows to a country can reduce the overall corruption level. However, no study has studied the link between Mergers and Acquisitions (M&A) and corruption. M&A is the primary mode of internationalization and the pillar of FDI. Contrary to FDI, M&A can have a strong influence on the market environment of the host country; can bring new norms and policies; and can increase competition. Thus, they can reduce the national level of corruption. Essay one is the first study to examine the effects of M&A on the corruption level of the host country. A panel data framework in a cross-section of 50 countries is used to measure the effects of country-specific institutional, cultural, and political variables. The data spans from 1998 to 2013. While other studies fail to address the problem of simultaneity between investment and corruption, Essay one tackles this problem by using lagged variables. The results show that M&A are a robust determinant of corruption. Higher M&A levels both in number and in volume can lead to lower levels of corruption of the host country.

Essay two investigates the effects of corruption distance on bilateral M&A. Corruption distance, defined as the absolute gap in the level of corruption between two countries, can also play a big role in the amount and value of bilateral M&As

between country pairs. Multinational firms exposed to corrupt environments at home have a competitive advantage of expertise in managing corruption. However, this advantage turns into a disadvantage and becomes useless in transparent markets. Alternatively, firms from countries with low levels of corruption have a comparative disadvantage in dealing with corruption since they face an additional challenge in conducting business in corrupt countries. Thus, companies in corrupt countries prefer to invest in similarly corrupt countries, while companies in clean countries opt to merge with companies in other clean countries. Essay two hypothesizes that an increase in corruption distance between two countries would result in less bilateral M&A activity. I investigate the association between corruption distance and mergers and acquisitions (M&A) in a sample of 60 country pairs. The data spans from 1995 to 2013. The methodology used to analyze the data is a two-stage approach. By using Probit regression in the first stage, I study how corruption distance affects the likelihood of M&A decisions. Then, in the second stage, I employ panel regression analysis to examine the effects of corruption distance on the amount of M&A. Essay two finds that corruption distance impacts merger decisions, the number of mergers, and the value of mergers in a country pair. Firms that experience corruption at home tend to merge with firms in countries with similar levels of corruption. I also found that acquirers in corrupt countries tend to merge with firms in countries whose corruption levels are slightly lower than theirs.

Essay three looks at the relationship between corruption and US outward foreign direct investment (FDI). There is a consensus in the literature that corruption has detrimental effects on FDI inflows. However, Essay three looks at corruption from a different perspective. I use the US media to measure corruption. There are numerous newspapers and journals that cover stories about corruption in other countries (e.g., *The Wall Street Journal*, *The New York Times*, *Chicago Tribune*, etc.). These journals are read by many CEOs and top executives, which can affect their perceptions of

corruption in a foreign country and consequently their investment decision. To construct media corruption perceptions of a country, I establish a ratio of the number of articles containing news about the country's corruption in a given year over the number of articles covering trades in the country. Then I investigate a possible relationship between media corruption perceptions and the US outward FDI towards that country by using a panel regression model. I use Factiva to extract the data relating to news stories about corruption and the gravity model to estimate bilateral trade and FDI flows. The data spans from 2000 to 2015.

The rest of the thesis is organized as follows. Chapter two presents Essay one, which is titled "Exporting Transparency Through Mergers". In Chapter three, Essay two, titled "Corruption Distance and Cross-Border Mergers", is presented. And finally, Chapter four contains Essay three, "Media Corruption Perceptions and US Foreign Direct Investment". Chapter five concludes the thesis.

ARTICLE I

EXPORTING TRANSPARENCY THROUGH MERGERS

ABSTRACT

Mergers and acquisitions (M&A) offer a framework for shedding new light on corruption. Closed economies are associated with higher possibilities of rent creation and extraction. In such economies, a basic remedy to cure corruption is the introduction of competition and openness to trade through M&A activity. I use the Corruption Perceptions Index (CPI) developed by Transparency International as a measure of corruption in a country. Using a large panel of 50 countries over a 16-year period, the results suggest that M&A activity helps countries reduce their level of corruption.

Keywords: Corruption, Mergers and Acquisitions, Openness.

JEL: D73, G34, F30, H10.

1.1 Introduction

"There is no compromise when it comes to corruption. You have to fight it."
- A. K. Antony, former defence minister of India and member of the parliament (as cited in Ullekh, 2012).

There have been several studies on the effects of foreign direct investment (FDI) inflows on host country corruption, but no study has investigated the effects of mergers and acquisitions (M&A) on the host country's level of corruption. This is somewhat surprising since M&A are the most important component of FDI. The share of M&A in FDI has been increasing in recent years, and M&A have become a primary mode of internationalization (UNCTAD, 2000). At the same time, policy makers view corruption as a major hindrance to economic growth and development. As a result, the fight against corruption has garnered considerable attention and international organizations such as the UN, the IMF and the OECD have taken a special interest in anti-corruption movements. Corruption is arguably the most serious problem in developing countries (e.g., Bardhan, 1997) and it is also a challenge for many developed countries (Kaufmann, 2004). Corruption can only be remedied if its causes and determinants are identified. This study aims to demonstrate that M&A activity is one of these determinants and attempts to illustrate its impact on corruption.

Literature on corruption identifies three prerequisites for corruption: the discretionary power of public officials, the association of this power with economic rents, and the probability of these officials getting caught and being penalized (Jain, 2001). However, the presence of rents is seen as the single most important prerequisite of corruption (Braguinsky, 1996) because the existence of economic rents fosters corruption (Ades and Di Tella, 1997). The possibility of corrupt transactions will decrease if bureaucrats have less opportunity to extract or create economic rents. As

one solution, Ades and Di Tella (1997) suggest an economist's approach to control corruption by increasing the role of competition and markets, thus lowering the chances of the exploitation of discretionary power. Reduced official discretion will reduce the potential for corruption (Rose-Ackerman, 1997).

Focusing on M&A activity as the proxy for openness is reasonable for several reasons. First, cross-border deals occur frequently and the M&A market is voluminous. Second, foreign investors bring new culture, norms and technologies which are spilled over to domestic firms. Third, domestic M&A facilitate the spread of these new norms and culture. The presence of foreign investors and multinationals along with domestic acquisitions intensifies competition. Moreover, competition restricts the profits of engaging in a corrupt transaction and discourages public officials from initiating corrupt behaviour. Although a closed economy provides a fertile ground for corruption activities, competition can hinder corruption.

As the major component of FDI, M&A introduce more competition in host countries. Because M&A are by far the main type of investment in a foreign country and M&A are more effective in introducing change to the target firms through ownership, in this study I investigate the effects of M&A on host country corruption. To the best of my knowledge, this is the first study that empirically analyzes the relationship between the intensity of M&A and local corruption. Although the level of corruption has a strong effect on M&A decisions, M&A could decrease corruption. This study may bring new insights into our understanding of corruption by addressing the problem of simultaneity between M&A and corruption.

The rest of the paper is structured as follows. In Section 2, I review the literature and develop the hypotheses. Section 3 presents the data and methodology; Section 4

reports and discusses the empirical results; and Section 5 concludes the paper with a discussion of the most important implications.

1.2 Literature Review and Hypotheses Development

Corruption is usually understood as the "misuse of public power for private gain", where private gain may occur either to the individual official or to the group to which they belong. The issue of corruption has attracted the interest of many political scientists and economists in recent years. Early studies mainly focused on the consequences of corruption and showed that corruption deters economic development and growth. These bodies of literature were pioneered by Mauro (1995), who reports a significant negative relationship between corruption and investment that extends to growth. Several consequent studies confirmed and broadened Mauro's (1995) results and extended to other macroeconomic variables such as foreign direct investment and mergers and acquisitions. Wei (2000b), Habib and Zurawicki (2002) and Lambsdorff (2003) focused on the link between corruption and FDI and show that corruption has an adverse effect on foreign investment and capital inflows because it renders a country unattractive to foreign investors.

Later studies investigated the causes of corruption to understand why some countries exhibit higher levels of corruption than others. Among other factors, competition serves as a major cause of corruption and has attracted the interest of many scholars. Lambsdorff (2005) contends that in competitive environments, public servants and politicians have less to sell in exchange for bribes, and as a result, they are less motivated to start a corrupt career. Ades and Di Tella (1995, 1997 and 1999), Sung and Chu (2003), and Gerring and Thacker (2005) also find a negative correlation between competition and corruption. The literature presents several other causes of corruption. Government size, institutional quality, degree of democracy, press

freedom, national income, and cultural determinants are among the other causes of corruption which will be addressed further in this paper.

The presence of resources that can be easily misappropriated or transferred, along with discretionary power in allocating them, nourishes corruption. Closed markets with imperfect competition are an important source of rents. In these markets, the possibility of corrupt transactions increases when the discretionary power of the relevant bureaucrats or public officials allows extraction or creation of economic rents, while these bureaucrats are not held accountable for their actions (Tanzi, 1998; Rose-Ackerman, 1999; Jain, 2001).

Ades & Di Tella (1995, 1997 and 1999) claim that corruption is higher when bureaucrats have the potential to extract larger economic rents. They argue that openness to international trade will reduce the monopolistic power of domestic producers and strengthen market competition, which in turn narrows the rents available for bureaucrats to extract. "A natural approach to corruption control is to appeal to the concept of competition as it is argued that bribes are harder to sustain where perfect competition prevails" (Ades & Di Tella, 1999). They use country's openness to trade as an alternative indicator of competition and find that openness, defined as the ratio of imports to GDP, is negatively linked to corruption. Sung and Chu (2003), Sandholtz & Koetzle (2000), Sandholtz & Gray (2003), and Gerring & Thacker (2005) report similar findings. Treisman (2000) also uses the share of imports in GDP as a proxy for openness to trade and fails to find a significant relationship between exposure to imports and lower corruption. However, Lambsdorff (2005) questions the usefulness of the ratio of imports to GDP as an indicator of competition or openness. He argues that this variable is highly dependent on the size of a country and can be a good indicator of competition in small countries, because large countries can compensate for a low ratio of import to GDP through

more competition within their own borders. Moreover, Gerring & Thacker (2005) argue that a country may have a high level of import ratio, but not a particularly open economy. Although domestic acquisitions can reduce competition if bidders acquire competitors, but this effect is not high enough to be considered in the paper.

Wei (2000a) applies a measure of "natural openness", which refers to the extent of openness in a country determined by its population and its remoteness from world trading centres. Using this measure, he finds that natural openness is indeed a determinant of corruption, pointing out the helpful role of competition in decreasing corruption. However, "natural openness" has been criticized because of its dependence on population size.[1]

Another possible measure of the extent of competition and openness of a country is its level of foreign direct investment (FDI). Larrain and Tavares (2004) use the ratio of FDI to GDP as an indicator of openness to trade and empirically find that higher exposure to FDI tends to be related to lower corruption levels. Gerring & Thacker (2005) also find a similar relationship between trade openness, measured by the ratio of FDI to GDP, and corruption.

As the most important component of FDI, M&A are also negatively affected by host country corruption. Corruption is seen as a market barrier to entry and it is a discount on merger synergies (Weitzel and Berns, 2006). Moreover, corruption in a host country shifts ownership from wholly owned (acquisitions) to joint ventures (Javorcik and Wei 2009). In addition, once a company has made an acquisition, it is difficult to resell it, whereas it is much easier to sell off a capital investment. Thus, when a company has an incentive to acquire or merge with another company, corruption in

[1] See Knack and Azfar (2003).

the host country is a matter of great consideration. Wei (2000b) finds evidence that American and European investors are indeed averse to corruption in host countries.

Cross-national economic ties can limit corruption by increasing its cost. Corrupt practices can perpetuate themselves more easily in closed economies, but in open markets corrupt officials would feel the pinch of international openness. Because bribe-paying companies suffer under international competition, they would have less money to offer, and bureaucrats would find that their corruption-related income declines. Greater exposure to international trade thus penalizes corruption. On the other hand, open societies not only import goods and capital from the rest of world but also ideas, policies and norms. International integration has its domestic consequences. Openness to international transactions can introduce policy shifts and reform the domestic economies and politics of countries. The effects of international interactions are very substantial and can affect norms and practices that are usually determined by local social and cultural factors. Although corruption in a country has powerful domestic determinants, it is significantly affected by the level of international integration and openness. Sandholtz and Gray (2003) investigate such a relationship and find that being tied to international networks of exchange, communication and organization decreases the level of corruption.

The volume of cross-national mergers and acquisitions has been growing worldwide. In the last decades, M&A have become the most important component of capital inflows and foreign investment. While the degree of market diversification and competition reduces opportunities for rent creation, which in turn leads to less corruption, cross-national M&A activity intensifies competition and fosters openness to trade in a country, and as a result, may decrease corruption. As put forward by Rose-Ackerman (1975), corruption may be less frequent if it has long-term negative consequences for the firms and individuals involved, as is the case with M&A

activity. Both cross-national and domestic M&A activity can open the economy to international trade and intensify the degree of competition within a country. Thus, total M&A activity can proxy competition in a host country.

Closed economies are associated with higher possibilities of rent creation and extraction. In these environments, the introduction of competition and openness to cross-border trades can be a basic remedy for corruption. M&A activity can open the gates of the economy and increase competition. It can also bring along ideas, norms and policies. In this paper, I assess M&A activity for each country through two separate measures: the total number of M&A deals per year and the total transaction value in US dollars per year. Based on the above analysis on the economic conditions affecting the opportunities and costs of corruption in host countries, I can hypothesize that a higher amount of M&A will decrease corruption.

1.3 Data and Methodology

1.3.1 The Model

To measure the effects of country-specific institutional, cultural, and political variables that affect the level of corruption over time, panel data is a rational approach. Other studies that investigate the causes of corruption neglected the effect of time. Most of the previous studies used a simple OLS regression model, which fails to address the effects of time. The dependent variable in the panel regression equation is the Transparency International measure of corruption and the independent variables are M&A activity measures plus the control variables. The panel model, which is used in the empirical analysis to test the hypotheses, is expressed as follows:

$$C_{i,t} = \alpha_0 + \beta M_{i,t-1} + \gamma' X_{i,t} + \lambda_t + \theta_i + \varepsilon_{i,t}, \quad (1)$$

Where $C_{i,t}$ is the level of corruption measured by CPI; $M_{i,t-1}$ is the lagged M&A activity measures in country i at time t; $X_{i,t}$ is the vector of control variables: former colony, per capita GDP (lagged), ethnolinguistic fractionalization, oil exporter, government expenditure, population, political rights, French legal origins, and primary religion; β and γ are the parameters to estimate; α_0 is the portion of intercept that is common to all years and countries; λ_t denotes year-specific effect common to all countries; θ_i is the source-country fixed effects; $\varepsilon_{i,t}$ is normal error terms with mean zero and variance σ^2_ε; i stands for the country (i = 1,...,N); and t stands for the year (t = 1,...,T). I include in the model the lagged variables of M&A activity and GDP per capita to tackle the issue of reverse causality. The prediction of β is also specific to the openness hypothesis; therefore, I hypothesize a positive relationship between corruption and M&A.

1.3.2 Control Variables[2]

The abundant empirical literature on the determinants of corruption identifies a series of alternative conditions which will affect the analysis and choice of controls.[3] Among the conditions found to affect corruption are:

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[2] I limit the report to the variables that are correlated with corruption. A number of indicators I collected were dropped for having no statistically significant relationship with corruption in bivariate and/or multivariate tests including sets of regional dummy variables, GDP (log), percentage of different religious affiliations, and British, German, Scandinavian and socialist legal origin dummy variables.

[3] See Lambsdorff (2006) for an excellent review of this literature.

1.3.2.1 Legal Systems

The most obvious cost of corruption is the risk of getting caught and punished (Treisman 2000, p. 402). The probability of getting caught and sanctioned depends in part on the country's legal system. The civil law system, which is found mostly in continental Europe and its former colonies, was introduced in the 19th century by Napoleon and Bismarck. La Porta et al. (1999) argue that the civil law system is "largely legislature created and is focused on discovering a just solution to a dispute (often from the point of view of the State), rather than on following a just procedure that protects individuals against the State". Civil law systems have largely been an instrument of the State in expanding its power and "can be taken as a proxy for an intent to build institutions to further the power of the State" (La Porta et al. 1999, Treisman 2000). Thus, a civil law tradition is expected to be associated with lower governance, less efficient governments, and higher levels of corruption (La Porta et al. 1999).

1.3.2.2 Religion

Religious practices have the potential "to shape national views regarding property rights, competition, and the role of State" (Beck et al. 2003, p. 151; Stulz and Williamson 2003; La Porta et al. 1999). "In religious traditions such as Protestantism, which arose in some versions as dissenting sects opposed to the State-sponsored religion, institutions of the church may play a role in monitoring and denouncing abuses by State officials" (Treisman 2000, p. 403). Since the Catholic and Muslim religions tend to limit the security of property rights and private contracting (Levine 2005 and Landes 1998), these religions may be associated with lower government performance and higher corruption (La Porta et al. 1999). Moreover, Protestant

countries have better creditor rights and less corruption (Stulz and Williamson 2003). Thus, I expect Protestant countries to have lower levels of corruption.

1.3.2.3 Ethnolinguistic Fractionalization

Corruption is an illegal contract which cannot be enforced by courts. Treisman (2000) argues that ethnic communities and networks may serve as one of the mechanisms to "enhance the credibility of the private partner's commitment. In ethnically divided societies, ethnic communities may provide cheap information about and even internal sanctions against those who betray their coethnics" (Treisman 2000, p. 406). Therefore, corruption contracts are strengthened within ethnic communities (Treisman 2000). La Porta et al. (1999) measure such fractionalization and find that higher levels of fractionalization are associated with worse property rights and regulation, lower government efficiency, and more corruption. Thus, more corruption is expected in societies with ethnolinguistic fractionalization.

1.3.2.4 Political Freedom

Free association, free press, and regular and open electoral contests can increase the likelihood of divulging corrupt activities. Higher political rights enhance the opportunity of detecting and punishing those who engage in corruption (Lederman et al., 2005). "Countries with more political competition have stronger public pressure against corruption - through laws, democratic elections, and even the independent press - and so are more likely to use government organizations that contain rather than maximize corruption proceeds" (Shleifer and Vishny 1993, p. 610). Moreover, Treisman (2007) finds that greater political rights are significantly related to lower perceived corruption.

1.3.2.5 GDP per Capita

Some authors suggest that the problem of corruption lies in the low salaries bureaucrats receive (Treisman 2000). They argue that to reduce the level of corruption, the wages of bureaucrats and public servants should be raised[4]. The literature empirically shows that wealthier countries are less likely to be corrupt. To measure the wealth of a nation, GDP per capita is a natural option. Ades and Di Tella (1999) also use per capita GDP as a control for the wealth of a nation. However, there is probably some degree of endogeneity between per capita GDP and corruption, since corruption and per capita GDP are simultaneously related. I address the issue by lagging the per capita GDP in the analysis.

1.3.2.6 Former Colonies

Acemoglu et al. (2001 & 2002) emphasize the importance of institutions, shaped by a country's colonization model. Mauro (1997) argues that it is difficult for countries that have been colonized to develop efficient institutions. Former colonies are considered less likely to have developed efficient and transparent local institutions because the colonizers' institution models "overlapped (and sometimes clashed) with previously existing informal institutions, fostering social fractionalization and hindering the mobility and social change required by the market" (Alonso 2007, p. 71). I expect that the countries that have been colonized in the past are more corrupt.

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[4] See Klitgaard (1988) and Besley and McLaren (1993).

1.3.2.7 Oil Exporter Countries

Leite and Weidmann (1999) present a model where economies abundant in natural resources show higher levels of corruption. They find that higher levels of natural resources are positively related to higher levels of corruption. Sachs and Warner (1995) show that natural resource economies grow more slowly, and they suggest this is due in part to a lower efficiency of government. Ades and Di Tella (1999) also find evidence that oil and corruption are correlated.

1.3.2.8 Government Expenditure

Many contemporary academic works suggest that a large public sector, measured by government expenditure, fosters corruption. The larger the role the government plays in the market - as producer and/or consumer - the greater its capacity to engage in corrupt activity, ceteris paribus. As a rule, "the larger the relative size and scope of the public sector, the greater will be the proportion of corrupt acts" (Scott 1972, p. 9).

1.3.2.9 Size

To control for the size of the country, I use its population because several papers suggest a relationship between population and government efficiency (Treisman 2000, Knack and Azfar 2003).

1.3.2.10 Issue of Endogeneity

There is abundant literature on the negative effects of corruption on openness. These studies show how a higher level of corruption is associated with lower foreign

investment (Hines, 1995; Henisz, 2000; Wei, 2000b, 2000c; Habib and Zurawicki, 2001, 2002). In this paper, I am interested precisely in the opposite direction of causality: how a higher degree of country openness affects the level of corruption in an economy. Since corruption is likely to explain as well as be explained by openness, the issue of simultaneity becomes key in interpreting the results. Most of the studies that address this link fail to deal with or overlook the endogeneity problem associated with the two-way causal relationship between openness and corruption. Since simultaneous equation models cannot be used simply because it is impossible to find an instrumental variable for corruption, one possible solution to this problem is to use lagged variables. I address the issue of reverse causality by using lagged variables for measures of M&A and GDP per capita.

The aim of models with lagged variables is to allow for causal effects that linger over a period of time rather than instantaneous ones[5]. While corruption can be explained by the same year openness levels, it cannot be explained by the openness in coming years. Using lagged variables enables us to tackle the problem of endogeneity/simultaneity.

1.3.3 Data

Our analysis is based on panel dataset of measures of corruption and its potential determinants in 50 countries. Since I am combining a number of datasets, I have different numbers of observations for different variables. This makes the panel dataset unbalanced. The data spans from 1998 to 2013. Appendix 1 summarizes the

[5] See Cingolani and Crombrugghe (2012) for an excellent survey on how to deal with reverse causality.

definition and sources of all the variables used in this article with their expected signs.

I estimate equations explaining corruption indices as a function of openness to trade and country characteristics. Since I have 16 years of observations and 50 countries, the total number of potential observations is 800 (16 × 50). However, for some countries, CPI is not available for the early years in the sample. Moreover, some data related to 2013 (for example GDP per capita or government expenditure) is not yet available for some countries, which further decreases the number of observations.

1.4 Results and Discussion

1.4.1 Descriptive Statistics

Table 1.1 presents summary statistics for the corruption index, M&A activity measures and the control variables. As to the measure of corruption, CPI ranges from 0 to 10 and has the maximum of 10 and minimum of 1 in the sample data. CPI has a mean of 3.67 and standard deviation of 2.48, showing that most of the population's CPI is not far from the sample mean, indicating the severity of the problem of corruption in the world. In measures of M&A, *total count per year* has the maximum of 11,019 and *total sum per year* has the maximum of 1,589,574 million dollars. Fifty-eight percent of the countries in the sample were a colony, 42 percent have a French legal origin, 24 percent are Protestant, and 12 percent are oil exporters.

Table 1.1
Summary Statistics

Variable	Obs	Unit	Mean	Std. Dev.	Min	Max
CPI	793	Between 0 and 10	5.66	2.48	1	10
Domestic count per year	800	Count	303.96	917.51	0	8709
Domestic sum per year	800	Million dollars	25856.70	114292.90	0	1226334
Cross-border count per year	800	Count	180.48	332.66	0	2580
Cross-border sum per year	800	Million dollars	19977.50	49955.32	0	492604.8
Total count per year	800	Count	484.43	1228.60	0	11019
Total sum per year	800	Million dollars	45834.19	156018.80	0	1589574
Per capita GDP	799	Dollars	19978.99	19031.53	274	100819
Former colony	800	Dummy	0.58	0.49	0	1
EF	800	Between 0 and 1	0.26	0.25	0.002	0.8567
Oil exporter	800	Dummy	0.12	0.33	0	1
Government expenditure	790	Million dollars	16.42	5.35	2.047121	31.59911
Population	799	Million	97.00	238.00	3.29	1360.00
Political rights	784	Between 1 to 7	2.32	1.74	1	7
French legal origin	800	Dummy	0.42	0.49	0	1
Primary religion	800	Dummy	0.24	0.43	0	1

Table 1.2 presents the pairwise correlations matrix of dependent and independent variables. The two variables *Cross-border count per year* and *Cross-border sum per year* are highly correlated. Their correlation coefficient is 0.9043, which confirms that the two variables actually measure the same thing: M&A activity. GDP per capita has a slightly high correlation with CPI, which is normal since GDP per capita is linked to corruption in the literature. Apart from the aforementioned variables, all other pairwise correlations between the independent variables are not high enough to cause a possible multicollinearity problem in the model. The correlation coefficients between main variables (*total sum per year* and *total count per year*) and CPI are positive and significant, which shows that lower levels of corruption (higher index) are associated with more M&A activity.

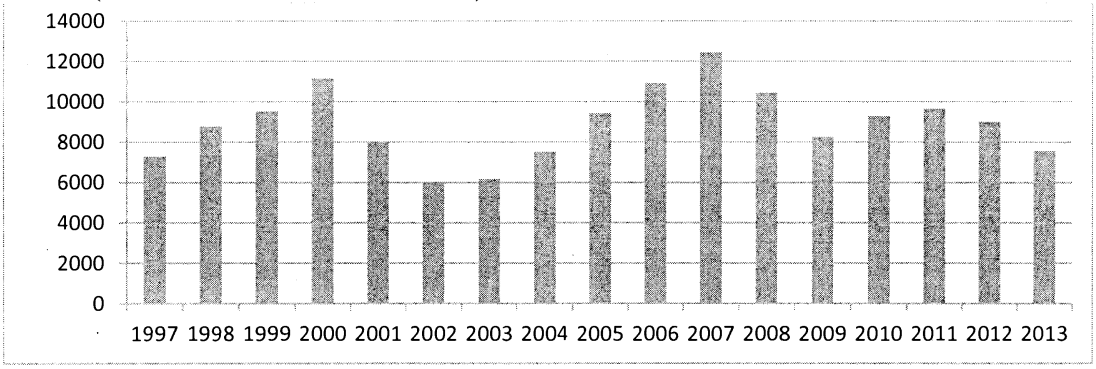
Table 1.2
Correlation matrix

Correlation Matrix	CPI	Count per year	Sum Per Year	Per Capita GDP	Former colony	EF	Oil exporter	Government Expenditure	Population	Political rights	French legal origin	Primary religion
CPI	1.0000											
Cross-border count per year	0.3915**	1.0000										
Cross-border sum per year	0.3010**	0.9043**	1.0000									
Per capita GDP	0.7891**	0.4239**	0.3202**	1.0000								
Former colony	-0.4469**	-0.3543**	-0.3140**	-0.5422**	1.0000							
Ethnolinguistic Fractionalization	-0.4722**	-0.1514**	-0.1347**	-0.4247**	0.3852**	1.0000						
Oil exporter	-0.2963**	-0.1632**	-0.1258**	-0.1109**	0.1895**	-0.0388	1.0000					
Government expenditure	0.5303**	0.1915**	0.1414**	0.5022**	-0.5216**	-0.3995**	-0.1839**	1.0000				
Population	-0.2662**	0.1038**	0.0699**	-0.2285**	-0.0388	0.2261**	-0.0719**	-0.1952**	1.0000			
Political rights	-0.6048**	-0.2984**	-0.2444**	-0.5760**	0.3921**	0.3467**	0.2647**	-0.4659**	0.2935**	1.0000		
French legal origin	-0.3538**	-0.2273**	-0.1539**	-0.3079**	0.0673	-0.2285**	0.1846**	-0.0930**	-0.1529**	0.0011	1.0000	
Primary religion	0.4210**	0.3915**	0.3239**	0.3774**	-0.1860**	-0.1007**	-0.0634	0.3766**	-0.1069**	-0.3160**	-0.4782**	1.0000

** Significant at the 5% level.

Figure 1.1 plots the number (Panel A) and dollar value (Panel B) of cross-border deals over the sample period. Both panels show similar patterns. Cross-border M&A activity increases throughout the 1990s, declines after the stock market crash of 2000, then increases from 2002 until 2007, declines with the economic recession of 2007, and stays volatile until 2013. Erel et al. (2012) find the same pattern in M&A activity.

Panel A (Total number of cross-border deals)



Panel B (Total value of cross-border deals in $million)

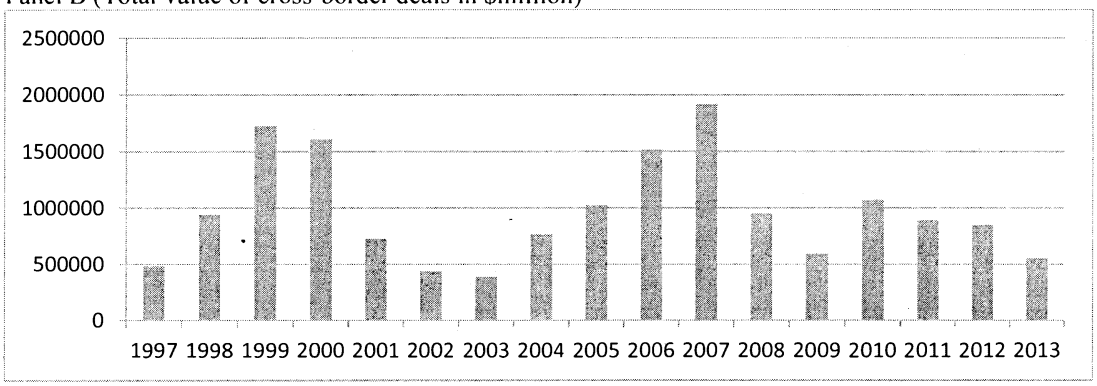


Figure 1.1 Cross-border M&A activity

1.4.2 Regression Results

To evaluate the effects of openness to trade and competition on corruption, I use a multivariate regression framework. Our goal is to analyze how M&A activity can affect the level of corruption in the host country over time. Because I am interested in the effects of M&A activity on corruption and how changes in M&A activity can influence corruption, I use panel analysis. Our dependent variable is the corruption index which measures the corruption perception level over the entire sample period. Our independent variables are the M&A activity measures and several determinants of corruption suggested in the literature as control variables.

Table 1.3 presents random effect panel regression estimates of the determinants of corruption as represented by proxies of openness to trade and competition (domestic, cross-border and total M&A activity). The results are revealing. All measures of M&A activity show significant and positive association to CPI, meaning that these activities decrease the level of corruption in host countries. An increase in the level of M&A activity leads to an increase in the corruption index, which means less corruption. Coefficients of both cross-border sum and cross-border count per year are significant and positive, showing that cross-border mergers can increase competition and spread the norms and cultures from the other side of the border. Domestic measures also show a positive and significant relation to corruption. This shows that domestic mergers also play a big role in decreasing corruption by transferring norms to other companies and increasing competition. Coefficients of total activity in a country are greater than cross-border or domestic activities alone. This means that both cross-border and domestic mergers are important in increasing competition and, as a result, reducing corruption.

Table 1.3
Panel Analysis of the Determinants of Corruption

	CPI	CPI	CPI	CPI	CPI	CPI	CPI
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Log cross-border sum per year$_{(t-1)}$	0.056***						
	(3.52)						
Log cross-border count per year$_{(t-1)}$		0.182***					
		(3.85)					
Log domestic sum per year$_{(t-1)}$			0.034**				
			(2.15)				
Log domestic count per year$_{(t-1)}$				0.146***			
				(3.1)			
Log Total sum per year$_{(t-1)}$					0.057***		
					(2.78)		
Log Total count per year$_{(t-1)}$						0.206***	
						(3.67)	
Former colony	-0.889**	-0.801**	-0.942**	-0.846**	-0.892**	-0.808**	-0.929**
	(-2.21)	(-2.09)	(-2.3)	(-2.17)	(-2.21)	(-2.13)	(-2.25)
Log GDP per capita$_{(t-1)}$	0.172**	0.149*	0.168*	0.127	0.173**	0.107	0.242***
	(2.17)	(1.76)	(1.93)	(1.52)	(2.1)	(1.31)	(2.83)
EF	-2.177**	-2.029**	-2.087**	-2.116**	-2.108**	-2.027**	-2.112**
	(-2.47)	(-2.45)	(-2.27)	(-2.5)	(-2.39)	(-2.49)	(-2.31)
Oil Exporter	-1.184***	-1.05***	-1.125***	-1.063***	-1.156***	-1.02***	-1.223***
	(-3.12)	(-2.8)	(-2.87)	(-2.73)	(-3)	(-2.7)	(-3.09)
Log Government Expenditure	0.047	0.063	0.053	0.03	0.05	0.055	0.053
	(0.88)	(1.13)	(0.95)	(0.58)	(0.91)	(0.97)	(0.94)
Log population	-0.705***	-0.739***	-0.752***	-0.766***	-0.722***	-0.784***	-0.683***
	(-6.24)	(-6.92)	(-6.28)	(-6.39)	(-6.33)	(-6.98)	(-5.8)
Political rights	-0.083*	-0.076*	-0.094*	-0.085*	-0.089*	-0.075	-0.082*
	(-1.7)	(-1.68)	(-1.8)	(-1.78)	(-1.86)	(-1.64)	(-1.8)
French legal origin	-1.241***	-1.195***	-1.231***	-1.179***	-1.242***	-1.165***	-1.237***
	(-2.78)	(-2.93)	(-2.68)	(-2.73)	(-2.79)	(-2.84)	(-2.71)
Primary religion	0.757	0.674	0.736	0.686	0.738	0.66	0.784
	(1.49)	(1.44)	(1.4)	(1.44)	(1.47)	(1.44)	(1.53)
Constant	17.357***	17.696***	18.414***	18.667***	17.594***	18.624***	16.767***
	(8.09)	(8.25)	(7.98)	(8.07)	(8.03)	(8.51)	(7.34)
Observations	753	768	711	753	763	773	775
R^2	0.75	0.78	0.74	0.77	0.75	0.78	0.74

This table presents estimates of panel regressions of the effects of cross-border and domestic mergers and acquisitions on corruption. The dependent variable is corruption perception index (CPI) for the year t and country i. To control for endogeneity, some independent variables are lagged one year. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Most of the control variables are significant and have the expected sign. Former colony has a negative and significant coefficient in all the models. While higher

values of CPI mean the country is less corrupt, these results confirm the literature stating that former colonies cannot develop efficient institutions and are more corrupt (lower CPI). The coefficient of Log per capita GDP is significant for most of the model specifications. This shows that GDP per capita and corruption are negatively associated and higher GDP per capita is linked to less corruption in a country. Entholinguistic fractionalisation is also significant and negative, as predeicted in the literature. This shows that more ethnolinguistic fractionalisation in a country is linked to higher corruoption. Moreover, Oil exporter dummy is strongly significant and negative in all the M&A measures. As stated before, oil exporter countries are tend to be more corrupt. Contrary to what is predicted in the literature, the coefficeients of government expenditure are not significant in any M&A measures. The coeficients of political rights are also significant and negative. This shows and increase in the variable (being less politically free) will decrease the CPI (being more corrupt). Thus higher political freedom in country is linked to less corruption in a country, as predicted by the literature. French legal origins dummy is also significant and negative stating that countries with civil law systems are tend to be more corrupt. Interestingly primary religion is not significant in any M&A measures contrary to what is reported in the literature.

1.4.3 Robustness Checks

In this section, I use different approaches to test the robustness of the results.

1.4.3.1 Alternative Corruption Measure

To gain robustness, I use an alternate measure of corruption in the analysis. The Political Risk Services corruption index (ICRG) is another measure of perceived

corruption which is widely used in the literature. This is particularly important since corruption is measured through surveys on the respondent's subjective perceived level of corruption. Using different indices of corruption reduces the risk of a respondent's misjudgment on their perceived level of corruption. The ICRG has a correlation coefficient of 0.8864 with CPI. Table 1.4 presents random effect panel regression estimates of the determinants of corruption. The dependent variable is ICRG and independent variables are measures of M&A activity.

Table 1.4
Robustness tests, Alternate Corruption Measure

	ICRG	ICRG	ICRG	ICRG	ICRG	ICRG
Log cross-border sum per year(t-1)	0.05***					
	(2.78)					
Log Cross-border Count per year(t-1)		0.13*				
		(1.68)				
Log Domestic sum per year(t-1)			-0.007			
			(-0.47)			
Log Domestic count per year(t-1)				0.128***		
				(2.89)		
Log Total sum per year(t-1)					0.033*	
					(1.95)	
Log Total count per year(t-1)						0.15**
						(2.32)
Former colony	-0.396	-0.339	-0.437	-0.369	-0.421	-0.358
	(-1.57)	(-1.37)	(-1.64)	(-1.49)	(-1.64)	(-1.46)
Log GDP per Capita(t-1)	0.079	0.05	0.126	0.029	0.083	0.016
	(0.74)	(0.41)	(1.12)	(0.26)	(0.75)	(0.13)
EF	-0.862	-0.726	-0.785	-0.745	-0.807	-0.716
	(-1.65)	(-1.54)	(-1.54)	(-1.62)	(-1.56)	(-1.57)
Oil Exporter	-0.245	-0.195	-0.332**	-0.169	-0.253	-0.173
	(-1.42)	(-1.32)	(-2.02)	(-0.98)	(-1.44)	(-1.12)
Log Government expenditure	-0.072	-0.044	-0.138**	-0.074	-0.064	-0.047
	(-1.19)	(-0.69)	(-2.13)	(-1.26)	(-1.02)	(-0.73)
Log population	-0.31***	-0.338***	-0.289***	-0.371***	-0.317***	-0.376***
	(-3.61)	(-3.58)	(-3.38)	(-4.42)	(-3.65)	(-4.01)
Political rights	-0.168***	-0.169***	-0.161**	-0.163***	-0.171***	-0.158***
	(-2.74)	(-2.82)	(-2.52)	(-2.6)	(-2.69)	(-2.66)
French legal origin	-0.258	-0.219	-0.255	-0.19	-0.257	-0.19
	(-0.95)	(-0.88)	(-0.93)	(-0.76)	(-0.94)	(-0.78)
Primary religion	0.587	0.578**	0.685**	0.58**	0.613**	0.582**
	(1.95)	(2.1)	(2.33)	(2.13)	(2.09)	(2.16)
Constant	8.544***	9.024***	8.384***	9.872***	8.739***	9.775***
	(3.93)	(3.8)	(3.7)	(4.42)	(3.94)	(4.05)
Observations	759	775	716	759	770	775
R2	0.64	0.66	0.61	0.66	0.63	0.78

This table presents estimates of random effect model of cross-border and domestic mergers and acquisitions activity. The dependent variable is Political Risk Services corruption index (ICRG) for the year t and country i. To control for endogeneity, some independent variables are lagged one year. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

The results are similar to Table 1.3 and confirm out results. The coefficients of both cross-border sum and count per year are positive and statistically significant. Domestic measures show a positive and significant relation to ICRG in at least one

measure, and the coefficients of both total sum and count per year are significant. Former colony, GPD per capita, EF and French legal origin do not show significance in any measures, but the coefficients of primary religion are statistically significant in most of the measures.

1.4.3.2 Longer Lags

Curing corruption is not easy. Corruption is rooted in the quality of a country's institutions, and institutional norms and policies may take years to change. As a result, I use longer lags in the second robustness checks to see if M&A activity from previous years has an effect on corruption. I use 2 year and 5 year lags in Table 1.5, which presents estimates of Pooled OLS model of cross-border and domestic merger and acquisition activity.

Table 1.5
Robustness tests, Longer lags

Lag 2	CPI	CPI	CPI	CPI	CPI	CPI
Log cross-border sum per year(t-2)	0.266*** (9.48)					
Log Cross-border Count per year(t-2)		0.702*** (13.53)				
Log Domestic sum per year(t-2)			0.173*** (6.24)			
Log Domestic count per year(t-2)				0.52*** (11.49)		
Log Total sum per year(t-2)					0.271*** (8.33)	
Log Total count per year(t-2)						0.68*** (12.93)
Control Variables	Yes	Yes	Yes	Yes	Yes	Yes
Observations	750	768	709	752	760	773
R2	0.82	0.86	0.81	0.84	0.83	0.85
Lag 5	CPI	CPI	CPI	CPI	CPI	CPI
Log cross-border sum per year(t-5)	0.221*** (8.04)					
Log Cross-border Count per year(t-5)		0.672*** (13.48)				
Log Domestic sum per year(t-5)			0.168*** (6.27)			
Log Domestic count per year(t-5)				0.459*** (11.59)		
Log Total sum per year(t-5)					0.238*** (7.55)	
Log Total count per year(t-5)						0.611*** (12.91)
Control Variables	Yes	Yes	Yes	Yes	Yes	Yes
Observations	741	761	704	746	755	770
R2	0.82	0.85	0.81	0.83	0.82	0.84

This table presents estimates of Pooled OLS model of cross-border and domestic mergers and acquisition activity. The dependent variable is corruption perception index (CPI) for the year t and country i. To control for endogeneity, some independent variables are lagged. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

All measures of lagged M&A activity show significant and positive association to CPI, meaning that these activities decrease the level of corruption in host countries. The results of this table further confirm the results.

1.4.3.3 Random Effects vs. Fixed Effect and Pooled OLS

To check the validity of the random effect model, Table 1.6 compares the random effect, fixed effect and pooled OLS results. For reasons of parsimony, I do not report the coefficients of the random effect model which has been reported in Table 1.3.

Table 1.6
Robustness tests, OLS vs. Fixed Effect

	Pooled OLS					
	CPI	CPI	CPI	CPI	CPI	CPI
Log cross-border sum per $year_{(t-1)}$	0.306***					
	(10.9)					
Log Cross-border Count per $year_{(t-1)}$		0.779***				
		(15.3)				
Log Domestic sum per $year_{(t-1)}$			0.156***			
			(5.53)			
Log Domestic count per $year_{(t-1)}$				0.557***		
				(12.21)		
Log Total sum per $year_{(t-1)}$					0.293***	
					(8.95)	
Log Total count per $year_{(t-1)}$						0.745***
						(13.93)
Former colony	-0.154	-0.123	-0.27**	-0.178**	-0.219	-0.168*
	(-1.51)	(-1.41)	(-2.43)	(-1.84)	(-2.09)	(-1.85)
Log GDP per $Capita_{(t-1)}$	0.475***	0.09	0.691***	0.259***	0.47***	0.052
	(6.58)	(1.18)	(8.27)	(3.21)	(5.7)	(0.62)
EF	-0.827***	-1.165***	-0.476**	-1.017***	-0.739***	-1.131***
	(-3.63)	(-5.59)	(-1.96)	(-4.73)	(-3.24)	(-5.45)
Oil Exporter	-0.69***	-0.333***	-0.613***	-0.334***	-0.6***	-0.273**
	(-6.06)	(-3.02)	(-4.85)	(-2.88)	(-5.29)	(-2.42)
Log Government expenditure	0.134	0.066	0.092	0.069	0.122	0.075
	(1.51)	(0.76).	(0.92)	(0.85)	(1.38)	(0.91)
Log population	-0.66***	-0.837***	-0.579***	-0.847***	-0.681***	-0.921***
	(-17.18)	(-19.16)	(-12.02)	(-17.19)	(-14.82)	(-18.65)
Political rights	-0.075**	-0.082**	-0.069**	-0.095***	-0.083**	-0.091***
	(-2.15)	(-2.74)	(-1.82)	(-2.67)	(-2.37)	(-2.81)
French legal origin	-1.115***	-1.008***	-1.046***	-0.937***	-1.108***	-0.939***
	(-11.35)	(-11.37)	(-10.17)	(-10.55)	(-11.48)	(-11.04)
Primary religion	0.376***	0.201***	0.47***	0.19**	0.376***	0.172*
	(3.48)	(2.25)	(4.18)	(1.99)	(3.56)	(1.96)
Constant	10.799***	16.876***	8.748***	16.422***	11.191***	18.275***
	(9.26)	(12.61)	(6.01)	(11.27)	(8.4)	(12.7)
Observations	753	768	711	753	763	773
R^2	0.83	0.86	0.81	0.84	0.83	0.86

continued on the next page...

Table 1.6
Robustness tests, OLS vs. Fixed Effect (continuation)

	Fixed Effect					
	CPI	CPI	CPI	CPI	CPI	CPI
Log cross-border sum per $year_{(t-1)}$	0.046***					
	(3.69)					
Log Cross-border Count per $year_{(t-1)}$		0.136***				
		(3.81)				
Log Domestic sum per $year_{(t-1)}$			0.028**			
			(2.34)			
Log Domestic count per $year_{(t-1)}$				0.117***		
				(4.22)		
Log Total sum per $year_{(t-1)}$					0.048***	
					(3.5)	
Log Total count per $year_{(t-1)}$						0.165***
						(4.71)
Former colony						
Log GDP per $Capita_{(t-1)}$	0.259***	0.268***	0.297***	0.219***	0.27***	0.225***
	(3.93)	(4.04)	(4.53)	(3.23)	(4.1)	(3.33)
EF						
Oil Exporter						
Log Government expenditure	0.03	0.044	0.04	0.017	0.034	0.038
	(0.67)	(0.96)	(0.79)	(0.37)	(0.76)	(0.85)
Log population	-1.73***	-1.822***	-2.043***	-1.61***	-1.743***	-1.784***
	(-4.15)	(-4.46)	(-4.87)	(-4.01)	(-4.28)	(-4.47)
Political rights	-0.067**	-0.069**	-0.092***	-0.078***	-0.081***	-0.071**
	(-2.33)	(-2.43)	(-3.22)	(-2.8)	(-2.88)	(-2.56)
French legal origin						
Primary religion						
Constant	32.811***	34.073***	38.231***	31.094***	32.906***	33.591***
	(4.87)	(5.15)	(5.61)	(4.78)	(4.99)	(5.2)
Observations	753	768	711	753	763	773
R^2	0.41	0.45	0.44	0.46	0.43	0.46

This table presents estimates of Pooled OLS and fixed effect panel model of cross-border and domestic mergers and acquisition activity. The dependent variable is corruption perception index (CPI) for the year t and country i. To control for endogeneity, some independent variables are lagged. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. Country and time fixed effects are included. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

As it is presented in Table 1.5, all the measures of M&A activity are statistically significant in both Pooled OLS and fixed effect panel analysis. I ran the Breusch and Pagan Lagrangian multiplier test for random effects for each of the models, and I conclude that random effect is a more appropriate model than OLS. Moreover, the Hausman tests show that fixed effect is actually a better fit, but since the fixed effect model does not take into account the effect of time invariant variables (like colonial

history or religion), and also all the coefficients of the variables of interest have the same signs and are statistically significant in both models, I preferred to use random effect models in the main table (Table 1.3).

1.4.3.4 Equity Acquisitions Activity

In order to test the robustness of the results, I construct two equity acquisition measures: *Equity acquisition sum per year* and *Equity acquisition count per year*, gauging all the deals with fewer than 25% of shares before the deal and more than 25% of shares after the deal. These new measures also include M&A activity and can be a suitable proxy of openness and competition since many cross-border deals are actually partial acquisitions. Table 1.7 exhibits the results of random effect panel analysis of the effects of equity acquisitions on corruption.

Table 1.7
Robustness tests, Equity acquisition activity

	CPI	CPI	CPI	CPI	CPI	CPI
Log cross-border sum per $year_{(t-1)}$	0.057***					
	(3.53)					
Log Cross-border Count per $year_{(t-1)}$		0.184***				
		(3.72)				
Log Domestic sum per $year_{(t-1)}$			0.045**			
			(2.4)			
Log Domestic count per $year_{(t-1)}$				0.139***		
				(2.93)		
Log Total sum per $year_{(t-1)}$					0.059**	
					(2.68)	
Log Total count per $year_{(t-1)}$						0.219***
						(3.98)
Former colony	-0.893**	-0.799**	-0.937**	-0.855**	-0.888**	-0.808**
	(-2.22)	(-2.08)	(-2.3)	(-2.17)	(-2.21)	(-2.13)
Log GDP per $Capita_{(t-1)}$	0.17**	0.149*	0.168*	0.133	0.168**	0.101
	(2.13)	(1.83)	(1.9)	(1.58)	(2.04)	(1.24)
EF	-2.177**	-2.049**	-2.084**	-2.118**	-2.125**	-2.03**
	(-2.47)	(-2.47)	(-2.32)	(-2.5)	(-2.42)	(-2.5)
Oil Exporter	-1.179***	-1.051***	-1.109***	-1.066***	-1.159***	-1.01***
	(-3.09)	(-2.79)	(-2.93)	(-2.76)	(-3.03)	(-2.68)
Log Government expenditure	0.047	0.06	0.035	0.025	0.046	0.052
	(0.89)	(1.1)	(0.57)	(0.46)	(0.85)	(0.97)
Log population	-0.705***	-0.734***	-0.739***	-0.755***	-0.722***	-0.788***
	(-6.25)	(-6.94)	(-6.28)	(-6.29)	(-6.29)	(-7.01)
Political rights	-0.082*	-0.079*	-0.097*	-0.088*	-0.094*	-0.073*
	(-1.67)	(-1.77)	(-1.85)	(-1.82)	(-1.93)	(-1.66)
French legal origin	-1.242***	-1.199***	-1.24***	-1.19***	-1.243***	-1.16***
	(-2.78)	(-2.93)	(-2.74)	(-2.75)	(-2.8)	(-2.83)
Primary religion	0.758	0.677	0.735	0.695	0.736	0.663
	(1.49)	(1.44)	(1.42)	(1.45)	(1.46)	(1.45)
Constant	17.371***	17.597***	18.163***	18.461***	17.634***	18.669***
	(8.08)	(8.44)	(7.87)	(7.92)	(8)	(8.58)
Observations	755	773	715	756	763	775
R^2	0.75	0.78	0.75	0.77	0.76	0.78

This table presents estimates of random effect model of cross-border and domestic equity acquisition activity. The dependent variable is corruption perception index (CPI) for the year t and country i. To control for endogeneity, some independent variables are lagged one year. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Measures of equity acquisitions, which cover the deals making the acquirer the owner of more than 25% of the total shares, are positive and significant in all the measures.

The more the equity activities, the higher the corruption indices (less corruption). The results are consistent with Table 1.4, which tests the hypothesis for M&A deals.

1.4.3.5 Regional Subsamples

To test the robustness of the sample data, I divide the data into regional subsamples and test the hypotheses for each subsample. The regional subsamples are: North and South America, Europe, Africa and the Middle East, and Asia and Oceania. Since the subsamples are fairly small, I use the simple OLS regression to estimate the coefficients. Table 1.8 summarizes the results. Results of domestic M&A activity are not shown in the interest of brevity.

Table 1.8
Robustness tests, Regional Subsamples

	North and South America				Europe			
	CPI	CPI	CPI	CPI	CPI	CPI	CPI	CPI
Log Cross-border sum per $year_{(t-1)}$	0.161***				0.473***			
	(3.34)				(7.14)			
Log Cross-border Count per $year_{(t-1)}$		0.482***				1.13***		
		(3.78)				(10.39)		
Log Total sum per $year_{(t-1)}$			0.192***				0.48***	
			(3.48)				(6.57)	
Log Total count per $year_{(t-1)}$				0.604***				1.105***
				(4.16)				(9.47)
Former colony	0.253	0.266	0.321	0.458	-1.03***	-1.335***	-1.119***	-1.285***
	(1.07)	(1.03)	(1.38)	(1.91)	(-5.95)	(-8.42)	(-6.26)	(-8.27)
Log GDP per $Capita_{(t-1)}$	-0.499***	-0.633***	-0.562***	-0.727***	0.109	-0.095	0.141	-0.066
	(-3.33)	(-4.03)	(-3.58)	(-4.22)	(0.66)	(-0.61)	(0.82)	(-0.38)
EF	-5.186***	-5.245***	-5.017***	-5.031***	0.747	-0.171	0.858	-0.078
	(-8.49)	(-9.22)	(-8.6)	(-9.12)	(1.08)	(-0.28)	(1.24)	(-0.13)
Oil Exporter	-1.811***	-1.679***	-1.779***	-1.55***	-0.672***	-0.632***	-0.765***	-0.662***
	(-6.37)	(-5.95)	(-6.11)	(-5.45)	(-3.86)	(-3.92)	(-4.48)	(-3.71)
Log Government expenditure	0.035	-0.014	-0.008	-0.069	0.652***	0.234**	0.694***	0.328**
	(0.26)	(-0.11)	(-0.05)	(-0.5)	(2.93)	(2.53)	(2.8)	(2.31)
Log population	-0.918***	-1.046***	-0.968***	-1.185***	-0.857***	-1.239***	-0.89***	-1.314***
	(-9.25)	(-7.46)	(-9.31)	(-7.9)	(-9.52)	(-12.75)	(-9.37)	(-11.51)
Political rights	-0.16	-0.087	-0.183	-0.104	-1.826***	-1.043***	-2.286***	-1.66***
	(-1.23)	(-0.61)	(-1.39)	(-0.75)	(-5.75)	(-3.71)	(-5.67)	(-5.11)
French legal origin	-5.393***	-4.848***	-5.331***	-4.456***	-1.231***	-0.587***	-1.31***	-0.83***
	(-12.76)	(-10.42)	(-13.09)	(-9.07)	(-5.78)	(-3.39)	(-5.87)	(-4.5)
Primary religion	Omitted[1]	Omitted[1]	Omitted[1]	Omitted[1]	0.52***	0.466***	0.484***	0.215
					(3.27)	(3.4)	(2.77)	(1.39)
Constant	29.822***	32.13***	30.91***	34.153***	16.395***	23.765***	16.711***	24.658***
	(11.77)	(10.65)	(11.6)	(10.72)	(7.31)	(10.46)	(7.26)	(9.22)
Observations	172	175	172	175	256	256	256	256
R^2	0.87	0.82	0.88	0.80	0.81	0.71	0.82	0.74

This table presents estimates of OLS regression of cross-border and total M&A activity. The dependent variable is corruption perception index (CPI) for the year t and country i. To control for endogeneity, some independent variables are lagged one year. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

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Table 1.8
Robustness tests, Regional Subsamples (...cont'd)

	Asia and Oceania				Africa and Middle East			
	CPI	CPI	CPI	CPI	CPI	CPI	CPI	CPI
Log Cross-border sum per $year_{(t-1)}$	0.203***				0.038			
	(4.4)				(1.41)			
Log Cross-border Count per $year_{(t-1)}$		0.738***				0.246***		
		(7.75)				(3.04)		
Log Total sum per $year_{(t-1)}$			0.185***				0.003	
			(3.69)				(0.09)	
Log Total count per $year_{(t-1)}$				0.557***				0.195**
				(6.65)				(2.62)
Former colony	-0.273	0.22	-0.33	0.259	0.62	0.147	0.647	0.001
	(-0.77)	(0.72)	(-0.93)	(0.82)	(1.38)	(0.33)	(1.53)	(0)
Log GDP per $Capita_{(t-1)}$	0.929***	0.312**	0.954***	0.479***	0.563***	0.507***	0.65***	0.518***
	(7.34)	(2.05)	(7.24)	(3.51)	(6.01)	(5.62)	(7.48)	(5.53)
EF	1.495*	-1.156	1.746**	-0.461	-0.678	0.939	-0.527	0.935
	(1.71)	(-1.35)	(2.01)	(-0.54)	(-0.66)	(0.78)	(-0.52)	(0.85)
Oil Exporter	Omitted[1]	Omitted[1]	Omitted[1]	Omitted[1]	0.154	0.732	0.203	0.884*
					(0.33)	(1.42)	(0.45)	(1.75)
Log Government expenditure	0.063	-0.089	0.011	-0.073	0.112*	0.164**	0.144**	0.16**
	(0.4)	(-0.7)	(0.07)	(-0.53)	(1.76)	(2.25)	(2.11)	(2.14)
Log population	-0.532***	-0.746***	-0.52***	-0.682***	-0.577***	-0.862***	-0.557***	-0.922***
	(-6.77)	(-9.03)	(-6.65)	(-8.64)	(-2.77)	(-3.55)	(-2.74)	(-3.92)
Political rights	-0.018	-0.085**	-0.007	-0.024	-0.327***	-0.218***	-0.307***	-0.209***
	(-0.44)	(-2.22)	(-0.16)	(-0.68)	(-4.47)	(-3.43)	(-4.42)	(-3.49)
French legal origin	-1.142***	-0.849***	-1.23***	-0.886***	0.216	0.951	0.227	0.96
	(-6.27)	(-4.97)	(-6.88)	(-5.11)	(0.39)	(1.44)	(0.41)	(1.56)
Primary religion	0.618**	-0.18	0.764***	0.132	-0.066	-0.022	-0.094	0.136
	(2.15)	(-0.62)	(2.69)	(0.47)	(-0.21)	(-0.08)	(-0.32)	(0.5)
Constant	4.687***	13.839***	4.275***	10.857***	9.812***	13.432***	8.753***	14.392***
	(2.13)	(5.32)	(1.99)	(4.92)	(3.18)	(3.78)	(2.99)	(4.07)
Observations	212	215	215	216	113	122	120	126
R^2	0.85	0.88	0.85	0.87	0.91	0.92	0.91	0.91

This table presents estimates of OLS regression of cross-border and total M&A activity. The dependent variable is corruption perception index (CPI) for the year t and country i. To control for endogeneity, some independent variables are lagged one year. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

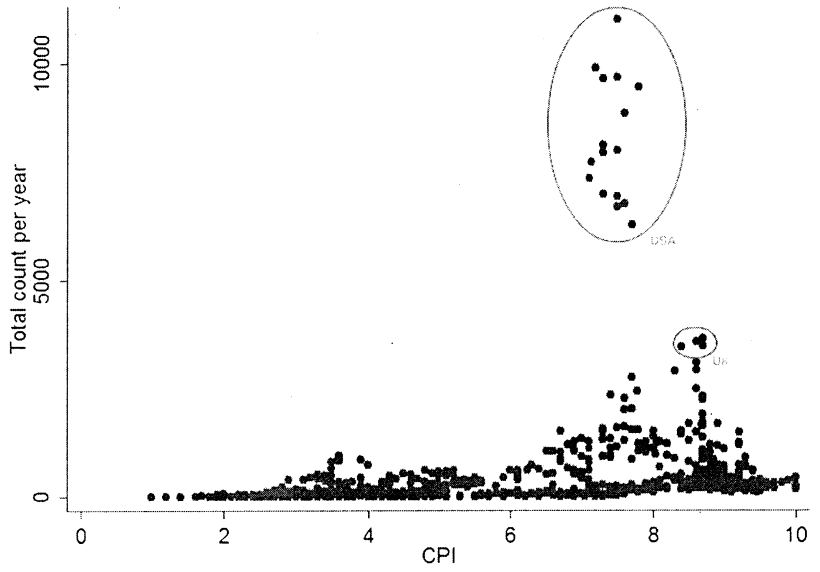
[1] The variable is omitted because of collinearity.

Except for Africa and the Middle East, all the other subsamples have positive and statistically significant coefficients for all the measures of M&A activity, which confirms the idea that M&A activity can reduce the level of corruption in these

subsamples. As for Africa and the Middle East, at least one of the two M&A activity pairs (sum or count) is statistically significant, which further confirms the results.

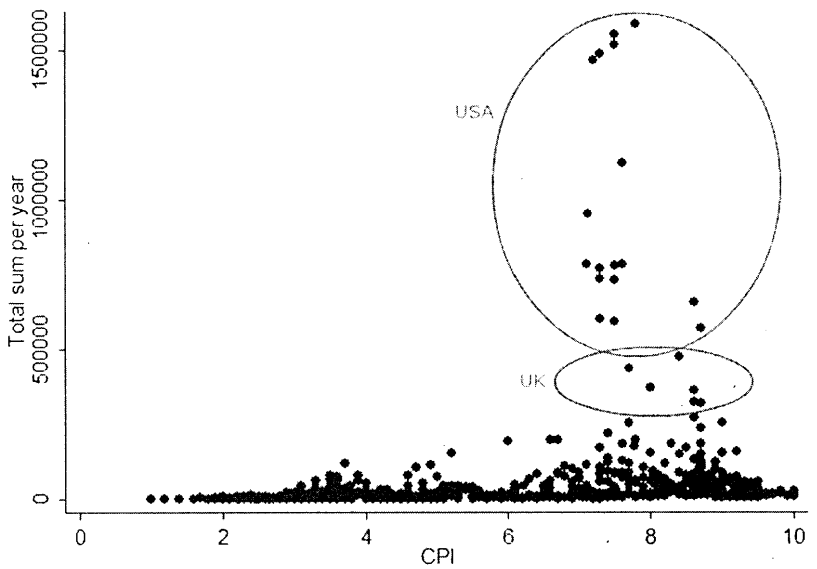
1.4.3.6 Outliers

To identify the outliers, I used a scatter plot to visually identify the possible outliers. Figure 1.2 and Figure 1.3 show the scatter plot for total count per year and total sum per year vs. CPI index. A cursory look at these graphs suggests that the United States and the United Kingdom are indeed outliers. As a robustness check, I remove these two countries from the sample data and run regressions to determine the effect of M&A activity on corruption. Table 1.9 sums up the results of random effect model panel regression. The results of this table match the previous results and support the hypothesis. In fact, these outlier countries do not affect the results.



The horizontal line represents corruption perception index and the vertical line represents the total count per year. Circled observations are noteworthy.

Figure 1.2 Scatter plot of total count per year and CPI



The horizontal line represents corruption perception index and the vertical line represents the total count per year. Circled observations are noteworthy.

Figure 1.3 Scatter plot of total sum per year and CPI

Table 1.9
Robustness tests, removing outliers

	CPI	CPI	CPI	CPI
Log Cross-border sum per year$_{(t-1)}$	0.054***			
	(3.38)			
Log Cross-border Count per year$_{(t-1)}$		0.173***		
		(3.67)		
Log Total sum per year $_{(t-1)}$			0.053***	
			(2.62)	
Log Total count per year $_{(t-1)}$				0.192***
				(3.45)
Former colony	-0.813**	-0.738*	-0.814**	-0.749**
	(-2.03)	(-1.93)	(-2.03)	(-1.97)
Log GDP per Capita$_{(t-1)}$	0.19**	0.168**	0.192**	0.13
	(2.42)	(2.01)	(2.36)	(1.61)
EF	-2.09**	-1.955**	-2.021**	-1.958**
	(-2.43)	(-2.4)	(-2.35)	(-2.43)
Oil Exporter	-1.166***	-1.04***	-1.139***	-1.016***
	(-2.99)	(-2.72)	(-2.88)	(-2.63)
Log Government expenditure	0.056	0.073	0.06	0.065
	(0.97)	(1.21)	(1.01)	(1.06)
Log population	-0.737***	-0.763***	-0.752***	-0.803***
	(-5.96)	(-6.51)	(-6.02)	(-6.56)
Political rights	-0.082*	-0.075*	-0.088*	-0.075
	(-1.67)	(-1.67)	(-1.84)	(-1.63)
French legal origin	-1.232***	-1.19***	-1.233***	-1.163***
	(-2.78)	(-2.91)	(-2.79)	(-2.83)
Primary religion	0.593	0.536	0.572	0.53
	(1.12)	(1.1)	(1.09)	(1.1)
Constant	17.659***	17.886***	17.866***	18.721***
	(7.66)	(7.82)	(7.61)	(8.05)
Observations	721	736	731	741
R^2	0.75	0.78	0.75	0.78

This table presents estimates of random effect model of cross-border and total M&A activity. The dependent variable is corruption perception index (CPI) for the year t and country i. To control for endogeneity, some independent variables are lagged one year. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

1.5 Conclusion

This paper makes a systematic attempt to estimate the effects of openness to mergers and acquisitions on corruption and addresses the issue of reverse causality by using lagged variables. I use two different measures of corruption (CPI and ICRG) and two different measures of M&A activity on a sample of 50 countries during the 1998-2013 period. Our results indicate that M&A activity is a robust determinant of corruption. More M&A activity results in lower national levels of corruption in a host country. This result is robust due to result confirmation in a series of robustness checks.

The literature has previously suggested that higher corruption levels deter foreign direct investment and mergers and acquisitions. Here I find that the opposite causality also holds; higher merger and acquisition activity is shown to deter corruption.

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APPENDIX 1.1

Definitions and expected signs of the variables

Variable Name	Definition and Source	Expected Sign
	Corruption indices:	
Corruption Perception Index	The Corruption Perceptions Index (CPI) is the index produced annually by Transparency International. This index has become a widely used measure of corruption in the literature. It is an aggregated, standardized "poll of polls" of experts, international business people, and citizens of each country covered. Every score thus captures the perceptions of both foreigners and nationals of the country being assessed. Transparency International uses a definition of corruption similar to ours: "the misuse of public power for private benefit." The index assigns a score, ranging from 0 (most corrupt) to 10 (least corrupt), to each country for each year. As of 2013, Transparency International decided to present the index ranging from 0 to 100. For simplicity the index is divided by 10 for 2012 and 2013. Source: Transparency International, various years.	
International Country Risk Guide	The International Country Risk Guide (ICRG) corruption index is an index produced by Political Risk Services. This index is a survey-based indicator, which has been widely used in the economics literature. This index is produced monthly. I use the average of the months of each year as the index for that year. The index scales from 0 to 6. Low scores on the ICRG corruption index indicate that "high government officials are likely to demand special payments". Source: Political Risk Services, various years.	
	Merger and Acquisition activity:	
Cross-border count per year	As a measure of M&A activity, I calculate the natural logarithm of the number of all cross-national deals which happened in a year for each country, whether the country was the target or the acquirer. I include only deals for which the acquirer owns less than 50% of the shares prior to transaction and owns at least 50% of the shares after the transaction. Deals with no information about before or after percentage of shares owned are excluded. The data is collected from Thomson Reuters's SDC Platinum database spanning from 1998 to 2013.	+
Cross-border sum per year	I have another measure of M&A activity, which is the natural logarithm of the sum of all cross-national deals' transaction value in US dollars, whether the country was the target or the acquirer. The deals with no information on deal value, or deals which did not make the acquirer the owner of 50% of the shares were excluded. Our data is taken from Thomson Reuters's SDC Platinum database for the years 1998 to 2013.	+
Domestic count per year	This variable is the natural logarithm of the total number of domestic M&A deals per year in a country. I excluded the deals which did not make the acquirer a controlling shareholder (more than 50% of the shares) or the deals	+

	which the acquirer was already a controlling shareholder. The data is downloaded from Thomson Reuters's SDC Platinum database.	
Domestic sum per year	This variable is the natural logarithm of the total domestic transaction value in US dollars. The deals which do not pass the ownership of 50% of the shares are excluded. This variable is downloaded from Thomson Reuters's SDC Platinum database.	+
Total count per year	I construct this variable as the natural logarithm of the total number of domestic and international deals in a country. This variable is simply a natural logarithm of the sum of Cross-border count per year and Domestic count per year.	+
Total sum per year	This variable is the natural logarithm of the total value of the cross-national and domestic deals in a country per year. The variable is the sum of Cross-border sum per year and Domestic sum per year.	+
	Control Variables:	
Former colony	is a dummy variable that takes the value of one if the country was a former colony after 1825 and zero otherwise. Source: Barro and Lee (1994).	-
Per capita GDP	is the natural logarithm of the per capita GDP in US dollars. Source: World Bank and Taiwan National Statistics.	+
Ethnolinguistic Fractionalization	Ethnolinguistic Fractionalization (EF) measures ethnolinguistic fractionalization, which is the probability that two randomly selected individuals within a country belong to the same religious and ethnic group scaling from 0 to 1. Source: La Porta et al. (1999).	-
Oil exporter	is a dummy variable for oil-exporting countries. The dummy takes the value of 1 if the country's fuel export is more than 30% of the total merchandise exports. Source: World Bank.	-
Government expenditure	is the natural logarithm of the government final consumption expenditure as a share of GDP. Source: World Bank and Taiwan National Statistics.	-
Population	is the natural logarithm of the total population of a country. Source: World Bank and Taiwan National Statistics.	-
Political rights	is the degree to which people are free to participate in the political process, freedom to vote for distinct alternatives in legitimate elections, freedom to compete for public office, join political parties and organizations, and elect representatives who have a decisive impact on public policies and are accountable to the electorate. This index is scaled from 0 to 7, where 1 denotes high political freedom. Source: Freedom House.	-
French legal origin	is a dummy variable denoting if the legal origin of the country is civil French law. Source: La Porta et al. (1999).	-
Primary religion	is a dummy variable which takes the value of 1 if the primary religion of the country is Protestant. Source: La Porta et al. (1999).	+

ARTICLE II

CORRUPTION DISTANCE AND CROSS-BORDER MERGERS

ABSTRACT

National borders can act as an extra element to be considered in the cost-benefit analysis of mergers since they are accompanied with additional sets of frictions that can hinder or motivate mergers. Corruption distance, defined as the absolute gap in the level of corruption between two countries, plays a big role in the amount and the value of bilateral mergers between country pairs. Exposure to corruption in the home country provides a learning experience, preparing potential investors to better handle corruption in the markets abroad. Thus, firms in corrupt countries tend to merge with firms in similarly corrupt countries. Conversely, firms with no experience of handling corruption at home tend to merge with firms from other clean countries. Using a large panel of 61 countries over an 18-year period, I find that corruption distance has a significant effect on merger decisions as well as on the number and value of mergers. As the corruption distance increases, I observe fewer mergers within the country pairs. I also find that acquirers in corrupt countries tend to merge with firms in countries whose corruption level is slightly better (lower) than theirs.

Keywords: Corruption, corruption distance, mergers and acquisitions.

JEL: D73, G34, F30.

2.1 Introduction

The volume of cross-border mergers and acquisitions (M&A) has been increasing over the last decade (UNCTAD 2004, 2014). In general, mergers occur when the acquiring firm's managers perceive that the value of the combined firm is greater than the sum of the values of the separate firms. In practice, most countries compete over the incentives to attract foreign investors believing that foreign investment can have significant positive effects on development. Simultaneously, governments encourage domestic firms to invest abroad for the purpose of developing a target industry. Somehow, cross-border M&A are currently the dominant policy issue for both acquirers' and target firms' home countries. However, in cross-border mergers, national borders can act as an extra element to be considered in the cost-benefit analysis because they are accompanied with additional sets of frictions that can hinder or motivate mergers. Geographic distance, cultural distance, differences in language, religion, income tax rates, and political stability along with many other factors can impede cross-border M&A. In this paper, I introduce another important issue: the impact of corruption distance on the decision and volume of M&A.

Corruption, roughly defined as the abuse of public office for private gain, is found to inhibit growth (Mauro, 1995), reduce the legitimacy of government (Anderson and Tverdorva, 2003), and deter foreign direct investment (Habib and Zurawicki, 2002; Aizenman and Speigel, 2006). Corruption distance, which is defined as the absolute gap in the level of corruption between two countries, can also play a big role in the amount and value of bilateral M&A between country pairs. In this paper, I study corruption distance as a determinant of bilateral M&A. First, I estimate the extent to which corruption distance influences the decision of firms to merge by using the Probit model. I then use panel analysis to measure the effect of corruption distance on the volume of M&A.

The rest of the paper is structured as follows. In Section 2, I review the literature and develop the hypotheses. Section 3 presents the data and methodology; Section 4 reports and discusses the empirical results; and Section 5 concludes the paper with a discussion of the most important implications.

2.2 Literature Review

Corruption plays a prominent role on the agenda of international organizations and national governments, which explains the increasing number of studies investigating the links between corruption and investment. This line of literature focuses mainly on the link between host country corruption and foreign direct investment (FDI) and asserts that corruption in the host country increases the cost of entry and acts as a barrier, reducing the profits of firms and therefore lowering a firm's incentives to invest in that country. In a seminal paper, Mauro (1995) finds that countries with higher corruption levels have low ratios of both total and private investment to GDP. Hines (1995) finds that corruption significantly reduces inward FDI. Using data of the 1990s from 12 source countries to 45 host countries, Wei (2000a) finds that corruption has a significant negative effect on FDI. Similarly, Drabek and Payne (2002) show that non-transparency, which consists of corruption, negatively impacts FDI. Sanyal and Samanta (2008) examine US FDI outflows with respect to the level of corruption in 42 host countries over a five-year period and find that US firms are less likely to invest in countries where bribery is prevalent.

2.2.1 Corruption as a market barrier to entry

Rose-Ackerman (1999) introduced a distinctive feature of corruption which is its "lock-in" effect. Once in the game, it is very difficult to get out. Firms that open their

doors to corruption may find it difficult to resist demands for bribery payments in the future. Additionally, firms with a reputation for bribing are more likely to receive demands for higher bribe payments by corrupt officials, sometimes even for the services that are normally offered for free. The threat of mutual denunciation ties the partners to each other even long after the exchange. This constant engagement in corrupt actions raises the barriers to entry in corrupt markets for foreign investors.

Host country corruption can also raise the cost of a firm's foreign investment, as (1) firms are expected to pay bribes since severe corruption has an effect similar to increasing the host country's tax rate (Wei, 2000a); (2) firms are engaged in resource-wasting, rent-seeking activities (Murphy et al., 1991; Shleifer and Vishny, 1993); and (3) firms have to accept additional contract-related risks, because corruption contracts are not enforceable in courts (Boycko et al., 1995).

In a corrupt environment, to circumvent the barrier problems and be able to gain access to that corrupt host market, international firms sometimes seek and employ brokers, middlemen, and local partners (Henisz, 2000; Javorcik and Wei, 2009; Lambsdorff, 2002). Because outside firms are not usually accustomed to such a corrupt environment, local partners can help them find their way in this environment. Javorcik and Wei (2009) show that corruption increases the advantages of having a local partner to navigate bureaucratic issues.[6] However, these advantages come at the cost of reducing the effective protection of a multinational firm's intangible assets. In addition, local firms increase the relative importance and bargaining power of the target, which can also add to the costs incurred by a company to enter a corrupt country.

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[6] Javorcik and Wei (2009) also indicate that corruption shifts the ownership structure from mergers to joint ventures.

2.2.2 Exposure to corruption at home

Exposure to corruption in the home country provides a learning experience preparing potential investors to better handle corruption in the markets abroad. Therefore, acquiring skills in managing corruption helps develop a certain competitive advantage. Andvig (2002) suggests that multinational firms exposed to corrupt environments typically have learned the organizational and financial techniques required to keep bribes and illegal transactions secret. However, this competitive advantage of expertise in managing corruption turns into a disadvantage and becomes useless in transparent markets. On the other hand, firms from countries with low levels of corruption have a comparative disadvantage in dealing with corruption, so that they face an additional challenge in conducting business in corrupt countries. Inability to handle corruption makes cross-border investment challenging for companies from less corrupt countries and can result in a negative investment decision. Therefore, multinationals from corrupt countries have a stronger tendency to invest in corrupt countries than their counterparts from less corrupt countries, and firms from cleaner countries prefer to invest in other clean countries to avoid additional costs associated with the difference in corruption levels.

2.2.3 Corruption distance and investment

Habib and Zurawicki (2002) and Wu (2006) find that the difference in corruption levels between the host and source countries is an important barrier for foreign investors. They analyze the absolute differences in perceived corruption level between the investors' home and host countries as one of the independent variables and find that similarity in overall corruption positively affects the bilateral FDI flows. In other words, companies from less corrupt countries prefer to invest in a similar

environment, and firms from corrupt countries would rather invest in similarly corrupt countries.

Corruption in a host location can be viewed from a cost/benefit perspective that will deter foreign investors if the costs of the potential deal exceed its benefits (Rose-Ackerman, 2008). This might suggest that while some firms with no experience in dealing with corruption at home might be at a disadvantage when operating in highly corrupt foreign countries, the same may not be true for firms familiar with operating in highly corrupt home countries. MNEs with knowledge of dealing with corrupt environments at home may be encouraged by their location-bound ownership advantages and willing to invest in similar locations. Thus, when analyzing how corruption affects investment, it is important to know if strategic knowledge of coping with corruption may be acquired at home by some firms and redeployed abroad without incurring high costs.

2.2.4 Corruption distance and M&A

Previous literature on the determinants of M&A mainly focuses on the economic determinants of mergers by using the gravity model[7] of trades. This line of literature argues that geographical distance between the two countries as well as the size of their economies (measured by GDP) affect the volume and intensity of mutual M&A (e.g., Di Giovanni, 2005). More recently, researchers have investigated the noneconomic determinants of mergers and have included corporate governance differences and cultural affinities in the gravity equation (Rossi & Volpin, 2004; Bris and Caboli, 2008; and Ahern et al., 2012). Ahern et al. (2012) find that culture has a

[7] The "gravity model" has been the workhorse model for trade in goods since the 1960s. It explains trade flows between two countries by the size of their economies (GDPs) and distance. See Rose (2000).

significant and economically meaningful effect on the volume of cross-border mergers and show that culturally distant countries have a lower volume of cross-border mergers. They argue that similar to the gravity literature, both physical and cultural distances should decrease the likelihood that two firms in different countries choose to merge.

In the literature, only a few empirical studies analyze the effect of corruption on cross-border M&A and simultaneously consider country-level characteristics as well as institutional attributes. Henisz (2000) and Smarzynska and Wei (2000) show that corruption affects the decision of the firm to enter a country as majority owner or to form a joint venture. Erel et al. (2012) use a sample of 56,978 cross-border mergers occurring between 1990 and 2007 to investigate the determinants of cross-border mergers. They construct an index of institutional quality by summing up corruption, law and order, and bureaucratic quality. However, they fail to show a negative link between the institution quality index and the volume of mergers. In a separate paper, Weitzel and Berns (2006) find negative effects of corruption on target premiums.

Low corruption levels indicate less risk of opportunism, which may create a favourable environment for investment. For foreign investors who are not familiar with the rules of the game in the host country, the level of corruption may be a deal breaker. But foreign investors who have experience in dealing with corruption in their home country may find the corrupt environment more favourable than a clean environment. In this paper, I contend that M&A are influenced by corruption levels in home countries as well as corruption in host countries. I define corruption distance as the absolute difference in the corruption level of home and host countries and posit that it can hinder mutual M&A the same way that cultural or geographical distances do.

The findings of this paper are consistent with the hypothesis. I find that corruption distance between two countries influences both the likelihood of mergers and the number of mergers. Corruption distance also reduces the value of mergers between two countries.

To the best of my knowledge, this is the first study that empirically analyzes the relationship between corruption distance and the volume of mergers and acquisitions. It may therefore provide new insights into corruption and may also add to the analysis of international M&A.

2.3 Data and Methodology

2.3.1 The Model

To study the effects of corruption distance on mergers, I base the methodology on the gravity model framework where bilateral trades are positively related to size of the two countries (measured by GDP) and inversely related to the geographical distance between the two. In the analysis, I also use corruption distance as one of the factors that can hinder bilateral mergers.

I use a two-stage model to investigate the effects of corruption distance along with country-specific institutional, cultural, and political variables on M&A. In the first stage, I estimate Probit models that predict the probability of an observed cross-border merger decision between a country pair as a function of corruption distance and control variables. Once a positive decision is made in the first stage, I examine the determinants of the amount of M&A to be invested in the second stage by calculating the inverse Mills ratio and include it in the second stage equation. I employ panel regression estimation to analyze the magnitude of corruption distance

effects in the second stage. In both models, I measure the effects of corruption distance of the same year on M&A activity simply because the investors take into account the corruption distance of the year that they want to invest.

The dependent variable in the Probit model equation is a dummy which takes the value 1 if there was at least one merger between the country pair in a specific year. Our variable of interest is corruption distance and I include a vector of control variables. The Probit model, which is used in the empirical analysis to test the hypotheses, is expressed as follows:

$$D_{ij,t} = \alpha + \beta \, CorDist_{ij,t} + \gamma \, X_{ij,t} + \varepsilon_{ij,t}, \quad (1)$$

Where $D_{ij,t}$ is a dummy indicator with $D_{ij,t}=1$ if there was at least one merger between country i and country j at the time t, and 0 otherwise; $CorDist_{ij,t-1}$ is the lagged corruption distance between country i and j at time t; $X_{ij,t}$ is the vector of control variables: population, GDP, GDP per capita, GDP growth, physical distance, Corruption Perceptions Index, political stability, common language, common religion, unemployment rate, disclosure quality, annual returns, and corporate income tax; β and γ are the parameters to be estimated; α is the portion of intercept that is common to all years and countries; $\varepsilon_{ij,t}$ is normal error terms with mean zero and variance σ^2_{ε}; i and j stand for the countries; and t stands for the year (t = 1,…,T).

The second stage of the analysis is random effect panel regression estimation. I use the volume and number of bilateral M&A in a country pair in a year as the dependent variable and the independent variables are the corruption distance along with control variables. The panel model used in the second stage analysis is expressed as follows:

$$Log\,(M\&A_{ij,t}) = \alpha + \beta \, CorDist_{ij,t} + \gamma \, X_{ij,t} + \omega \, Mills_{ij,t} + \lambda_t + \theta_i + \varepsilon_{ij,t}, \quad (2)$$

Where $M\&A_{ij,t}$ is the volume or the number of bilateral M&A between country i and j at the time t; $CorDist_{ij,t}$ is the lagged corruption distance between country i and j at time t; $X_{ij,t}$ is the vector of control variables: population, GDP, GDP per capita, GDP growth, physical distance, Corruption Perceptions Index, political stability, common language, common religion, unemployment rate, disclosure quality, annual returns, and corporate income tax; Mills is the inverse Mills ratio calculated from model (1); β and γ and ω are the parameters to be estimated; α is the portion of intercept that is common to all years and countries; λ_t denotes year-specific effect common to all country pairs; θ_{ij} is the country pair fixed effects; $\varepsilon_{ij,t}$ is normal error terms with mean zero and variance σ^2_{ε}; i and j stand for the countries; and t stands for the year (t = 1,…,T).

2.3.2 Control Variables

The gravity model (e.g., Hamilton and Winters, 1992) predicts that the bigger the size of the economies and the smaller the distance, the greater the bilateral international flows. There are standard control variables included in the basic gravity models. As gravity literature suggests (Hyun and Kim, 2010), I use GDP and population as proxies for the size of the economy because GDP levels measure the market size of the economy and potential demand for bilateral imports in the host country and the potential supply from the source country. Also, high GDP per capita reflects high consumption potential in the host country (Habib & Zurawicki, 2002). I utilize GDP growth as a proxy for the change in macroeconomic conditions (Rossi and Volpin, 2004). Physical distance serves as a proxy for transportation and transaction costs associated with trade and reflects the resistance to bilateral trade.

Since a common culture potentially makes mergers more likely, I additionally include a dummy variable equal to 1 if the target and acquirer share a primary religion (Same

Religion), and another dummy variable equal to 1 if they share a primary language (Same Language). Moreover, because of the possibility that international tax differences could motivate cross-border mergers, I also include the average difference in corporate income tax rates between acquirer and target countries in 1990 (Income Tax).

Country level unemployment rate has been considered a proxy for labour availability (Habib and Zurawicki, 2002) and attractiveness of the host country (Godinez and Liu, 2015). Thus, I use the host country's unemployment rate as a control variable (Unemployment Rate). Erel et al. (2012) suggest that differences in exchange rate returns as well as country-level stock returns in local currency predict the volume of mergers between specific country pairs. I include the annualized 12-month stock return difference of the country indices measured in local currency over the sample period for each country pair (Annual Returns). Unfortunately, the annual returns data are not available for all the countries and years of the sample. Furthermore, because regulatory and legal differences between countries potentially affect cross-border acquisitions (Rossi and Volpin, 2004), I include as independent variables the difference in the index on the quality of their disclosure of accounting information (Disclosure Quality).

Uncertain political situations can make investors and public officials short-term oriented and lead them to pursue personal gains while sacrificing legality. Alternatively, a stable political environment encourages a long-term orientation and reduces incentives for quick illegal returns. I include Political Stability as the measure of location attractiveness of a host country.

2.3.3 Data

The data used in this paper are generated from several datasets. First, I identify mergers and acquisitions with announcement dates between 1995 and 2013 using the Securities Data Company (SDC) Mergers and Acquisitions database. I require that the acquisition be completed and that acquirers gain more than 50% of shares of the target after the transaction. I obtain relevant data from the SDC including the acquisition announcement date and the value of the transaction. I merge the sample of acquirers and targets with the Bloomberg database to obtain financial data. Our dataset spans from 1995 to 2013. Appendix 1 summarizes the definition and sources of all the variables used in this article with their expected signs.

To analyze the cross-national patterns among acquirers and targets more formally, I use a two stage model: the Probit model and multivariate regression framework. Our goal is to measure the factors affecting the decision and the propensity of firms from one country to acquire firms from another country. Our dependent variable in the first stage is a dummy that takes the value 1 if there was at least one merger between the country pair in a year. Our dependent variable for the second stage is the number or the volume of mergers between each country pair in a year. I have 61 countries and the dataset spans from 1995 to 2013, thus the total number of potential observations is 69,540 ($61 \times 60 \times 19$).

I limit the report to the variables that are correlated with M&A. A number of indicators I collected were dropped for having no statistically significant relationship with M&A in first and/or second stage tests including sets of regional dummy variables, percentage of different religious affiliations, and British, German, Scandinavian and socialist legal origin dummy variables.

2.4 Results and Discussion

2.4.1 Descriptive Statistics

Table 2.1 presents summary statistics for the corruption index, M&A activity measures and relevant variables. Our measure of corruption, CPI, ranges from 0 to 100 with higher scores indicating lower corruption levels. The measure ranges from 6.9 in Nigeria in 1996 to 100 in Denmark in 1998 and 1999. Moreover, the measure of corruption distance ranges from 0 (e.g., between Argentina and Bulgaria in 2000) to 89 (between Finland and Nigeria in 2001). Furthermore, the geographic distance ranges from 59 kilometres, between Austria and Slovakia, to 19,772 kilometres between Colombia and Indonesia. Same language is a dummy which takes the value of 1 if any of the official languages of the acquirer country are the same as any of the official languages of the target country. Based on this definition, about 9% of the country pairs have the same official language. About 24% of the pairs have the same religion. Additionally, more than 39% of completed deals have acquirers that are more corrupt than the target countries.

Table 2.1
Summary Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
Dependent variables					
M&A Value (US$ million)	76608	107.5807	1502.39	0	205048
M&A Number	76608	1.01586	7.302513	0	361
Location-specific factors					
CPI	71505	56.15231	23.84018	6.9	100
Population	76608	7.93E+07	2.10E+08	267468	1.36E+09
GDP (US$ million)	76545	6.91E+11	1.76E+12	2.75E+08	1.68E+13
GDP PC (US$)	76545	19589.77	19526.04	263.288	112028.6
GDP Growth (%)	76104	3.536706	3.7266	-14.0983	33.73578
Annual Returns (%)	72387	0.1594779	0.640804	-0.93217	16.59867
5year Annual Returns (%)	72639	0.2331028	1.028754	-0.39843	19.28414
Corporate Income Tax (%)	36099	0.2995652	0.077784	0.125	0.567992
Unemployment Rate (%)	72639	7.603851	4.458533	0.3	27.2
Disclosure Quality (%)	47880	61.675	12.5129	24	83
Political Stability	76041	73.69768	12.11612	37	97
Composite Risk	76041	75.00025	8.865572	41	93.5
Relationship					
Corruption distance	67506	2.76563	1.956943	0	8.9
Geographical distance (kilometres)	76608	7237.8	4784.65	59.61723	19772.34
Common Language	76608	0.0892857	0.285158	0	1
Common Religion	76608	0.2395833	0.426832	0	1
Exchange rate ratio	51370	279.0581	2425.749	4.15E-06	240772.9
More-corrupt acquirer country	7535	0.3929662	0.4884418	0	1

Table 2.2 [preview on page 66, see the Table magnification on Appendix A] depicts the pairwise correlations matrix of dependent and independent variables. The two dependent variables, M&A value and M&A number, do not show a strong correlation with a correlation coefficient of 0.5293. Our measure of corruption, CPI, shows strong correlations to GDP per capita, political stability and composite risk. However, the variable of interest, Corruption Distance does not show any high correlation with any of the variables. Only the two control variables, Political Stability and Composite Risk are highly correlated; therefore, they are not used within a same model. Apart

from the aforementioned variables, all other pairwise correlations between the independent variables are not high enough to cause a possible multicollinearity problem in the model.

Table 2.2
Correlation matrix

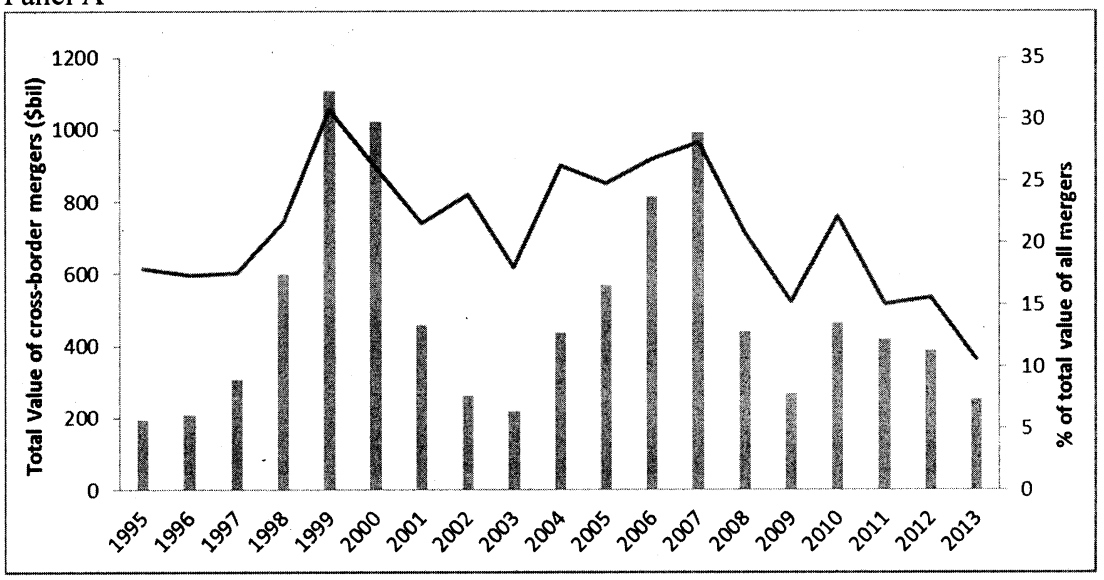
	M&A value	M&A number	CPI	Corruption distance	Population	GDP	GDP per capita	GDP growth	Geographical distance	Common language	Common religion	Unemployment rate	Disclosure quality	Annual returns	Corporate income tax	Exchange rate ratio	5year annual returns	Political stability	Composite risk
M&A value	1																		
M&A number	0.5293*	1																	
CPI	0.0607*	0.1257*	1																
Corruption Distance	-0.0482*	-0.0817*	0.0625*	1															
Population	0.0102*	0.0323*	-0.2826*	0.0012	1														
GDP	0.1237*	0.2902*	0.1554*	-0.0280*	0.2648*	1													
GDP per capita	0.0544*	0.1231*	0.7549*	0.0481*	-0.2184*	0.2165*	1												
GDP growth	-0.0112*	-0.0291*	-0.2012*	0.0300*	0.2561*	-0.0707*	-0.2675*	1											
Geographical distance	-0.0359*	-0.0799*	-0.0830*	0.0561*	0.0380*	0.0235*	-0.1334*	0.0613*	1										
Common language	0.0742*	0.1776*	0.0522*	-0.0162*	0.0418*	0.0520*	0.0267*	0.0266*	-0.0393*	1									
Common religion	0.0024	0.0166*	0.0087	-0.0911*	-0.0542*	-0.0257*	0.0316*	-0.0476*	-0.1456*	0.1312*	1								
Unemploymen t rate	-0.0158*	-0.0361*	-0.2212*	-0.0700*	-0.1432*	-0.0776*	-0.2733*	-0.1408*	-0.0517*	-0.0001	0.0653*	1							
Disclosure quality	0.0560*	0.1170*	0.6010*	0.0742*	-0.0703*	0.1939*	0.4936*	-0.0546*	-0.0400*	0.0787*	-0.0945*	-0.1672*	1						
Annual returns	-0.0081	-0.0171*	-0.0736*	0.0118*	0.005	-0.0316*	-0.0987*	0.0318*	0.0288*	-0.0027	0.0034	0.0626*	-0.1059*	1					
Corporate income tax	0.0541*	0.1029*	0.1181*	0.0451*	0.4078*	0.4258*	-0.0085	0.0296*	0.0552*	0.0445*	-0.0462*	-0.0385*	0.0969*	-0.0685*	1				
Exchange rate ratio	-0.0075	-0.0130*	-0.1466*	0.0477*	-0.004	-0.0332*	-0.0902*	0.0381*	0.0379*	-0.0221*	-0.0164*	-0.0533*	-0.0592*	-0.0001	0.0420*	1			
5year annual returns	-0.0084	-0.0177*	-0.1111*	0.005	0.0241*	-0.0203*	-0.1040*	0.0432*	0.0519*	-0.0185*	0.0220*	-0.0074	-0.1153*	0.0085	-0.1726*	-0.0108	1		
Political stability	0.0527*	0.1053*	0.8406*	0.0178*	-0.2555*	0.1619*	0.6709*	-0.1534*	-0.1205*	-0.0159*	0.0502*	-0.2006*	0.5336*	-0.0918*	0.1610*	-0.0968*	-0.0871*	1	
Composite risk	0.0451*	0.0899*	0.7891*	0.0313*	-0.1556*	0.1429*	0.6588*	0.0483*	-0.1003*	0.0067	0.0250**	-0.3193*	0.5534*	-0.0830*	0.2198*	-0.1152*	-0.1086*	0.8946*	1

* Significant at the 1% level.

2.4.2 Facts About Cross-border M&A

Mergers and acquisitions are popular around the world. Firms acquire other firms in the hope that the value of the merged firm will be more than the sum of the value of two firms. Figure 2.1 plots the value (Panel A) and the number (Panel B) of cross-border mergers over the sample period. Both panels show similar patterns. The number of cross-border mergers increases throughout the 1990s, drops after the two financial crises of 2000 and 2007, and starts to increase again as of 2009. Moreover, between 10 to 20 percent of all the mergers are cross-border. This percentage also follows the stock market. It increases in the 1990s, drops after the stock market crises of 2000 and 2007, and increases after 2007.

Panel A



Panel B

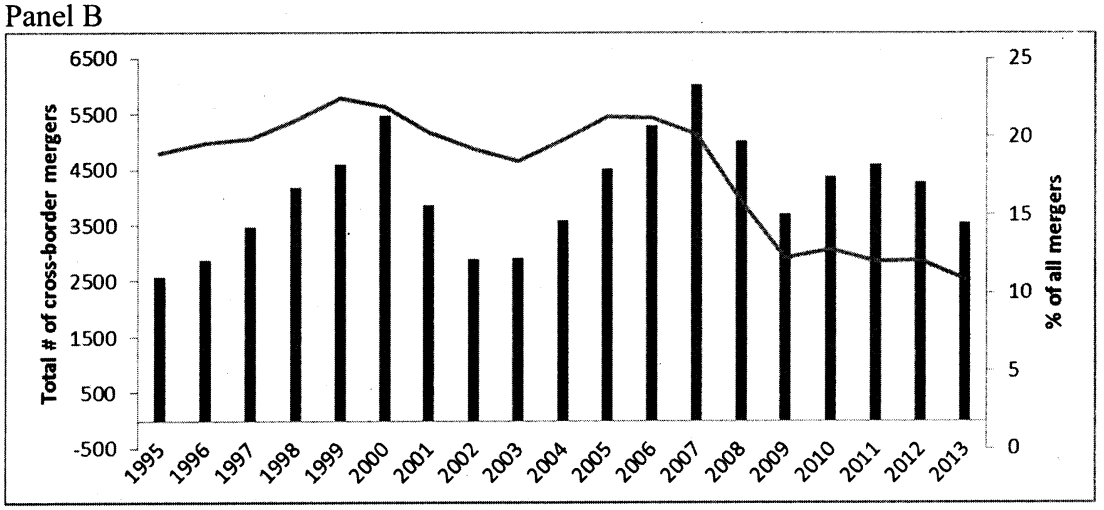


Figure 2.1 Total value and number of cross-border mergers.
This figure plots the value (Panel A) and the number (Panel B) of cross-border mergers in the sample between 1995 and 2013. Bars represent values and numbers in a given year while solid lines represent the fraction of value or number of cross-border mergers on the total (including domestic mergers) value or number of mergers in a given year.

Table 2.3 portrays the pattern of cross-border and domestic mergers for the country pairs in the sample. The columns represent the target countries while rows represent acquirers. The diagonal entries are the number of domestic mergers in a country and off-diagonal entries are the number of mergers between the corresponding country pair. The totals are reported in the right column and bottom row. Since the domestic numbers are excluded, the totals report the number of cross-border mergers in the corresponding country. The country with the largest number of mergers is the United States with 19,922 being acquirers and 13,126 being targets.

Physical distance does indeed matter for mergers. For every country, domestic mergers outnumber cross-border mergers. Moreover, neighbouring countries have more merger activity. For example, Belgium has more mergers with its neighbours (Germany, France and the Netherlands) than with the rest of the world (1534 out of 2888 total mergers). Similarly, Hong Kong has its main merger activity with China (996 merges with Chinese companies out of 2829 total mergers).

Table 2.3
Number of Mergers by Country Pair

Target Country (columns AR–JO)

Acquirer Country	AR	AU	AS	BL	BR	BU	CA	CE	CH	CO	CT	CY	CZ	DN	EQ	EG	ES	FN	FR	GE	GR	HK	HU	IC	IN	ID	IR	IS	IT	JP	JO
Argentina (AR)		1			31		1	13	2	7					3					1	1						1		3		
Australia (AU)	12		8	21	31	1	118	32	46	3	1	3	3	4	3	2		11	23	65	4	57	4		24	33	9	2	18	11	
Austria (AS)	3	8		14	7	39	8		5		28	1	62	11			3	8	32	366	2		47	1	7		5	1	40	2	1
Belgium (BL)	2	9	11		9	13	12	2	15	1			21	14		1	2	12	317	137	2	4	13		10		8	2	41	4	
Brazil (BR)	57	4	2	4			9	15	1	17			2		2				8	2		2			1			1	4	3	
Bulgaria (BU)												2	1								1		1								
Canada (CA)	66	211	20	19	87			70	74	52		5	5	13	17	6	2	26	125	110	5	45	6		13	14	15	21	23	8	
Chile (CE)	29			1	35		3			26				1	2				3	1											
China (CH)	2	57	3	2	3		40	1		3			3	2	1			1	22	40		203	4		5	8	1	3	11	38	1
Colombia (CO)	2				6		5	14							8			1	1								1				
Croatia (CT)														1						1			2								
Cyprus (CY)			2	1		9	5						9	3			3	1		10	14		2		1		2				
Czech R.(CZ)		1	3			13			1		3	1							2	17			4			1	1		1		
Denmark (DN)	6	14	11	19	15	2	21	2	10		2		10			1	8	83	51	142	3	6	2	2	7		8		24	2	
Ecuador (EQ)	1									3																					
Egypt (EG)							2						1							4											2
Estonia (ES)						1							1	2				21	1				1								1
Finland (FN)		14	14	15	9	1	18	2	12	1	1		13	56			75		39	125		4	10	1	5	1	2		28	3	
France (FR)	47	66	36	274	143	12	119	19	71	18	11	3	55	50	1	12	6	25		519	16	23	40	1	76	3	27	12	258	22	1
Germany (GE)	17	76	314	120	66	28	61	7	53		11	3	127	113	1	4	7	66	482		9	17	74		51	5	30	16	236	30	1
Greece (GR)	2		3	4		27	4		1		1	22	1	1		2	1		8	12			5			1	2		10	1	
Hong Kong (HK)	2	97	1		8	2	33		793	1		2						3	22	28					20	20	1	2	6	33	1
Hungary (HU)			4			5		1			5		7					1	2	4									3		
Iceland (IC)		1		2		2	4		2				5	35			1	7	14	5			2		3		2		1		
India (IN)	7	42	2	10	10	2	29	4	11	2	1	1	6	5		4		6	31	57		9	2			21	6	2	25	3	1
Indonesia (ID)		11			2				4									1		3		6							2	2	
Ireland (IR)	1	18	6	22	7	5	19		13	2			7	11			2	6	30	50	1	1	4		1			5	13	5	
Israel (IS)		3	1	4	10	3	20		4			1	7	4				3	21	36	2	4	5	1	2		1		12	5	1
Italy (IT)	18	11	23	24	44	10	23	5	12	4	9		14	10	1	4	2	13	194	162	6	2	13		9		7	2		5	
Japan (JP)	5	63	9	14	31		32	4	80	1	1		6	12		3		8	56	88		41	2		40	36	6	2	29		
Jordan (JO)									2							3				1									1		
Luxembourg (LX)	3	5	8	24	3	7	8		5	1		2	8	8		1	1	5	95	113	4	5	4		3	1	5	2	47	3	
Malaysia (MA)		66	1		3		8		36					2		3			2	12		178		1	26	80	1	1	2	7	
Mexico (MX)	19	2	1	2	34		10	7	1	21				1	4	2			1	6					1	1					
Netherlands (NT)	25	56	30	291	35	17	62	14	37	8	9	7	61	64	3	4	2	48	280	514	9	10	37		33	15	23	5	124	20	
New Zealand (NZ)	1	241	1	1	1		11	3	2	1				1					6	8		2					3		2		
Nigeria (NG)																				1											
Norway (NO)	1	16	5	10	13	3	21	7	4			3	7	165			15	66	30	60	1	4	5	2	8	2	10		9	2	
Pakistan (PA)																						1									
Peru (PE)	5				1		6	15		10					7														1		
Philippines (PH)		5			1		4	2	4		1									1		10			5	1				1	
Poland (PL)		1	4	3		3	3	1			5	2	21	4			2		3	15			9				2		2		
Portugal (PO)		1	1	2	47	1	1	1	1	1	1					1		1	10	11	1				1		2		8		
Russia (RU)	1	1	11	4	4	9	11		3		2	56	17	4			10	7	10	23	4	2	5		7		4	1	15		
Singapore (SG)		122	1	6	9		13		193		1	3		3		3	1	4	12	24		174	3		56	150	2	1	3	41	1
Slovakia (SO)			1	1		1					2		19							1			4			1					
Slovenia (SV)			3			2			1		13		1						1	6	1								6		
South Africa (SA)	4	69	2	3	7		10	3	3	1			1	3				2	8	20		5	1		4	2	5		5	1	
South Korea (SK)	1	11		2		2	14		67				4	2	1	1	1		8	23		14	3		9	20	1	1	6	33	
Spain (SP)	82	11	6	13	112	2	15	53	18	29	1		11	7	6	2	2	15	135	82	4	4	6	1	10	2	5	1	79	2	1
Sri Lanka (SL)							1																		3				1		
Sweden (SW)	11	36	24	46	16	2	42	8	17	2	7		29	317	2	1	34	394	148	206	4	8	8	3	9	3	12	3	50	8	
Switzerland (SZ)	14	63	66	35	42	12	60	4	15	11	5	1	30	40	2	4	2	32	193	544	3	9	13		28	10	15	4	104	15	
Taiwan (TW)		3	2	1			3		43				1	1				2	3	8		16	1		2			1	2	21	
Thailand (TH)	1	7					3		9					1					5	2		8			2	11	2		3	2	
Turkey (TK)		2	3	1	1	6	1		1		2	3							3	10		1	4			1	1	2	9		
U.A.E (UA)	1	4	1	1	1		9		2	2		1		1		19		1	6	16	1	1	2		17	2	2		4	2	5
U.K (UK)	40	485	53	159	99	23	302	28	88	13	13	13	91	149	3	16	8	104	803	967	17	83	45	4	101	41	417	29	311	35	2
United States (US)	281	975	100	245	539	24	3567	121	530	80	9	9	120	224	22	17	15	140	1147	1772	20	252	74	9	361	34	261	292	472	306	3
Venezuela (VE)	3				2			3		6					1					1											
Vietnam (VI)		1					1		1									1				1							1		
Total	772	2890	797	1420	1524	289	4772	461	2293	327	145	144	787	1345	90	116	205	1125	4393	6432	135	1212	467	26	961	520	908	414	2055	676	22

Target Country (columns LX–VI, Total)

Acquirer Country	LX	MA	MX	NT	NZ	NG	NO	PA	PE	PH	PL	PO	RU	SG	SO	SV	SA	SK	SP	SL	SW	SZ	TW	TH	TK	UA	UK	US	VE	VI	Total
Argentina (AR)			4	1					2										10								1	17	1		100
Australia (AU)	4	30	6	18	468	1	7	2	14	17	7	8	12	59	1		56	10	29	2	14	13	9	7	5	5	282	562		6	2203
Austria (AS)	1		3	25			9	1			42	1	27	1	24	16	3	1	11		18	73			20	2	46	55		1	1081
Belgium (BL)	26		3	201	1		10			2	26	17	10	2	4	4	5	4	48		21	45	1	4	13	3	114	138			1364
Brazil (BR)			16	4	1		5		12			10	1				1		8		1	1			3		7	53	6		263
Bulgaria (BU)													6												1		1	1			14
Canada (CA)	6	6	217	48	45	3	22	2	104	8	18	12	24	10	3		38	10	33		50	33	8	3	15	3	376	3911	17	2	6085
Chile (CE)			5	2					19										7							1	1	10	2		148
China (CH)	1	6		14	8		3	2	2	1	1	1	11	29			4	9	6	1	5	4	8	4	1		26	127	1	3	732
Colombia (CO)		1	8	1					17			1															1	10	7		84
Croatia (CT)							1				1		1		1	4			1			1					2	1			17
Cyprus (CY)				3			4				13	1	773		5		1				3	1			1		6	9			882
Czech R.(CZ)				3							16		14		29	3			1		2	2			6		8	2			134
Denmark (DN)	2	1	7	43	4		141		1	2	29	4	7	4	7	2	7	3	37		274	27	2	2	4	1	118	111	2	2	1295
Ecuador (EQ)									3																			2	1		10
Egypt (EG)				1				2								2	2		2						1	5	5	3			32
Estonia (ES)				1			1				2		11								1							2			46
Finland (FN)		3	3	37	2		84				35		58	3	9	3	6	3	17		284	25	2	1	4	1	64	140			1233
France (FR)	33	7	25	166	9		35	1	1	7	89	46	62	26	14	5	31	28	311		88	158	4	8	50	5	542	692	7	6	4422
Germany (GE)	29	17	25	289	10	1	57		3	2	128	19	103	19	17	2	30	21	179	1	149	434	10	5	44	4	534	729	1	2	4889
Greece (GR)	2		2	3		1	2				5		4				3		13		2				12	1	17	11			186
Hong Kong (HK)	2	45	9	10	11		1	1	1	23		2	12	87			10	19	2	5	6	11	27	20	1	4	78	146		9	1617
Hungary (HU)				2					1		8	2	6	1	3				1			1			3		3	8			71
Iceland (IC)				6			10						2				1		4		10	2			1		43	14			179
India (IN)	1	11	6	16	3	3	2			3	5	3	11	41	1		18	4	17	15	12	14		11	2	19	136	320		4	977
Indonesia (ID)		11		1			1			1				22			1							2			2	4		1	77
Ireland (IR)	2		4	44			8				10	4	7	2	3		9	2	13		13	8	1		2	1	554	311	1		1228
Israel (IS)		1		8	2		2		1		6		6	2	1	1	3	4	9		3	15	1	2	4		40	220			481
Italy (IT)	12		6	38	1		10				26	12	23	6	9	5	11		123		24	56		1	15	1	127	147	2		1282
Japan (JP)	2	37	10	29	13		5	1		17	6	5	25	42			12	59	18	1	13	21	26	55	6	2	114	469	1	16	1574
Jordan (JO)																									3	7	2	1			20
Luxembourg (LX)		2	3	22	1		7				11	4	20	1	3		4	2	15		10	23			2	1	48	43	1		594
Malaysia (MA)			1	7	8		4	2	2	13				222			10	4	1	5	2	8	5	43	3	3	38	32		10	852
Mexico (MX)	2	1		2			2		9	3								1	16						1	1	3	100	3		257
Netherlands (NT)	11	13	25		12	5	37	2	6	6	70	21	115	13	11	5	13	13	170	2	107	67	5	7	43	4	400	427	1	6	3460
New Zealand (NZ)		1	4	3		1							1	1			1					1		2			26	40		1	366
Nigeria (NG)							1							1			1											3			7
Norway (NO)		1	1	35	3				2		16	2	15	13	3	1	1	2	15		349	14		1	2	3	116	92			1156
Pakistan (PA)																				1							1	6			9
Peru (PE)			2																2								1	2			52
Philippines (PH)		9	3	1			1		2		1			5			1					2	2	1		1	6	17		1	88
Poland (PL)	1			4									20	1	3				10		3	4			5		4	2			137
Portugal (PO)				2	1	1	1		1		6								82		1				3		14	14			218
Russia (RU)	4	1		14	1	1	1		2		3			1	2	1	2	1	10		3	12			11	4	32	43		1	361
Singapore (SG)	3	221	2	11	24	4	6	1	1	28	3		5		2		7	20	2	3	8	12	26	72	6	4	63	130		17	1507
Slovakia (SO)											2		1						1			1					1				36
Slovenia (SV)				1							1		2		1				1		1	1			1		1				44
South Africa (SA)	1	1	2	10	7	7	1		1		3		6	1				3	2	1	2	5	1	2	2	2	112	60		1	392
South Korea (SK)	1	8	3	2	2		3	2	1	1	5	1	13	8	1		2		1	1	2	1	10	3	1	1	16	105		5	423
Spain (SP)	2	9	70	33			12		29	2	25	129	11	3	1		8	4			6	11		1	10	1	98	168	10		1360
Sri Lanka (SL)														1			1											1			8
Sweden (SW)	8	3	9	94	3	2	369	1		1	48	12	58	7	5	6	16	13	53	2		51	6	3	12	1	257	308		1	2799
Switzerland (SZ)	15	9	10	85	11	2	27	1	3	1	19	17	53	14	5	2	21	12	58		51		1	2	19	5	184	397		1	2401
Taiwan (TW)		5	1	5	1				1	1				8				3			3	2		3			5	84		4	236
Thailand (TH)		4		4	3	1	2			6	1		2	12								5	2		1		8	13		10	130
Turkey (TK)				5			1				1		7				1		3		1	1					2	7	1		81
U.A.E (UA)	1	2		3			1	5					3	10	1		2	1	10	5	1	5		2	11		40	27			231
U.K (UK)	33	23	28	436	74	9	144	2	9	8	103	54	135	59	16	5	168	29	348	4	333	163	19	24	43	48		2770	3	9	9641
United States (US)	41	57	429	584	171	1	178	9	63	47	123	45	164	169	12	3	132	167	409	2	377	337	122	52	58	31	4066		37	15	19922
Venezuela (VE)				1									2															6			25
Vietnam (VI)									1				1	1								1		2				3			15
Total	246	546	952	2378	900	43	1218	37	314	200	914	433	1850	907	197	70	643	452	2109	51	2253	1672	298	345	451	175	8792	13126	105	134	

This table presents the number of mergers by country pairs in the sample period. The rows represent the country of the acquirer firms and columns represent the country of target firms.

2.4.3 Determinants of the Likelihood of Mergers

In this section, I use a Probit model to measure the likelihood of M&A decisions. Our dependent variable is a dummy which takes the value of 1 if there is at least one merger between the country pair and 0 if there are no mergers between the country pair. To better analyze the determinants of merger decisions, I use 5 models with

different sets of variables. I have variables of interest, Distance Variables, Target-specific variables and cultural variables. Our variables of interest are corruption distance and corruption of target. Cultural variables are dummies of common language and common religion. Distance variables are the absolute difference of the variable values of the two countries in a country pair. This variable set is used in Model 1 throughout the paper. Target-specific variables are the variables concerning only the target country in the country pair. This variable set is used in Model 2 throughout the paper. Model 3 uses a mix of variables from both Distance and Target-specific variables, which have been used before in the literature. To increase the observations, I delete the 3 variables of disclosure quality, annual returns, and corporate income tax in Model 4. I add corruption of target in Model 5 to test if corruption in the target country also affects the analysis.

Table 2.4 illustrates the results of Probit estimation. A number of patterns are seen that characterize the likelihood of mergers. First, corruption distance is a strong determinant of merger decisions. Corruption distance has a negative and statistically significant coefficient meaning: the likelihood of mergers decreases as corruption distance increases. This confirms the notion that firms in a clean country that have no experience in dealing with corruption at home prefer to invest in other clean countries; and since firms in a corrupt country are familiar with corruption at home, they prefer to invest in other similarly corrupt countries. Second, Geographical distance clearly matters and has strong significance in all the models. Countries with shorter distances between them have a higher likelihood of mergers. This is in line with the gravity literature. Third, the GDP of the countries is also important. GDP distance shows a significant and positive coefficient. As the distance between the GDPs increases, mergers also increase. This confirms that firms in countries with larger GDPs are willing to invest in comparably smaller countries. Finally, cultural variables, common language and common religion are significant and positive in all

the models. Countries that share a common language or religion have more merger activity.

Table 2.4
Probit analysis of the likelihood of cross-border mergers

	(1)	(2)	(3)	(4)	(5)
			Variables of interest		
Corruption distance	-0.28*** (-7.84)	-0.38*** (-33.15)	-0.32*** (-29.61)	-0.07*** (-9.35)	-0.07*** (-9.36)
Corruption of target					0.45*** (7.69)
			Distance Variables		
Geographical Distance	-0.89*** (-16.95)	-0.54*** (-30.06)	-0.57*** (-32.33)	-0.64*** (-50.76)	-0.64*** (-51.06)
GDP Distance	0.65*** (18.82)		0.51*** (31.13)	0.53*** (55.02)	0.53*** (55.09)
GDP Per Capita Distance	0.06(1.45)				
GDP Growth Distance	-0.08* (-1.69)		-0.2*** (-12.95)	-0.13*** (-12.9)	-0.13*** (-12.72)
Unemployment Rate Distance	-0.15*** (-3.31)				
Disclosure Quality Distance	-0.1* (-1.65)				
Annual Returns Distance	-0.11 (-1.58)				
Corporate Income Tax Distance	-1.66* (-1.95)				
Ave. 5year Annual Returns Distance	-0.19** (-2.21)				
Political Stability Distance	-0.05 (-0.79)				
Composite Risk Distance	-0.09* (-1.73)				
% of Trade in GDP Distance	-0.16*** (-3.93)				
Exchange rate ratio	-0.01 (-0.19)				

	(1)	(2)	(3)	(4)	(5)
		Target-specific variables			
GDP		0.55***			
		(23.3)			
GDP Per Capita		0.23***	0.17***	0.05***	-0.03
		(4.5)	(3.6)	(3)	(-1.54)
GDP Growth		0.06***			
		(2.73)			
Unemployment		0.11**	0.01	-0.05*	-0.05*
Rate		(2.19)	(0.13)	(-1.93)	(-1.88)
Disclosure		0.91***	1.44***		
Quality		(5.44)	(10.06)		
Annual Returns		-0.02(-	-0.02(-		
		0.43)	0.69)		
Corporate		-3.34***	-2.28***		
Income Tax		(-8.34)	(-6.67)		
Average 5year		0.2***	0.17***	0.07***	0.07***
Annual Returns		(3.61)	(3.31)	(6.4)	(6.67)
Political		4.96***	3.86***	0.92***	0.37**
Stability		(12.55)	(11.27)	(5.44)	(2)
Composite Risk		-4.42***	-3.65***	0.68***	0.6**
		(-8.31)	(-8.23)	(2.81)	(2.48)
% of Trade in		0.25***(4.	0.22***(4.	-0.1***(-	-0.12***
GDP		34)	31)	4.25)	(-4.94)
		Cultural Variables			
Common	1.38***	1.35***	1.32***	1.46***	1.42***
Language	(9.46)	(22.39)	(22.79)	(39.28)	(38.12)
Common	0.49***	0.08*	0.09**	0.18***	0.19***
Religion	(4.58)	(1.81)	(2.3)	(6.36)	(6.95)
		Model Summary			
Constant	-9.49***	-19.41***	-18.06***	-16.89***	-14.13***
	(-10.37)	(-12.67)	(-14.51)	(-24.36)	(-18.53)
No. Observations	3122	19245	22324	55671	55671
Prob > chi2	0	0	0	0	0
Pseudo R2	0.30	0.21	0.23	0.20	0.20

This table presents estimates of Probit analysis of the likelihood of cross-border mergers. The dependent variable is a dummy that takes the value 1 if there was at least one merger in a country pair. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

In Model 1 I include all the distance variables. Most of the variables show significant coefficients. A larger difference in GDP increases the likelihood of mergers. GDP per capita distance does not show any significance. Unemployment rate distance is also

significant and shows that firms in countries with lower unemployment rates merge with firms in countries with higher rates. Annual returns distance and exchange rate ratio does not show any significance.

Model 2 includes all the target specific variables. Higher GDP, GDP per capita and GDP growth all increase the likelihood of mergers. Target unemployment rate and disclosure quality are also significant and can increase the probability of mergers. Annual returns show no significant relation to mergers but average 5 year annual return is positive and significant, which shows that stock market long-run performance can affect merger decisions. Political stability and risk of the target also influence merger decisions.

In Model 3, I include the variables from both the distance and target-specific groups, which have been recommended by the literature. GDP distance represents the difference in GDP of the countries in the country pair. GDP growth distance shows the difference in economic prosperity of the countries in the pair. Target GDP per capita is a proxy for target country wealth. Disclosure quality, unemployment rate, annual returns, corporate income tax, average 5 year annual returns, political stability, composite risk and percentage of trades in GDP are the variables that show the characteristics of the target country. A quick glance at Model 3 indicates that all the variables are statistically significant and have the expected sign.

To increase the number of observations, in Model 4, I remove the variables that limit the sample size. Thus, target disclosure quality, target corporate income tax rate and target annual returns are excluded. The results of Model 4 are similar to those of Model 3. All the variables are significant with expected signs. I have 55,671 country pairs and a pseudo R-squared of 20%.

I add target corruption in Model 5 to analyze whether merger decisions are influenced by the corruption level of the target country. Although corruption distance strongly affects the merger decision, corruption in the target country is also a determinant of merger decision. These results mean that firms in cleaner countries are more likely to acquire firms in countries with less corruption distance and lower corruption, but firms in corrupt countries are more likely to target firms in countries with less corruption distance and higher corruption levels.

2.4.4 Determinants of Cross-border Merger Activity, Pooled OLS

I use a multivariate framework to analyze the determinants of cross-border merger activity. Our goal is to investigate the factors affecting the tendency of firms from one country to merge with firms from another country. Our dependent variable is the number of mergers that occurred in a particular country pair over the entire sample period. Out of the 69,540 country pairs, I include only 13,191 pairs with more than 1 merger over the sample period. Moreover, because of the selection bias in the sample, I calculate inverse Mills ratio for each model in Table 2.4 and I include it in the corresponding models in Table 2.5 as a control variable.

Table 2.5 contains estimates of pooled OLS regression of the sample. Model 1 includes all the distance variables, Model 2 uses all the target specific variables, Models 3, 4 and 5 include the variables that are recommended by the literature. To gain more observations, limiting variables are deleted in Model 4, and finally, I add target corruption in Model 5.

Table 2.5
Pooled Analysis of the number of cross-border mergers

	(1)	(2)	(3)	(4)	(5)
			Variables of interest		
Corruption	-0.25***	-0.36***	-0.31***	-0.08***	-0.08***
distance	(-8.98)	(-17.51)	(-21.14)	(-14.79)	(-13.66)
Corruption of					0.52***
target					(10.94)
			Distance Variables		
Geographical	-0.65***	-0.52***	-0.57***	-0.54***	-0.56***
Distance	(-14.49)	(-19.51)	(-27.15)	(-23.16)	(-24.24)
GDP Distance	0.66***		0.49***	0.45***	0.46***
	(16.77)		(22.64)	(21.05)	(22)
GDP Per Capita	-0.03				
Distance	(-1.11)				
GDP Growth	-0.1***		-0.19***	-0.13***	-0.13***
Distance	(-3.65)		(-15.13)	(-14.98)	(-15.27)
Unemployment	-0.14***				
Rate Distance	(-5.27)				
Disclosure Quality	-0.07*				
Distance	(-1.9)				
Annual Returns	-0.14***				
Distance	(-3.16)				
Corporate Income	-0.76				
Tax Distance	(-1.55)				
Ave. 5year Annual	-0.29***				
Returns Distance	(-5.96)				
Political Stability	-0.02				
Distance	(-0.51)				
Composite Risk	-0.07*				
Distance	(-1.96)				
% of Trade in	-0.18***				
GDP Distance	(-6.94)				
Exchange rate	0.01				
ratio	(0.19)				
			Target-specific variables		
GDP		0.49***			
		(15.27)			
GDP Per Capita		0.17***	0.13***	0.08***	-0.01
		(4.25)	(4.03)	(7.44)	(-0.22)
GDP Growth		0.08***			
		(4.75)			
Unemployment		0.02	-0.05	-0.11***	-0.11***
Rate		(0.33)	(-1.47)	(-5.95)	-5.97)
Disclosure Quality		1.1***	1.77***		
		(10.08)	(18.13)		
Annual Returns		0.02	-0.01		
		(1.22)	(-0.05)		

	(1)	(2)	(3)	(4)	(5)
Corporate Income		-1.42***	-0.63***		
Tax		(-4.39)	(-2.68)		
Average 5year		0.23***	0.19***	0.04***	0.04***
Annual Returns		(6.72)	(6.06)	(4.5)	(5.17)
Political Stability		3.81***	2.83***	0.27*	-0.32**
		(10.21)	(9.79)	(1.82)	(-2.14)
Composite Risk		-4.33***	-3.63***	1.01***	0.85***
		(-10.08)	(-10.79)	(5.27)	(4.47)
% of Trade in		-0.01	-0.07*	-0.34***	-0.36***
GDP		(-0.18)	(-1.83)	(-21.9)	(-22.98)
		Cultural Variables			
Common	1.04***	1.1***	1.03***	1.2***	1.19***
Language	(12.53)	(17.9)	(21.37)	(22.78)	(23.38)
Common Religion	0.13*	-0.04	0.01	0.01	0.03
	(1.83)	(-1.29)	(0.33)	(0.16)	(1.19)
Inverse Mills Ratio	0.82***	0.75***	0.81***	0.65***	0.68***
	(8.66)	(10.59)	(14.79)	(12.91)	(13.81)
		Model Summary			
Constant	-10.72***	-12.23***	-12.9***	-12.38***	-9.55***
	(-12.08)	(-7.53)	(-11.14)	(-13.97)	(-11.11)
No. Observations	1494	5665	6539	11667	11667
R^2	0.42	0.29	0.34	0.29	0.30

This table presents estimates of Pooled OLS analysis of the number of cross-border mergers. The dependent variable is the logarithm of the number of mergers within a country pair. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

A number of patterns are seen in this table. Corruption distance is strongly significant and negative in all the models. It stays significant even after adding target corruption in Model 5. As the distance in corruption increases, I observe less mergers occurring in the country pair. A closer look at Model 5 reveals that although mergers occur between similar countries in terms of corruption, target corruption is also an important matter. This can imply that acquirers seek targets in countries that have slightly better corruption levels. Geographical distance is also statistically significant and negative in all the models, meaning that country pairs which are located closer to each other have a larger number of mergers. The inverse Mills ratio is significant in all the models, which confirms sample selection bias in the data. While common

language is statistically significant in all the models, common religion does not show any significance. GDP per capita distance and corporate income tax rates are not significant in Model 1, but target GDP per capita and target corporate income tax rate are among the determinants of the number of mergers.

2.4.5 Determinants of Cross-border Merger Activity, Panel Analysis

To further extend the analysis, I use a panel analysis to investigate the effects of corruption distance on merger activity in a country pair. Panel regressions claim to provide a more robust picture and they control for country and time fixed effects. Table 2.6 reports panel analysis estimates.

Table 2.6
Panel Analysis of the number of cross-border mergers

	(1)	(2)	(3)	(4)	(5)
			Variables of interest		
Corruption distance	-0.08* (-1.92)	-0.17*** (-4.78)	-0.18*** (-6.89)	-0.07*** (-7.34)	-0.07*** (-7.55)
Corruption of target					0.3*** (4.33)
			Distance Variables		
Geographical Distance	-0.35*** (-3.97)	-0.35*** (-6.64)	-0.43*** (-9.58)	-0.61*** (-9.35)	-0.62*** (-9.51)
GDP Distance	0.38*** (4.57)		0.37*** (8.42)	0.52*** (9.18)	0.53*** (9.35)
GDP Per Capita Distance	0.01 (0.14)				
GDP Growth Distance	-0.02 (-0.93)		-0.08*** (-6.2)	-0.09*** (-7.93)	-0.09*** (-8.09)
Unemployment Rate Distance	-0.05** (-2.29)				
Disclosure Quality Distance	-0.06 (-0.99)				
Annual Returns Distance	-0.04* (-1.9)				
Corporate Income Tax Distance	0.39 (0.61)				

	(1)	(2)	(3)	(4)	(5)
Ave. 5year Annual Returns Distance	-0.11** (-2.52)				
Political Stability Distance	-0.01 (-0.25)				
Composite Risk Distance	-0.04* (-1.77)				
% of Trade in GDP Distance	-0.02 (-0.58)				
Exchange rate ratio	0.01 (0.1)				
Target-specific variables					
GDP		0.36*** (6.39)			
GDP Per Capita		0.25*** (6.21)	0.23*** (6.55)	0.17*** (12.95)	0.12*** (7.62)
GDP Growth		0.08*** (7.83)			
Unemployment Rate		-0.11** (-2.53)	-0.14*** (-3.71)	-0.1*** (-4.12)	-0.1*** (-4.14)
Disclosure Quality		0.52*** (2.7)	1*** (5.37)		
Annual Returns		-0.01 (-0.43)	-0.02 (-0.94)		
Corporate Income Tax		-0.68* (-1.7)	-0.44 (-1.31)		
Average 5year Annual Returns		0.11*** (3.3)	0.12*** (3.83)	0.04*** (4.55)	0.04*** (4.77)
Political Stability		1.89*** (3.91)	1.6*** (4.35)	0.58*** (3.25)	0.23 (1.38)
Composite Risk		-2.87*** (-5.62)	-2.19*** (-5.29)	0.39* (1.77)	0.32 (1.47)
% of Trade in GDP		0.18** (2.49)	0.15** (2.31)	-0.15*** (-4.88)	-0.16*** (-5.19)
Cultural Variables					
Common Language	0.81*** (4.16)	0.98*** (6.71)	1.04*** (8.23)	1.44*** (9.45)	1.43*** (9.65)
Common Religion	-0.07 (-0.54)	0.01 (0.04)	0.02 (0.33)	0.12*** (2.62)	0.13*** (2.84)
Invers Mills Ratio	0.11 (0.57)	0.34*** (2.95)	0.51*** (5.3)	0.92*** (7.35)	0.94*** (7.51)
Model Summary					
Constant	-6.23*** (-3.39)	-7.13*** (-3.25)	-10.34*** (-5.78)	-15.04*** (-7.58)	-13.32*** (-7.63)
No. Observations	1494	5665	6539	11667	11667
R^2	0.39	0.26	0.30	0.26	0.27

This table presents estimates of Panel analysis of the number of cross-border mergers. The dependent variable is the logarithm of the number of mergers within a country pair. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. Country and time fixed effects are included. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

In Table 2.6, I follow the models of previous tables. Model 1 includes distance variables, Model 2 uses target specific variables, Model 3 uses variables commonly used in the literature, Model 4 excludes the variables that limit the number of observations, and finally Model 5 adds target corruption.

The results are similar to those of Table 2.5. Corruption distance is negative and strongly significant for all the models even when I add target corruption in Model 5. Firms in countries with similar levels of corruption have a higher number of mergers than firms in countries with a high corruption distance. Moreover, target corruption is also a strong determinant of the number of mergers, meaning that firms prefer to acquire other firms in similar but slightly less corrupt countries than their own. Geographical distance also significantly affects the number of mergers. The greater the distance between country pairs, the fewer number of mergers. The inverse Mills ratio is statistically significant for most of the models, which confirms the sample selection bias in the dataset. GDP per capita distance, corporate income tax rates, and disclosure quality difference are not significant in Model 1, but target GDP per capita, target corporate income tax rate, and target disclosure quality are among the determinants of the number of mergers. These results imply that for acquirers, target GDP per capita, income tax, and disclosure quality are more important than their home country measures. Target average 5 year annual returns are significant, whereas target annual returns do not show any significance in all the models. This result confirms the notion that mergers are a long-term decision and acquirers take into account the long-run stock market returns of the target country rather than the short-time returns. Common language shows significance in all the models; however, common religion is not significant in some of the models.

2.4.6 Determinants of Cross-border Merger Value, Panel Analysis

Table 2.7 reports the panel analysis of determinants of merger values in US dollars. Corruption distance is a strong determinant of merger value. Not only does corruption distance affect the number of mergers between country pairs, but it also has an impact on the value of mergers in the pair. Even after adding target corruption (Model 5), corruption distance stays significant and negative. Target corruption also affects merger value in the sense that firms prefer to merge with other firms in countries with similar but slightly lower corruption levels.

Table 2.7
Panel Analysis of the value of cross-border mergers

	(1)	(2)	(3)	(4)	(5)
	Variables of interest				
Corruption distance	-0.26**	-0.37***	-0.34***	-0.12***	-0.12***
	(-2.46)	(-4.68)	(-5.35)	(-5.04)	(-4.84)
Corruption of target					0.47**
					(2.35)
	Distance Variables				
Geographical Distance	-0.36**	-0.52***	-0.57***	-0.71***	-0.72***
	(-1.97)	(-4.79)	(-6.06)	(-6.9)	(-6.83)
GDP Distance	0.6***		0.59***	0.71***	0.71***
	(3.41)		(6.07)	(7.63)	(7.56)
GDP Per Capita	-0.08				
Distance	(-1.27)				
GDP Growth Distance	-0.11*		-0.13***	-0.13***	-0.13***
	(-1.74)		(-3.81)	(-4.69)	(-4.64)
Unemployment Rate	-0.1				
Distance	(-1.24)				
Disclosure Quality	-0.11				
Distance	(-0.76)				
Annual Returns Distance	-0.1*				
	(-1.92)				
Corporate Income Tax	1.01				
Distance	(0.61)				
Ave. 5year Annual	-0.28				
Returns Distance	(-0.87)				
Political Stability	0.09				
Distance	(0.98)				
Composite Risk	-0.07				

	(1)	(2)	(3)	(4)	(5)
Distance	(-0.66)				
% of Trade in GDP	-0.02				
Distance	(-0.13)				
Exchange rate ratio	0.01				
	(1.47)				
Target-specific variables					
GDP		0.65***			
		(5.42)			
GDP Per Capita		0.39***	0.27**	0.39***	0.32***
		(2.86)	(2.3)	(8.91)	(5.94)
GDP Growth		0.14***			
		(3.23)			
Unemployment Rate		-0.25**	-0.38***	-0.12	-0.12
		(-1.96)	(-3.22)	(-1.59)	(-1.59)
Disclosure Quality		1.39***	1.92***		
		(2.94)	(4.26)		
Annual Returns		0.01	-0.03		
		(0.07)	(-0.36)		
Corporate Income Tax		-2.68***	-1.12		
		(-2.57)	(-1.24)		
Average 5year Annual		0.3*	0.24	0.07***	0.08***
Returns		(1.8)	(1.53)	(3.1)	(3.2)
Political Stability		5.82***	3.51***	0.66	0.11
		(4.53)	(3.45)	(1.15)	(0.18)
Composite Risk		-7.21***	-4.28***	0.51	0.4
		(-5.23)	(-3.94)	(0.71)	(0.55)
% of Trade in GDP		0.1	-0.03	-0.48***	-0.5***
		0.5)	(-0.14)	(-6.61)	(-6.72)
Cultural Variables					
Common Language	0.96***	0.95***	0.93***	1.48***	1.45***
	(2.75)	(3.74)	(4.15)	(6.34)	(6.28)
Common Religion	-0.27	0.05	0.11	0.13	0.15
	(-0.97)	(0.36)	(0.79)	(1.28)	(1.42)
Inverse Mills Ratio	0.46	0.84***	0.89***	1.18***	1.18***
	(1.05)	(3.08)	(3.83)	(5.4)	(5.35)
Model Summary					
Constant	5.8	1.48	-0.08	-3.65	-0.81
	(1.43)	(0.26)	(-0.02)	(-0.98)	(-0.23)
No. Observations	1143	3921	4461	7665	7665
R^2	0.23	0.11	0.12	0.15	0.15

This table presents estimates of Panel analysis of cross-border mergers. The dependent variable is the logarithm of the value of mergers within a country pair. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Distance variables do not show statistical significance (Model 1), whereas target specific variables are mostly significant. Target unemployment rate is not significant in Models 4 and 5; however, it is one of the strongest determinants of the merger activity (Table 2.6, Models 4 and 5). In cultural variables, only common language shows statistical significance. This indicates that speaking a common language not only increases the number of mergers in a country pair (Table 2.6) but also increases merger value. The inverse Mills ratio is also significant showing the sample selection bias of the dataset.

2.4.7 Determinants of Cross-border Merger Activity, Clean or Corrupt Acquirers

To further investigate the effects of corruption distance on merger activity and to better understand the behaviour of the investeors, I divide the sample into two subsamples: country pairs which the acquirer's country has a better corruption level than that of the target country (cleaner acquirer), and country pairs which the acquirer's country is more corrupt than the target's country (corrupt acquirer). I reproduce the Models 4 and 5 of Table 2.6 for each subsample. The aim of this analysis is find how clean and corrupt acquirers react to corruption distance and also to corruption in the target country. Since clean acquirers are corruption-averse and corrupt acquirers prefer corrupt countries, it is expected that target corruption should be more important for clean acquirers than the corrupt acquirers. However, corruption distance should be important for both clean and corrupt acquirers.

Table 2.8
Clean vs. corrupt countries

	(4,1) Cleaner AC	(4,2) Corrupt AC	(5,1) Cleaner AC	(5,2) Corrupt AC
		Variables of interest		
Corruption distance	-0.03*	-0.13***	0.01	-0.15***
	(-1.83)	(-10.12)	(0.59)	(-11.19)
Corruption of target			0.63***	0.95***
			(7.55)	(8.49)
Distance Variables				
Geographical Distance	-0.62***	-0.5***	-0.62***	-0.52***
	(-8.59)	(-5.74)	(-8.48)	(-6.11)
GDP Distance	0.53***	0.46***	0.52***	0.46***
	(8.42)	(5.86)	(8.23)	(6.1)
GDP Growth Distance	-0.09***	-0.08***	-0.09***	-0.08***
	(-6.45)	(-5.19)	(-6.21)	(-5.27)
		Target-specific variables		
GDP Per Capita	0.21***	0.23***	0.13***	0.11***
	(12.96)	(9.41)	(6.75)	(4.07)
Unemployment Rate	-0.1***	-0.09**	-0.1***	-0.11***
	(-3.63)	(-2.28)	(-3.68)	(-2.94)
Average 5year Annual	0.04***	0.06***	0.04***	0.07***
Returns	(3.6)	(4.22)	(3.77)	(4.23)
Political Stability	0.61***	1.51***	-0.04	0.62**
	(2.99)	(5.3)	(-0.2)	(2.2)
Composite Risk	0.75***	-0.67*	0.69***	-0.99***
	(2.9)	(-1.78)	(2.7)	(-2.66)
% of Trade in GDP	-0.22***	-0.06	-0.24***	-0.1**
	(-5.31)	(-1.46)	(-5.74)	(-2.35)
		Cultural Variables		
Common Language	1.41***	1.39***	1.36***	1.35***
	(8.48)	(6.86)	(8.29)	(7.05)
Common Religion	0.11*	0.08	0.13**	0.1
	(1.86)	(1.17)	(2.26)	(1.52)
Inverse Mills Ratio	0.9***	0.78***	0.88***	0.8***
	(6.55)	(4.48)	(6.35)	(4.72)
Model Summary				
Constant	-16.93***	-14.32***	-13.81***	-9.44***
	(-7.77)	(-5.09)	(-7.15)	(-3.7)
No. Observations	6892	4775	6892	4775
R^2	0.29	0.30	0.29	0.32

This table presents estimates of pooled analysis of cross-border mergers. The dependent variable is the logarithm of the number of mergers within a country pair. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Appendix 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Table 2.8 reports the panel analysis of determinants of number of mergers for country pairs with cleaner acquirers than targets (Models 4.1 and 5.1) and cleaner targets than acquirers (Models 4.2 and 5.3). The results are interesting. Corruption distance is less significant for cleaner acquirers than corrupt acquirers (Models 4.1 and 4.2). Distance in corruption is not a very important issue for the acquirers from cleaner countries; however, corruption distance is more important for acquirers from corrupt countries.

A closer look at Model 5.1 reveals an interesting fact. Adding target corruption to the regression analysis makes the corruption distance totally insignificant. Conversely, adding target corruption in Model 5.2 does not affect the significance of corruption distance. This means that acquirers from cleaner countries only take target corruption into consideration, but not corruption distance, whereas acquirers from corrupt countries consider both corruption distance and target corruption. This result confirms the notion that acquirers from corrupt countries tend to merge with firms in slightly less corrupt countries.

Geographical distance also counts for both corrupt and clean acquirers. All the other control variables are significant and have the expected signs except common religion. Since I have sample selection bias in the data, the inverse Mills ratio is significant.

2.5 Conclusion

This paper makes a systematic attempt to study the effect of corruption distance on M&A decisions and activity. Corruption distance is defined as the absolute difference between the corruption index of the acquirer and the target in each country pair. First I analyze the effects of corruption distance on M&A decision making by using a Probit model, and then I use a multivariate regression framework and panel analysis

to investigate the propensity of firms from one country to acquire firms from another country.

I found that corruption distance impacts merger decisions, the number of mergers, and the value of mergers in a country pair. Firms in countries that experience corruption at home tend to merge with firms in a country with similar levels corruption. I also found that acquirers in more corrupt countries tend to merge with firms in countries with slightly lower corruption levels than theirs. Geographical distance between the countries also affects the decision, number and value of mergers. Countries with a same official language also have a higher number of mergers between them. Moreover, acquirers focus on the long-term stock market returns of the target country rather than the actual returns.

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APPENDIX 2.1

Variable Name	Definition and Source
Variables of interest:	
Corruption distance	The absolute difference between the Corruption Perceptions Index (CPI) of the acquirer and the target in a country pair. The Corruption Perceptions Index (CPI) is the index produced annually by Transparency International. Transparency International uses a definition of corruption similar to ours: "the misuse of public power for private benefit." The index assigns a score, ranging from 0 (most corrupt) to 10 (least corrupt), to each country for each year. As of 2013, Transparency International decided to present the index ranging from 0 to 100. For simplicity, the index is divided by 10 for 2012 and 2013. Source: Transparency International, various years.
Target corruption	The Corruption Perceptions Index of the target. The index assigns a score, ranging from 0 (most corrupt) to 10 (least corrupt), to each country for each year. As of 2013, Transparency International decided to present the index ranging from 0 to 100. For simplicity, the index is divided by 10 for 2012 and 2013. Source: Transparency International, various years.
Distance Variables:	
Geographical distance	The logarithm of great circle distance between the capitals of countries in a country pair in kilometres. Source: CEPII (Research and expertise on the world economy, retrieved from http://www.cepii.fr/CEPII/en/bdd_modele/presentation.asp?id=6).
GDP distance	The logarithm of the absolute difference in annual GDP in 2010 US dollar values of countries in a country pair. Source: World Bank, World Development Indicators.
GDP per capita distance	The logarithm of the absolute difference in annual GDP per capita in 2010 US dollar values of countries in a country pair. Source: World Bank, World Development Indicators.
GDP growth distance	The absolute difference in annual GDP growth of countries in a country pair. Source: World Bank, World Development Indicators.
Unemployment rate distance	The absolute difference between the unemployment rates of the acquirer and the target in a country pair. Source: World Bank, World Development Indicators.
Disclosure quality distance	The absolute difference in the index created by the Centre for International Financial Analysis and Research to rate the quality of 1990 annual reports on their disclosure of accounting information. Source: La Porta et. al. (1997, 1998).
Corporate tax income rate distance	The absolute difference in income tax rates of the countries in each country pair. Source: OECD.
Annual returns distance	The absolute difference in annual stock market returns. The monthly returns are calculated from the market index of each country and are annualized to calculate the annual returns. Source: Bloomberg.
Average 5 year annual returns distance	The preceding five-year average of the absolute difference in the annual stock market returns of countries in each country pair. The monthly returns are calculated from the market index of each country and are annualized to calculate the annual returns. Source: Bloomberg.
Political stability distance	The absolute difference in political risk ratings in each country pair. The political risk rating is a means of assessing the political stability of a country on a comparable basis with other countries by assessing risk points for each of the component factors of government stability, socioeconomic conditions, investment profile, internal conflict, external conflict,

Variable Name	Definition and Source
	corruption, military in politics, religious tensions, law and order, ethnic tensions, democratic accountability, and bureaucracy quality. Risk ratings range from a high of 100 (least risk) to a low of 0 (highest risk). Source: International Country Risk Guides.
Composite risk distance	The absolute difference in composite risk ratings of the countries in each country pair. It consists of composite political, financial, and economic risk rating for a country. It ranges from very high risk (0) to very low risk (100). The higher the points, the lower the risk. Source: International Country Risk Guides.
Percentage of trades in GDP distance	The absolute distance between the percentages of trades in GDP of the companies in each country pair. Source: World Bank, World Development Indicators.
Exchange rate ratio	The exchange rate between the currencies of the two countries in each pair. Source: World Bank, World Development Indicators.
Target-specific variables:	
GDP	The logarithm of the annual GDP in 2010 US dollar values of target country. Source: World Bank, World Development Indicators.
GDP per capita	The logarithm of the annual GDP per capita in 2010 US dollar values of target country. Source: World Bank, World Development Indicators.
GDP growth	The annual GDP growth rate of target country. Source: World Bank, World Development Indicators.
Unemployment rate	The unemployment rate of the target country. Source: World Bank, World Development Indicators.
Disclosure quality	The index created by the Centre for International Financial Analysis and Research to rate the quality of 1990 annual reports on their disclosure of accounting information. Source: La Porta et. al. (1997, 1998).
Corporate income tax rate	The income tax rate of the target country. Source: OECD.
Annual returns	The annual stock market returns. The monthly returns are calculated from the market index of each country and are annualized to calculate the annual returns. Source: Bloomberg.
Average 5 year annual returns	The preceding five-year average of the annual stock market returns of the target country. The monthly returns are calculated from the market index of each country and are annualized to calculate the annual returns. Source: Bloomberg.
Political stability	The political risk ratings in the target country. Source: International Country Risk Guides.
Composite risk	The composite risk ratings of the target country. Source: International Country Risk Guides.
Percentage of trades of GDP	The percentage of trades in GDP of the target company. Source: World Bank, World Development Indicators.
Cultural variables:	
Common language	Dummy variable that takes the number 1 if any of the official languages of the acquirer are the same as any of the official languages of the target. Source: CEPII (Research and expertise on the world economy, retrieved from http://www.cepii.fr/CEPII/en/bdd_modele/presentation.asp?id=6).
Common religion	Dummy variables that take the number 1 if any of the official religions of the acquirer are the same as any of the official religions of the target. Source: CEPII (Research and expertise on the world economy, retrieved from http://www.cepii.fr/CEPII/en/bdd_modele/presentation.asp?id=6).

ARTICLE III

MEDIA CORRUPTION PERCEPTIONS AND US FOREIGN DIRECT INVESTMENT

ABSTRACT

Media play an important role in shaping people's beliefs and ideas. More specifically, media have a great influence on what we think about foreign countries. The mass media influence the way a country's citizens view the people and governments of other countries. All types of stories about foreign countries are covered in the media. Investors looking to invest abroad certainly pay attention to what is reported in the media about corruption in other countries. Since corruption plays a huge role in investment location decisions, this paper investigates the role of US media corruption perceptions on US foreign direct investment (FDI) outflows. I find that an abundance of corruption stories about a specific country can demotivate investors and reduce the amount of foreign direct investment outflows to that country.

Keywords: Corruption, Media, Foreign direct investment, investment

JEL: D73, G11, G14.

3.1 Introduction

"Whoever controls the media, controls the mind."
Jim Morrison, American poet, songwriter, and singer.

Media play an important role in shaping people's beliefs and ideas. More specifically, media have a great influence on what we think about foreign countries. Although tourism has grown rapidly in the last few decades, and people visit other countries more often, they usually depend on media stories to get information about other nations. Kunczik (1997) supports this notion, stating that "the mass media influence the way a country's people form their images of the people and governments of other countries, because it is the mass media that disseminate the greater part of the information about foreign countries" (p. 7). Media cover all types of stories about foreign countries. Investors willing to invest abroad certainly pay attention to what the media are reporting about foreign countries. Since corruption plays a huge role in investment location decisions, this paper investigates the role of US media on US foreign direct investment outflows. I construct two media-related variables to gauge the perceptions of the US media on countries' corruption: Media Corruption Perceptions of all US media and Media Corruption Perceptions of *The Wall Street Journal*. Both variables are the ratio of the number of stories that cover corruption in a specific country to the number of stories that cover trades in that country for each year. Using a panel of 46 countries spanning from 2000 to 2015, I find that the media have a huge role to play on investment location decisions. Higher Media Corruption Perceptions about a country can lead to lower US foreign direct investment outflows to that country, even after introducing the Corruption Perceptions Index in the regressions.

The paper is organized as follows. In Section 2, I review the literature and outline the analytical framework in more detail. In Section 3, I construct the data and present the

methodology. Section 4 reports and discusses the empirical results. Section 5 concludes the paper with a discussion of the most important implications.

3.2 Literature Review

In modern economies and societies, the availability of information is central to better decision-making by consumers and investors. Nearly all of that information is provided by the media including newspapers, television, and radio, which collect information and make it available to the public. Media are responsible for shaping the thoughts and the opinions about almost everything, from new fashion trends to our understanding of other countries' politics. The power of the media is so strong that they can distort and manipulate information to entrench incumbent politicians, preclude investors from making informed decisions, and ultimately undermine the markets (Djankov et al., 2003). They can also have an effect on both our conscious and subconscious. When reading, watching or listening to the media, we are bombarded by information. Even if we are not actively paying attention, this information is processed (both consciously and unconsciously) and over time, these images, sounds and ideas build patterns in our subconscious and profoundly shape the way we think about health, success, relationships, other countries, and many other things (Porter, 2004).

The first to discuss the importance of the media in shaping our thoughts is Sen (1984), who explains why India has not experienced any major famines in the post-Independence era. He observes that newspapers play an important part in making acts known and forcing catastrophes to be faced. In contrast, the lack of free media has been pointed to as a reason behind why China experienced a major famine between 1958 and 1961. As Sen (1984) clearly states, the media increases the sensitivity of people towards certain issues. When natural disasters strike, active mass media

increase the ability of citizens to monitor how much effort their representatives have put into protecting the vulnerable. Besley & Burgess (2002) test Sen's proposition empirically. Using data compiled across Indian states, they find that free media increase government responsiveness to natural shocks because media have the ability to make an issue important to the people.

Djankov et al. (2003) also build on Sen's work, analyzing the ownership structure of media and find that countries with greater state ownership of the media have lower life expectancy, a greater infant mortality rate, and less access to sanitation and health system responsiveness. The World Development Report 2002, *Building Institutions for Markets*, dedicated a chapter to the importance of media and development. The role of media has been studied in terms of its impact on government transparency and accountability (Stiglitz 2002), solving the principal (citizens)-agent (government) problem (Besley and Burgess, 2001; Besley et al., 2002), public policy (Spitzer 1993), and corporate governance (Dyck and Zingales, 2002). Additionally, many case studies have analyzed the importance of the media industry in specific countries (e.g., Gross, 1996; O'Neil, 1997; McAnany, 1980; Paletz et al., 1995; Lent, 1980). These studies provide evidence suggesting that media can be a powerful force for economic development, building sustainable societies, and social progress.

Corruption, on the other hand, is one of humanity's most ancient problems. It is generally defined as the misuse of public power for private gains. Corruption is widely seen as one of the foremost problems in developing countries (e.g., Bardhan, 1997). Common sense leads us to view corruption as an impediment to growth, development and investment. The literature that investigates the consequences of corruption posits that a high level of corruption is associated with slow economic growth and low investment. These hypotheses are supported by empirical studies. In a seminal paper, Mauro (1995) reports empirical evidence for a negative correlation

between corruption and the ratio of inward investment to gross domestic product (GDP), as well as economic growth, in a cross-section of countries. Several consequent studies broaden his results and some focus on the effects of host country corruption on foreign direct investment and find the deterrent role of corruption on inward FDI (Hines, 1995; Henisz, 2000; Wei, 2000; Habib and Zurawicki, 2001, 2002).

FDI is defined as an investment involving a long-term relationship and reflecting a long-term interest and control of a resident entity in one economy other than that of the investor. Since FDI boosts economic growth and development through technology transfers and spillovers, many countries have long-term policies to attract investors. Grosse and Trevino (1996) and Chen and Chen (1998) classify the determinants of FDI into three categories: (1) firm-specific factors, (2) location-specific factors, and (3) measures of the relationship between the source and host countries. Location factors such as market size, borrowing costs, unit labour costs, and institutional and political stability are critical for the firm's investment decision. Corruption is determined by a country's institutional and political environment; thus high levels of corruption reduce locational attractiveness and have a negative impact on investors' decision to invest. Habib and Zurawicki (2002) state that "a corrupt economy does not provide open and equal market access to all competitors. Price and quality become less important than access, since bribery takes place in secret. Payments to the host country officials do not have a market value and, hence, raise the cost of goods when compared to a competitive market. This can be a major disincentive for foreign investors" (p. 293). Host country corruption also raises the cost of a firm's foreign investment, since (1) firms are expected to pay bribes. Wei (2000a) suggests that severe corruption has an effect similar to increasing the host country tax rate; (2) they are engaged in resource-wasting, rent-seeking activities (Murphy et al., 1991; Shleifer and Vishny, 1993); and (3) they have to accept

additional contract-related risks, because corruption contracts are not enforceable in courts (Boycko et al., 1995). Likewise, Javorcik and Wei (2009) investigate the effects of host country corruption on FDI inflows and show that corruption increases the advantages of having a local partner to navigate bureaucratic issues. However, these advantages come at the cost of reducing the effective protection of a multinational firm's intangible assets. Also, corruption reduces the productivity of public inputs (e.g., infrastructure) which, in turn, decreases a country's locational attractiveness (Bardhan, 1997; Rose-Ackermann, 1999; Lambsdorff, 2003). Therefore, corruption in the host country increases the cost of entry and acts as a barrier, reducing firm profits and therefore lowering a firm's incentives to invest in the corrupt country.

There is a consensus on the detrimental effects of corruption on FDI in the literature. Hines (1995) finds that corruption significantly reduces inward FDI. Drabek and Payne (2002) investigate the effect of non-transparency, i.e., corruption, on FDI. They report that non-transparency negatively impacts FDI. Wei (2000a) finds that corruption has a significant negative effect on FDI, using data of the 1990s from 12 source countries to 45 host countries. Brada et al. (2012) study the effects of home and host country corruption on inward FDI flows and find that corrupt host countries are less likely to receive FDI inflows than less corrupt ones. Mathur and Singh (2013) find quite convincingly that corruption does play a big role in investors' decision of where to invest; the more corrupt a country is perceived to be, the less the flows of FDI to that country. Mudambi et al. (2013) also find that higher levels of corruption are associated with lower levels of FDI in a panel of 55 countries from 1985 to 2000. In another paper, Delgado et al. (2014) investigate the impact of corruption on the effectiveness of FDI on growth and find that corruption significantly reduces the effectiveness of FDI on growth.

US investors are corruption-averse. The US was the first industrial country to address the issue of corruption and bribery by implementing the Foreign Corrupt Practice Act (FCPA) in 1997. The 1999 OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions made it even harder for US investors to engage in corrupt transactions. Cuervo-Cazurra (2008) analyzes the effectiveness of laws against corruption and bribery in inducing foreign investors to reduce their investments in corrupt countries. He emphasizes the role of the FCPA and OECD convention in binding US investors and shows the high sensitivity of US investors to host country corruption. He argues that US foreign direct investment to corrupt countries has reduced drastically following the implementation of the FCPA and OECD convention. In a seminal paper, Click (2005) innovatively isolates the political risk, which includes the measure of corruption, from the total risks of MNCs. He uses US FDI data in 59 countries and finds that political risk in the host country reduces its location attractiveness for US FDI. Sanyal and Samanta (2008) also examined US FDI outflows with respect to the level of corruption in 42 host countries over a five-year period. Their analysis indicates that US firms are less likely to invest in countries where bribery, as measured by the Corruption Perceptions Index (CPI), is widespread. Oseghale and Nwachukwu (2010) use six indicators to construct a measure of the quality of institutions in the host country. While corruption is one of the six indicators, they find that the quality of the host country's institutions has a statistically significant and negative effect on outward FDI decisions by US multinationals. Bekaert et al. (2014) used corruption to construct their political risk index and identify political risk, which includes corruption, has a negative effect on US FDI.

There are numerous daily journals and newspapers that cover many stories about corruption in the US (e.g., *The Wall Street Journal*, *The New York Times*, *Chicago Tribune*, etc.). These newspapers are read by many CEOs and their consultants,

which can affect their perceptions of corruption in a foreign country and consequently their investment decisions. The media have the power to affect managers' judgment both consciously and unconsciously. By the very nature of mass media (collecting and disseminating information to people), it is probable that unconsciously (or consciously), managers are reluctant to invest in countries that are portrayed in the media as being corrupt. Our core hypothesis is as follows: The media are an important factor in managers' investment decision-making. I construct media corruption perceptions of a country by counting the number of articles containing news about that country's corruption in a given year. Then, by utilizing a panel regression model, I investigate a possible relationship between media corruption perceptions and US outward FDI towards that country.

3.3 Data and Methodology

3.3.1 Data

The data used in this paper are compiled from several datasets. I count the corruption news stories from the Factiva database. The FDI data are collected from the US Bureau of Academic Analysis, which publishes the data related to US foreign direct investment. This database provides us with detailed data about the US FDI outflows to all the countries around the world. Our dataset spans from 2000 to 2015. Table 3.1 summarizes the definition and sources of all the variables used in this article.

Table 3.1
Definitions and Sources of the Variables

Variable Name	Definition and Source
Independent variable:	
Outward FDI	This variable is the natural logarithm of total US foreign direct investment in a given year towards a country. The data is collected from the Bureau of Economic Analysis.
Media Corruption Perceptions (MCP)	
MCP_all	is the ratio of the number of stories in all US media covering corruption in a country in a year divided by the number of stories in all US media covering news about trades in that country. Data are extracted from the Factiva database.
MCP_WSJ	MCP_WSJ is the ratio of the number of stories in *The Wall Street Journal* covering corruption in a country in a year divided by the number of stories in *The Wall Street Journal* covering news about trades in that country. Data are extracted from the Factiva database.
Corruption Indices:	
CPI	The Corruption Perceptions Index (CPI) is the index produced annually by Transparency International. This index has become a widely used measure of corruption in the literature. It is an aggregated, standardized "poll of polls" of experts, international business people, and citizens of each country covered. Every score thus captures the perceptions of both foreigners and nationals of the country being assessed. Transparency International uses a definition of corruption similar to ours: "the misuse of public power for private benefit." The index assigns a score, ranging from 0 (most corrupt) to 10 (least corrupt), to each country for each year. As of 2013, Transparency International decided to present the index ranging from 0 to 100. For simplicity, the index is divided by 10 for 2012 and 2013. Source: Transparency International.
ICRG	The International Country Risk Guide (ICRG) corruption index is an index produced by Political Risk Services. This index is a survey-based indicator, which has been widely used in the economics literature. This index is produced monthly. I use the average of the months of each year as the index for that year. The index scales from 0 to 6. Low scores on the ICRG corruption index indicate that "high government officials are likely to demand special payments". Source: Political Risk Services.
Control Variables:	
Population	is the natural logarithm of the total population of a country. Source: World Bank and Taiwan National Statistics.
Geographical distance	The logarithm of great circle distance between the capitals of countries in a country pair in kilometres. Source: CEPII (Research and expertise on the world economy, retrieved from http://www.cepii.fr/CEPII/en/bdd_modele/presentation.asp?id=6).
GDP growth	The annual GDP growth rate of the target country. Source: World Bank Development Indicators.
GDP per capita growth	is the GDP per capita growth in US dollars. Source: World Bank Development Indicators.
Unemployment rate	The unemployment rate of the target country. Source: World Bank Development Indicators.
Trade intensity	The percentage of trades in GDP of the target country. Source: World Bank Development Indicators.
Common language	Dummy variable that takes the number 1 if any of the official languages of the acquirer are the same as any of the official languages of the target. Source: CEPII (Research and expertise on the world economy, retrieved from http://www.cepii.fr/CEPII/en/bdd_modele/presentation.asp?id=6).

To analyze the patterns of US FDI outflows, I use a multivariate panel regression framework. Our goal is to measure the factors affecting the level of US FDI outflows. I have 46 countries in the sample and the dataset spans from 2000 to 2015, thus the total number of potential observations is 782 (17 × 46). I limit the report to the variables that are correlated with FDI.

3.3.1.1 Media Corruption Perceptions (MCP)

Factiva allows us to search its entire database and count the articles that contain a specific word or phrase. The results can be filtered by region, date and language. To construct Media Corruption Perceptions (MCP), I use two different types of variables: the number of corruption stories about each country and the number of trade stories about each country. The number of corruption stories about each country is the yearly total count of articles that contain words like corruption, bribery, embezzlement and graft within three words of the country name. Thus, I can isolate the articles about corruption in that country for each year. However, media can focus on some countries while ignoring others. For example, in the US media, a case of corruption in China will be the subject of numerous articles covering the stories and its aftermath, while a comparable scandal in Zimbabwe will not attract the same media attention. This special media attention (Media bias) may cause errors to the analysis. To correct these errors, I use another variable, i.e., the number of trade stories about each country, which is the yearly total count of articles in the media that contain stories about trades with that country. This can measure the attractiveness of the country in the media. Media corruption perceptions (MCP) are simply the ratio of the number of corruption stories about each country over the number of trade stories about that country for each year. Similar to Tetlock et al. (2008), I require that the story mentions the country name at least once within the first 25 words, including the

headline, and the country name at least twice within the full news story. Additionally, I require that each news story contains at least 50 words.

I construct two MCPs: MCP_all is the number of corruption stories about each country in all US English media over the number of trade stories about that country in all US English media for each year, and MCP_WSJ, which is the number of corruption stories about each country in *The Wall Street Journal* over the number of trade stories about that country in the same journal for each year.

For MCP_all, I include all English-language US media sources included in Factiva's category of major news and business publications plus newswire services. Major newspapers and business publications include a large number of publications, such as *USA Today*, *The Wall Street Journal*, and *The New York Times*, among many others. Our counts of media articles include reprints or highly similar articles. This means the media coverage variables measure breadth of coverage across multiple media outlets, rather than unique news events. Moreover, even if the story principally focuses on something other than corruption, the presence of phrases such as "corruption in ..." could endorse the existence of corruption in that country and influence managerial decisions.

I begin the sample in 2000, since Factiva's news coverage in earlier years is scarcer.

3.3.2 The Model

Gravity models are traditionally used to study trade flows from source to host economies, but they are also increasingly used to study FDI flows. The gravity model is a vigorous method to estimate bilateral trade and FDI flows. The model has been a

great empirical success and presents a geographic view of trade and FDI. In its simple form, the model aims to measure trade and the FDI potential of the countries and explain the 'natural' pattern of bilateral trade and FDI flows. The main components of the model are the relative market sizes of the two economies (proxied by population) and the geographic distance between their main economic centres. Given the gravity variables, the FDI potential between two countries can be estimated. I use a panel regression model to study the effects of media corruption perceptions on FDI and the variable of interest is media corruption perceptions as one of the factors that can hinder FDI outflows. The panel model, which is used in the empirical analysis to test the hypotheses, is expressed as follows:

$$FDI_{i,t} = \alpha_0 + \beta\, MCP_{i,t} + \gamma' X_{i,t} + \lambda_t + \theta_i + \varepsilon_{i,t}, \quad (1)$$

Where $FDI_{i,t}$ is the level of US foreign direct investment to country i in year t; $MCP_{i,t}$ is the media corruption perceptions of country i in year t; $X_{i,t}$ is the vector of control variables: Corruption Perceptions Index, population, physical distance, GDP growth, GDP per capita growth, unemployment rate, trade intensity, and common language; β and γ are the parameters to be estimated; α_0 is the portion of intercept that is common to all countries and years; λ_t denotes the year-specific effect common to all countries; θ_i is the source-country fixed effects; $\varepsilon_{i,t}$ is normal error terms with mean zero and variance σ^2_ε; i stands for the country (i = 1,...,N); and t stands for the year (t = 1,...,T).

3.3.3 Control Variables

To isolate the impact of the media on management's decision to invest in a country, I control for other variables that prior studies have shown to be correlated with the

level of foreign direct investment. The source of the data and the way in which each variable is calculated are given in Table 3.1.

The gravity model (Hamilton and Winters, 1992) predicts that the bigger the masses of two countries and the closer the distance, the greater the bilateral international flows. There are some standard control variables included in the basic gravity models. As gravity literature suggests, FDI is positively influenced by the size of the host economy because large markets provide a reasonable scope for investment (Habib and Zurawiki 2002). Thus, I use the log of *population* as a proxy for country size. On the other hand, FDI is negatively affected by the physical distance between the two countries. *Geographical distance* serves as a proxy for transportation and transaction costs associated with trade and reflects the resistance to bilateral trade. High *GDP growth* is also an incentive to invest and is a proxy for the change in macroeconomic conditions (Rossi and Volpin, 2004). High *GDP per capita growth* reflects high consumption potential in the host country (Habib & Zurawicki, 2002), so positively affects FDI. Country level *unemployment rate* has been considered a proxy for labour availability (Habib and Zurawicki, 2002) and attractiveness of the host country (Godinez and Liu, 2015). *Trade intensity* measured as the trade/GDP ratio of the host country can stimulate FDI because countries open to international trade provide a good platform for global business operations. Moreover, having a *common language* can also facilitate FDI between 2 countries. I also include the *Corruption Perceptions Index (CPI)* and the *International Country Risk Guide (ICRG)* as control variables.

3.4 Results and Discussion

3.4.1 Descriptive Statistics

Table 3.2 presents summary statistics for the MCPs, US outward FDI, and other control variables. US outward FDI ranges from 29 million dollars to Sri Lanka in 2000, to 850 million dollars to the Netherlands in 2015. Number of corruption stories in all US media ranges from 0, for some European countries, to 806 stories for China in 2013. Number of country trade stories in all US media has a minimum of 150 for Zimbabwe in 2001, and a maximum of 109,341 for China in 2010. Moreover, the number of corruption stories in *The Wall Street Journal* (WSJ) ranges from 0 for some European countries to 153 for China in 2014. In addition, the number of country trade stories in the WSJ has a minimum of 4 for Zimbabwe in 2004, and a maximum of 2,370 for China in 2010. MCP_all ranges from 0 to 11% and MCP_WSJ ranges from 0 to 57%.

China, with a population of about 1.37 billion, is the most populated country in the sample, whereas Ireland, with a population of about 3.7 million, is the least populated country. The closest country to the US is Canada with a distance of 737 km between the two capitals, and the farthest country is Indonesia with a distance of 16,371 km. Same language is a dummy which takes the value of 1 if any of the official languages of the acquirer country are the same as any of the official languages of the target country. Based on this definition, about 25% of the countries have the same official language (English) as the US.

Table 3.2
Summary Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
Dependent variables					
US outward FDI (US$ million)	716	43700.6	86844.77	29	858102
Variables of interest					
No. of corruption stories in all US media	748	22.94519	53.63078	0	806
No. of corruption stories in WSJ	748	3.542781	11.43924	0	153
No. of country trade stories in all US media	748	13893.49	16024.46	150	109341
No. of country trade stories in WSJ	748	284.5027	371.7042	4	2370
MCP_all	748	0.0034065	0.007915	0	0.1107754
MCP_WSJ	748	0.0190703	0.047292	0	0.5714286
Corruption indices					
Corruption perception index (TI)	745	55.61274	24.80127	10	100
Corruption index (ICRG)	656	3.248349	1.386093	0	6
Control variables					
Population	745	9.89E+07	2.51E+08	3805174	1.37E+09
Geo-distance	748	8864.192	3868.962	737.0425	16371.12
GDP growth	745	3.195366	3.730606	-17.66895	33.73578
GDP per capita growth	735	2.071069	3.541073	-18.87482	30.34224
Unemployment rate	703	7.399972	4.346269	0.7	27.2
Trade intensity rate	725	86.07494	73.63405	20.25789	455.2767
Common language	748	0.2566845	0.4370961	0	1

Table 3.3 depicts the pairwise correlations matrix of the dependent variable, variables of interest, and control variables. The dependent variable, US outward FDI, does not show a strong correlation with any other variables. Number of corruption stories in all US media has a strong correlation with Number of corruption stories in the WSJ, which was expected. MCP_all and MCP_WSJ do not seem to have a strong pairwise correlation. Most of the control variables do not have a strong correlation with the other variables, with the exception of the two corruption indices (CPI and ICRG), which have a strong correlation and are not used together in a regression. Apart from the aforementioned variables, all other pairwise correlations between the independent

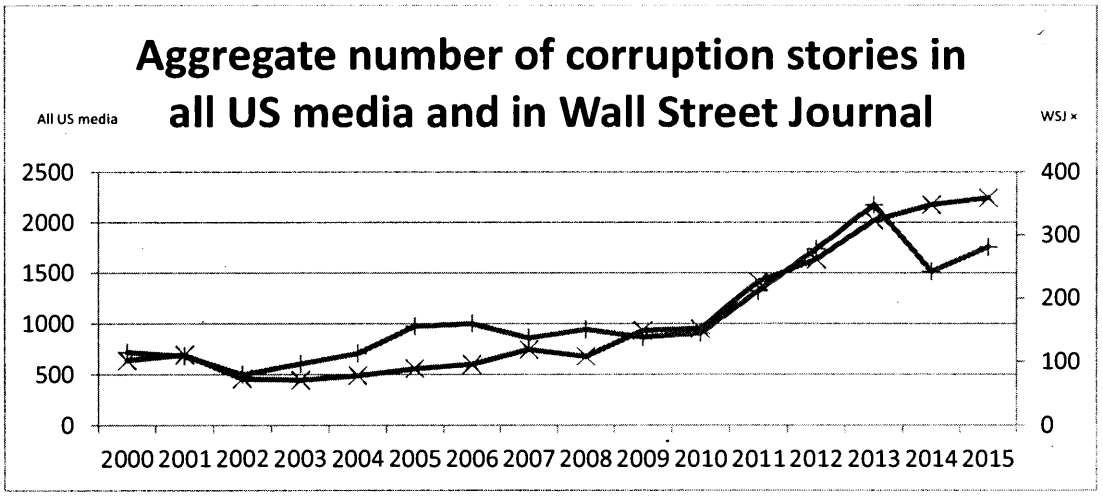
variables are not high enough to cause a possible multicollinearity problem in the model.

Table 3.3
Correlation matrix

	US outward FDI (US$ million)	No. of corruption in all US media	No. of corruption in WSJ	No. of specific country in all US media	No. of specific country in WSJ	MCP_ all	MCP_ WSJ	Population	Geo-distance	GDP growth	GDP per capita growth	Un-employ-ment rate	Trade intensity rate	Corruption perception index (TI)	Corruption index (ICRG)	Common language
US outward FDI (US$ million)	1															
No. of corruption stories in all US media	0	1														
No. of corruption stories in WSJ	-0.0096	0.9041	1													
No. of country trade stories in all US media	0.4004	0.3495	0.3281	1												
No. of country trade stories in WSJ	0.1712	0.4092	0.4384	0.6971	1											
MCP_all	-0.1445	0.2485	0.1203	-0.1925	-0.1312	1										
MCP_WSJ	-0.1325	0.2598	0.3031	-0.0838	-0.1072	0.4261	1									
Population	-0.0513	0.5508	0.6038	0.3623	0.5481	0.0437	0.1027	1								
Geo-distance	-0.2139	0.064	0.1343	-0.0339	0.0532	-0.0302	0.0715	0.1844	1							
GDP growth	-0.1289	0.1382	0.137	-0.0142	0.0678	-0.0219	0.0494	0.3121	0.2519	1						
GDP per capita growth	0.4252	-0.1922	-0.1653	0.2511	0.0794	-0.3216	-0.2908	-0.2686	-0.2101	-0.3111	1					
Unemployment rate	-0.1327	-0.0777	-0.0906	-0.1038	-0.1231	0.0007	-0.0449	-0.1466	-0.1108	-0.1189	-0.2057	1				
Trade intensity rate	0.1948	-0.1021	-0.0622	0.0362	-0.0196	-0.1131	-0.0901	-0.1808	0.2696	0.0597	0.2602	-0.2281	1			
Corruption perception index (TI)	0.3712	-0.2407	-0.1907	0.2141	0.1287	-0.4121	-0.3615	-0.279	-0.0609	-0.2402	0.8125	-0.19	0.3683	1		
Corruption index (ICRG)	0.3472	-0.2441	-0.2081	0.1787	0.0651	-0.4034	-0.347	-0.2569	-0.1053	-0.2064	0.7406	-0.1362	0.2243	0.9018	1	
Common language	0.1007	0.0115	-0.0038	0.1653	0.0119	-0.0222	0.0348	0.1044	0.3458	0.1718	0.0217	0.0504	0.2876	0.1192	0.0393	1

3.4.2 Facts About the Variables of Interest

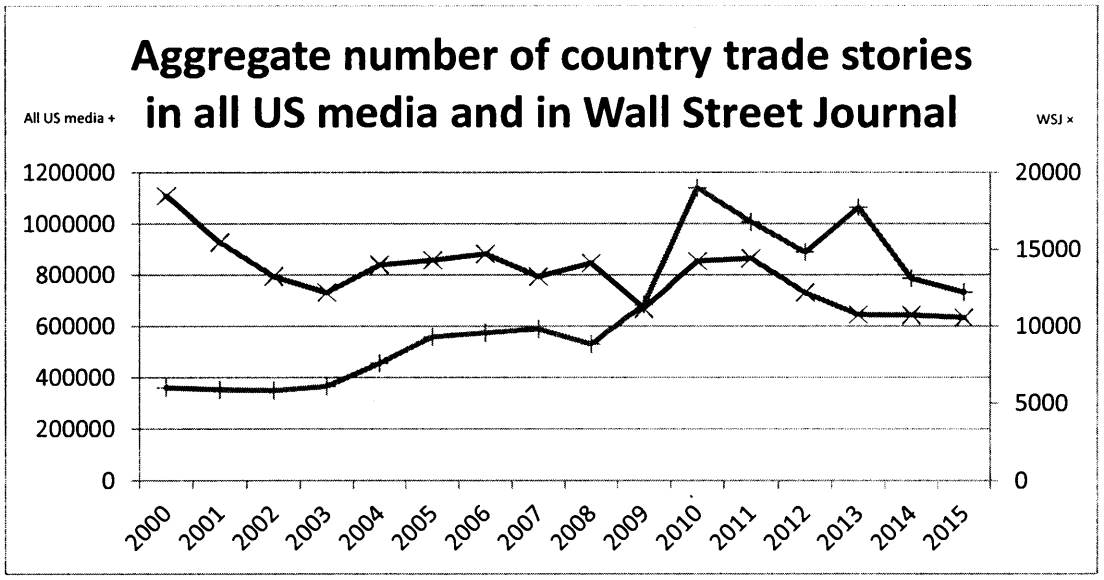
Figure 3.1 plots the aggregate number of corruption stories in all US media (marked by +) and the aggregate number of corruption stories in the WSJ (marked by ×) over the sample period. The number of corruption stories in all US media stays stable until 2010, when I see a sharp increase until it peaks in 2013 with a total number of 2,174 US media stories covering corruption in the countries of the sample. In addition, the number of corruption stories in the WSJ also follows the same pattern; it is stable until 2010 and then it increases sharply in 2015.



This figure plots the aggregate number of corruption stories in all US media (+) and Wall Street Journal (×) in the sample between 2000 and 2015.

Figure 3.1 Aggregate number of corruption stories in all US media and in Wall Street Journal

Figure 3.2 plots the aggregate number of country trade stories in all US media (marked by +) and the aggregate number of country trade stories in the WSJ (marked by ×) over the sample period. The number of country trade stories in all US media has increased throughout the sample period. However, it peaked in 2010. In contrast to the aforementioned trend, the number of country trade stories in the WSJ has decreased over the sample period. Interestingly both measures have a peak in 2010.



This figure plots the aggregate number of country trade stories in all US media (+) and Wall Street Journal (×) in the sample between 2000 and 2015.

Figure 3.2 Aggregate number of country trade stories in all US media and in Wall Street Journal

3.4.3 Determinants of Foreign Direct Investment, Panel Analysis

To analyze the effects of media corruption perceptions on US outward foreign direct investment, I use a multivariate regression framework. Our goal is to investigate how media perceptions of a country's corruption can affect the level of US FDI towards that country. Because I am interested in the effects of media corruption perceptions on FDI and how changes in these perceptions can influence outward FDI, I use a panel analysis. Our dependent variable is the level of FDI towards receiving country and the variables of interest are the MCP_all and MCP_WSJ. I also use several control variables that are suggested by the literature as a determinant of outward FDI.

Table 3.4 presents random effect panel regression estimates of the determinants of US outward FDI as represented by media corruption perceptions (MCP_all and

MCP_WSJ). The results are revealing. Models 1, 2 and 3 illustrate that MCP_all is a strong determinant of US outward FDI. The coefficient of MCP_all is very significant in all the models and has the expected signs. An increase in the MCP_all (having more stories about corruption in a country) reduces the amount of FDI towards that country. In Model 2, I add the Corruption Perceptions Index as a control variable. I observe that the coefficient of MCP_all stays significant even after taking into account corruption in the target country. CPI is also strongly significant and the positive sign shows that when the index increases (higher values show less corruption), I observe that US FDI towards that country also increases. In Model 3, I use the ICRG as the corruption index. The results are the same as in Model 2. MCP_all stays significant and negative, while ICRG is significant and positive. Although the corruption index is a determinant of FDI, the media perception of corruption in a country also plays a big role on the amount of US outward FDI towards that country. For Model 2, there are 657 observations and R-squared equals 19%.

Table 3.4
Panel Analysis of the outward US foreign direct investment

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Variables of interest							
MCP All	-9.304***	-8.217***	-10.882***				
	(-3.61)	(-2.77)	(-4.1)				
MCP WSJ				0.234	-0.03	0.055	
				(0.22)	(-0.03)	(0.05)	
Corruption indices							
CPI		0.026***			0.026***		0.026***
		(2.6)			(2.86)		(2.63)
ICRG			0.14**			0.128*	
			(2.04)			(1.79)	
Control variables							
Geographical Distance	-1.465***	-1.307***	-1.362***	-1.492***	-1.351***	-1.382***	-1.363***
	(-2.75)	(-2.95)	(-2.84)	(-2.67)	(-2.83)	(-2.74)	(-2.81)
Population	1.732***	1.661***	1.542***	1.822***	1.807***	1.607***	1.836***
	(5.97)	(6.23)	(5.87)	(6.38)	(6.93)	(6.23)	(6.43)
GDP Growth	-0.048	-0.05	-0.041	-0.045	-0.047	-0.04	-0.045
	(-0.8)	(-0.86)	(-0.7)	(-0.74)	(-0.79)	(-0.67)	(-0.79)
GDP per capita Growth	0.034	0.036	0.029	0.033	0.034	0.03	0.033
	(0.56)	(0.61)	(0.48)	(0.55)	(0.58)	(0.5)	(0.57)
Unemployment rate	-0.011	-0.005	-0.013	-0.01	-0.004	-0.012	-0.004
	(-0.79)	(-0.37)	(-0.97)	(-0.69)	(-0.28)	(-0.9)	(-0.27)
Trade Intensity	0.006**	0.007***	0.006**	0.006**	0.006***	0.006**	0.006***
	(2.52)	(2.71)	(2.24)	(2.5)	(2.68)	(2.25)	(2.67)
Common Language	0.673	0.446	0.631	0.689	0.469	0.645	0.475
	(0.61)	(0.48)	(0.64)	(0.59)	(0.47)	(0.62)	(0.47)
Constant	5.82	4.191	7.755	4.449	2.036	6.791	1.649
	(0.83)	(0.66)	(1.22)	(0.63)	(0.32)	(1.07)	(0.24)
Observations	660	657	621	660	657	621	657
R^2	5.29%	18.28%	8.67%	4.28%	14.78	6.88%	14.18%

This table presents random effect estimates of Panel analysis of the US foreign direct investment outflows. The dependent variable is the logarithm of the amount of US foreign direct investment towards each country. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Table 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Models 4, 5 and 6 show MCP_WSJ as the variable of interest. The variable is not significant in any models; however, it has the expected sign. Although *The Wall Street Journal* is an influential source of information for investors, its stories covering corruption all around the world are not powerful enough to solely sway foreign direct investment.

As expected in the gravity models, geographical distance is also statistically significant and negative in all the models, meaning that countries located closer to the United States receive larger numbers of US FDI. Moreover, population is significant, and a larger population attracts more FDI. GDP growth and GDP per capita growth are not significant in all the models, and it seems that investors do not pay attention to GDP growth or GDP per capita growth. Unemployment rate is not significant in all the models. Political stability shows a little bit of significance, meaning that investors prefer not to invest in countries that are not politically stable. In addition, having a common language with the US is not significant.

3.4.4 Determinants of Foreign Direct Investment, Pooled Analysis

Here I use a multivariate framework to analyze the determinants of US outward FDI to a country. Our goal is to investigate the factors affecting the tendency of investors to invest in another country. Our dependent variable is the dollar amount of US outward FDI to a particular country over the entire sample period.

Table 3.5 contains estimates of pooled OLS regression of the sample. Models 1, 2 and 3 include MCP_all as the variable of interest and in Models 3, 4 and 5 I have MCP_WSJ as the variable of interest. I add Corruption Perceptions indices to Models 2, 3, 5 and 6. In Model 7, I use only the control variables without including the variables of interest.

Table 3.5
Pooled Analysis of the outward US foreign direct investment

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Variables of interest							
MCP All	-83.98***	-46.973***	-60.072***				
	(-4.68)	(-4.94)	(-5.93)				
MCP WSJ				-10.098***	-3.481**	-6.564***	
				(-6.49)	(-2.38)	(-4.46)	
Corruption indices							
CPI		0.051***			0.056***		0.058***
		(15.35)			(15.83)		(16.94)
ICRG			0.595***			0.68***	
			(9.4)			(9.75)	
Control variables							
Geographical	-1.105***	-0.971***	-1.056***	-1.059***	-0.949***	-1.017***	-0.963***
Distance	(-11.36)	(-10.75)	(-9.95)	(-10.5)	(-10.16)	(-9.39)	(-10.22)
Population	0.514***	0.965***	0.808***	0.513***	0.998***	0.845***	0.992***
	(11.21)	(19.75)	(14.36)	(10.78)	(19.96)	(14.53)	(19.93)
GDP Growth	-0.609***	-0.095	-0.306***	-0.773***	-0.143*	-0.382***	-0.151*
	(-7.3)	(-1.08)	(-3.59)	(-9.53)	(-1.69)	(-4.47)	(-1.78)
GDP per capita	0.54***	0.052	0.248***	0.724***	0.115	0.339***	0.126
Growth	(6.15)	(0.57)	(2.78)	(8.07)	(1.33)	(3.81)	(1.46)
Unemployment rate	-0.066***	-0.019*	-0.042***	-0.064***	-0.013	-0.037***	-0.009
	(-5.52)	(-1.93)	(-3.73)	(-4.93)	(-1.2)	(-3.08)	(-0.82)
Trade Intensity	0.01***	0.008***	0.01***	0.01***	0.008***	0.01***	0.008***
	(9.84)	(12.46)	(11.86)	(9.33)	(12.22)	(11.76)	(12.15)
Common Language	0.698***	0.069	0.43***	0.848***	0.085	0.492***	0.055
	(4.97)	(0.49)	(2.9)	(5.83)	(0.6)	(3.2)	(0.4)
Constant	24.808***	12.114***	16.696***	24.39***	10.941***	15.318***	10.978***
	(25.55)	(9.95)	(11.56)	(23.81)	(8.43)	(9.91)	(8.38)
Observations	660	657	621	660	657	621	657
R^2	45.89%	63.70%	54.70%	38.97%	61.07	51.04%	60.66%

This table presents estimates of Pooled OLS analysis of the US foreign direct investment outflows. The dependent variable is the logarithm of the amount of US foreign direct investment towards each country. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Table 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

The results are the same as the panel data analysis. MCP_all is strongly significant and negative, meaning that covering more stories about corruption in a country reduces US foreign direct investment to that country. The coefficient of MCP_all stays strongly significant even after adding the corruption indices to the equation in Models 2 and 3. This means that although corruption in the target country (measured

by the CPI or ICRG) is important for the investors, stories about corruption in that country covered by the media have a bigger influence on their decision. Corruption in the target country is also a strong and significant determinant of FDI. In addition, the gravity model suggests that geographic distance and population affect the mutual investment between two countries. Table 3.5 proves this claim. Both geographical distance and population are strongly significant and have the expected signs. GDP growth and GDP per capita growth are significant in some of the models. Unemployment rate is also significant in some of the models. Moreover, trade intensity shows a strong significance, and common language is significant in some models. The R-squared varies between 38 and 63 percent. And I have around 660 observations for the models.

3.4.5 Determinants of Foreign Direct Investment, Regional Dummy Interactions

To check the robustness of the results, Table 3.6 includes regional dummy interactions with the variables of interest. I have five regional dummies: South America, Europe, Asia, the Middle East and Africa. North America is omitted to avoid multicollinearity. Table 3.6 presents the estimates of Pooled OLS analysis of US foreign direct investment outflows to specific regions. The dependent variable is the logarithm of the amount of US foreign direct investment towards each country. The variables of interest are MCP_all and MCP_WSJ. Because I include the regional dummy interactions, I have to interpret the coefficients of the interaction variables with respect to the variable of interest. The coefficients of MCP_all are positive and strongly significant in all the models. However, the coefficients of interaction variables are negative and strongly significant for South America, Asia, the Middle East and Africa. The coefficients of interaction variables of Asia, the Middle East and Africa are smaller than the MCP_all. This means that the overall effect of media corruption perceptions is strong, negative and significant in Asia, the Middle East and

Africa. The coefficients of MCP_WSJ are positive and significant for Models 3 and 4. However, the interaction variables are negative and significant for South America, Asia, the Middle East and Africa. The coefficients of these regions are smaller than the coefficient of MCP_WSJ in respective models, which means that overall media corruption perceptions have a negative and significant effect on US FDI. The only regional dummy interaction variable that shows no significance is the interaction variable of Europe. As mentioned earlier, Europe is considered a corruption-free region by the media, and there is no corruption coverage in most of the European countries in the sample. This is the reason why the coefficient of Europe dummy interaction is not significant. Corruption indices stay positive and strongly significant in all models.

Table 3.6
Pooled Analysis of the outward US foreign direct investment, Regional dummy interactions

	(1)	(2)	(3)	(4)
Variables of interest				
MCP All	232.066***	137.36***		
	(3.39)	(3.01)		
MCP WSJ			42.596***	35.049***
			(3.16)	(3.51)
Corruption indices				
CPI	0.053***		0.056***	
	(15.41)		(15.57)	
ICRG		0.596***		0.69***
		(9.65)		(10.04)
Regional dummy interactions				
South America	-194.589***	-170.394***	-40.32***	-37.926***
	(-2.87)	(-3.67)	(-3)	(-3.8)
Europe	-112.617	47.268	-18.493	-5.81
	(-1.26)	(0.46)	(-1.26)	(-0.45)
Asia	-299.642***	-248.296***	-47.532***	-46.502***
	(-4.35)	(-5.21)	(-3.51)	(-4.62)
Middle East	-300.98***	-207.166***	-38.35***	-25.821**
	(-4.15)	(-3.55)	(-2.61)	(-2.31)
Africa	-278.753***	-194.246***	-48.801***	-41.466***
	(-4.16)	(-4.4)	(-3.66)	(-4.23)
Control variables				
Geographical	-0.824***	-0.928***	-0.884***	-0.916***
Distance	(-9.02)	(-8.8)	(-8.86)	(-8.23)
Population	1.001***	0.851***	0.988***	0.857***
	(18.29)	(13.67)	(18.6)	(13.74)
GDP Growth	-0.091	-0.29***	-0.161*	-0.405***
	(-1)	(-3.31)	(-1.83)	(-4.73)
GDP per capita	0.049	0.231**	0.14	0.369***
Growth	(0.53)	(2.53)	(1.56)	(4.12)
Unemployment rate	-0.018	-0.047***	-0.013	-0.043***
	(-1.64)	(-4)	(-1.15)	(-3.45)
Trade Intensity	0.008***	0.01***	0.008***	0.011***
	(12.08)	(11.99)	(11.57)	(11.67)
Common Language	0.145	0.529***	0.149	0.572***
	(1.01)	(3.47)	(1.04)	(3.73)
Constant	9.92***	14.754***	10.459***	14.151***
	(7.21)	(9.49)	(7.43)	(8.45)
Observations	618	621	618	621
R^2	65.37%	55.99%	62.51%	52.71%

This table presents estimates of Pooled OLS analysis of the US foreign direct investment outflows to specific regions. The dependent variable is the logarithm of the amount of US foreign direct investment towards each country. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Table 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

Table 3.7 includes regional dummy interaction with the variables of interest, but omits the MCP_all and MCP_WSJ. In Models 1 and 2, I include the regional dummy interactions with MCP_all and in Models 3 and 4 I have the regional dummy interactions with MCP_WSJ. The results of Table 3.7 further confirm the results. The coefficients of interaction dummies in Models 1 and 2 are significant and negative for Asia, the Middle East and Africa. In Models 3 and 4, the coefficients for Asia and Africa are negative and significant. Moreover, corruption indices stay positive and significantly strong in all the models. The results suggest that media corruption perceptions are a strong determinant of US FDI outflows.

Table 3.7
Pooled Analysis of the outward US foreign direct investment, Regional dummy interactions only

	(1)	(2)	(3)	(4)
Corruption indices				
CPI	0.053***		0.056***	
	(15.33)		(15.43)	
ICRG		0.59***		0.685***
		(9.56)		(9.92)
Regional dummy interactions				
South America	29.571	-37.085*	1.764	-3.268
	(1.2)	(-1.93)	(0.7)	(-1.34)
Europe	114.457**	181.128**	23.433***	28.652***
	(1.97)	(2.02)	(3.59)	(3.37)
Asia	-70.989***	-112.609***	-5.168*	-11.599***
	(-3.34)	(-4.52)	(-1.79)	(-4.04)
Middle East	-74.53**	-73.111*	3.908	8.919
	(-2.2)	(-1.73)	(0.61)	(1.54)
Africa	-48.429***	-57.827***	-6.436***	-6.608***
	(-4.5)	(-5.84)	(-5.23)	(-4.26)
Control variables				
Geographical Distance	-0.887***	-0.964***	-0.94***	-0.962***
	(-9.7)	(-9.36)	(-9.37)	(-8.76)
Population	1.012***	0.859***	1.002***	0.869***
	(18.44)	(13.84)	(18.8)	(13.93)
GDP Growth	-0.079	-0.281***	-0.151*	-0.396***
	(-0.87)	(-3.22)	(-1.72)	(-4.63)
GDP per capita Growth	0.034	0.22**	0.127	0.358***
	(0.36)	(2.42)	(1.42)	(4.02)
Unemployment rate	-0.022**	-0.049***	-0.017	-0.045***
	(-2.05)	(-4.24)	(-1.43)	(-3.67)
Trade Intensity	0.008***	0.01***	0.008***	0.011***
	(12.29)	(12.09)	(11.8)	(11.83)
Common Language	0.133	0.519***	0.143	0.564***
	(0.92)	(3.37)	(0.98)	(3.65)
Constant	10.376***	14.982***	10.778***	14.398***
	(7.55)	(9.63)	(7.61)	(8.57)
Observations	618	621	618	621
R^2	65 %	55.86%	62.08%	52.43%

This table presents estimates of Pooled OLS analysis of the US foreign direct investment outflows to specific regions. The dependent variable is the logarithm of the amount of US foreign direct investment towards each country. Variables MCP_all and MCP_WSJ are not used in this table. Heteroskedasticity-corrected t-statistics are in parentheses. The variable definitions are provided in Table 1. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively.

3.4.6 Determinants of Foreign Direct Investment, Percentile Analysis

In the next robustness test, I conduct the percentile analysis for the determinants of US FDI outflows, as shown in Table 3.8. I use 10^{th}, 50^{th} and 90% percentiles, and I separately include the two corruption indices in the models. For the 10^{th} and 50^{th} percentiles, I observe the same results as in the other tables: MCP_all and MCP_WSJ are negative and strongly significant; corruption indices have the expected signs and are significant and positive. However, for the 90^{th} percentile in Models 3 and 9, I observe that a corruption perceptions indice's t-values decrease and even lose its significance in Model 12, meaning that in the 90^{th} percentile of media corruption perceptions (all media), news about corruption of a country is more important and more significant than the corruption index per se. Model 6 and Model 12 exhibit different patterns. In Model 6 in the 90^{th} percentile, MCP_WSJ loses its significance, while CPI remains significant. This can show that the corruption perceptions of only one media source is not an important determinant of US FDI outflows in comparison to MCP_all, which represents the corruption perceptions of all media. However, Model 12 contradicts Model 6. The coefficient of ICRG loses its significance while MCP_WSJ stays negative and significant. The contradiction between the two models can arise from two things. First, the CPI (Corruption Perceptions Index) is widely used and trusted in measuring countries' level of corruption, whereas the ICRG is less known and not as widely used in the cost benefit analysis of investment projects. Since the CPI is more trusted by the US industry, it can be a stronger determinant of US FDI than MCP_WSJ (Model 6). However, the ICRG is less used and therefore loses its significance in comparison to MCP_WSJ in Model 12. Second, the number of observations is too small for both models (43 vs. 37). Thus, the small number may be causing a sample selection bias, creating contradictory results in the two models.

Table 3.8
Pooled Analysis of the outward US foreign direct investment, Percentile analysis

	(1) (10^{th} percentile)	(2) (50^{th} percentile)	(3) (90^{th} percentile)	(4) (10^{th} percentile)	(5) (50^{th} percentile)	(6) (90^{th} percentile)
Variables of interest						
MCP All	-49.029***	-44.532***	-			
	(-4.71)	(-4.1)	36.733***			
			(-3.05)			
MCP WSJ				-5.901***	-6.592***	-8.702
				(-4.22)	(-4.4)	(-1.53)
Corruption indices						
CPI	0.049***	0.05***	0.042***	0.054***	0.056***	0.042**
	(13.63)	(9.23)	(4.03)	(11.77)	(9.54)	(2.57)
ICRG						
Control variables						
Geographical	-0.932***	-0.881***	-0.952***	-0.805***	-0.777***	-0.792***
Distance	(-10.05)	(-6.39)	(-4.29)	(-7.09)	(-6.06)	(-2.76)
Population	0.885***	0.946***	0.883***	0.665***	0.743***	0.831***
	(17.03)	(13.12)	(6.22)	(9.99)	(9.24)	(4.83)
GDP Growth	-0.208**	-0.226*	-0.208	-0.171	-0.146	-0.496
	(-2.31)	(-1.78)	(-0.48)	(-1.51)	(-1.11)	(-1.55)
GDP per capita	0.173*	0.177	0.215	0.145	0.129	0.459
Growth	(1.87)	(1.38)	(0.5)	(1.24)	(0.95)	(1.39)
Unemployment rate	-0.021**	-0.016	-0.036	-0.018*	-0.021*	-0.038
	(-2.02)	(-1.01)	(-1.06)	(-1.79)	(-1.71)	(-1.3)
Trade Intensity	0.008***	0.008***	0.008***	0.005***	0.005***	0.007**
	(10.56)	(8.06)	(4.08)	(5.69)	(4.99)	(2.54)
Common Language	0.092	0.201	-0.157	-0.301*	-0.15	0.35
	(0.63)	(0.94)	(-0.25)	(-1.84)	(-0.72)	(0.72)
Constant	13.555***	11.906***	14.224***	16.449***	14.707***	14.588***
	(10.85)	(6.54)	(3.95)	(9.46)	(7.09)	(2.96)
Observations	563	319	62	307	218	43
R^2	65.77%	65.41%	72.95%	69.17%	70.14%	72%

	(7) (10^{th} percentile)	(8) (50^{th} percentile)	(9) (90^{th} percentile)	(10) (10^{th} percentile)	(11) (50^{th} percentile)	(12) (90^{th} percentile)
Variables of interest						
MCP All	-62.236***	-59.862***	-			
	(-5.59)	(-4.92)	48.175***			
			(-3.69)			
MCP WSJ				-9.111***	-10.833***	-13.323**
				(-5.56)	(-4.89)	(-2.44)
Corruption indices						
CPI						
ICRG	0.575***	0.539***	0.386**	0.714***	0.688***	0.355
	(8.48)	(5.23)	(2.1)	(7.84)	(6.3)	(1.62)
Control variables						
Geographical	-0.978***	-0.914***	-1.208***	0.714***	-0.821***	-0.661**
Distance	(-9.16)	(-5.99)	(-3.38)	(7.84)	(-4.64)	(-2.22)
Population	0.736***	0.809***	0.761***	0.714***	0.617***	0.771***

	(7)	(8)	(9)	(10)	(11)	(12)
	(10^{th} percentile)	(50^{th} percentile)	(90^{th} percentile)	(10^{th} percentile)	(50^{th} percentile)	(90^{th} percentile)
	(12.44)	(9.18)	(5.05)	(7.84)	(7.12)	(3.66)
GDP Growth	-0.402***	-0.446***	-0.452	0.714***	-0.357**	-0.617
	(-4.53)	(-3.5)	(-1.09)	(7.84)	(-2.24)	(-1.66)
GDP per capita	0.348***	0.372***	0.425	0.714***	0.334**	0.546
Growth	(3.73)	(2.82)	(1)	(7.84)	(2.05)	(1.42)
Unemployment rate	-0.044***	-0.042**	-0.058	0.714***	-0.045***	-0.056
	(-3.73)	(-2.32)	(-1.55)	(7.84)	(-2.98)	(-1.61)
Trade Intensity	0.009***	0.01***	0.01***	0.714***	0.006***	0.007**
	(9.93)	(7.5)	(2.92)	(7.84)	(4.34)	(2.3)
Common Language	0.419***	0.471**	0.208	0.714***	0.257	0.828
	(2.69)	(2.05)	(0.32)	(7.84)	(1.01)	(1.66)
Constant	17.618***	15.893***	19.995***	0.714***	18.518***	15.984***
	(12)	(7.03)	(5.36)	(7.84)	(7.87)	(2.9)
Observations	529	297	60	285	196	37
R^2	58.43%	57.60%	63.88%	61.94%	62.07%	69.56%

3.5 Conclusion

The media are a powerful tool to shape and form our ideas about almost anything. They can change the way I think about a foreign country, its people and its situation. Media also affect investors who want to invest abroad. They are affected by both the news stories about a country's corruption and the abundance of these stories. This study analyzes the effect of US media news stories that cover corruption in a country on US foreign direct investment outflows to that country. I study the effect of having many news stories covering corruption in a specific country on the volume of US foreign direct investment towards that country. I construct two variables related to news stories: MCP_all, which is the ratio of the number of stories in all US media covering corruption in a country in a year divided by the number of stories in all US media covering news about trades in that country; and MCP_WSJ, which is the ratio of the number of stories in *The Wall Street Journal* covering corruption in a country in a year divided by the number of stories in *The Wall Street Journal* covering news about trades in that country. I use a panel of 46 countries over a 16-year period to test

the hypotheses. I find that both MCP_all and MCP_WSJ are strong determinants of US foreign direct investment. Even after introducing corruption indices in the regressions, the two media corruption variables stay strong and significant. This further confirms the hypotheses that the media have a significant impact on foreign investment.

Our results also confirm previous studies on this subject. Brada et al. (2012) study the effects of host country corruption on inward FDI flows and find that corrupt host countries are less likely to receive FDI inflows. Mathur and Singh (2013) find that corruption does play a big role in investors' decision of where to invest, stating that corrupt countries receive less flows of FDI. Mudambi et al. (2013) also find that higher levels of corruption are associated with lower levels of FDI. I also find that corruption gauged by the perception of foreign country corruption by the US media, has a negative and significant effect on investment decisions and the amount of FDI outflows by the United States.

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GENERAL CONCLUSION

Corruption is widely viewed as one of the foremost problems in developing countries (e.g., Bardhan, 1997). Common sense dictates that corruption be viewed as an impediment to growth, development and investment. The literature that investigates the consequences of corruption posits that a high level of corruption is associated with slow economic growth and low investment. These hypotheses are supported by empirical studies. In a seminal paper, Mauro (1995) reports empirical evidence for a negative correlation between corruption and the ratio of inward investment, GDP, as well as economic growth, in a cross-section of countries. Several consequent studies broaden his results and some focus on the effects of host country corruption on foreign direct investment (FDI) and find the deterrent role of corruption on inward FDI (Hines, 1995; Henisz, 2000; Wei, 2000; Habib and Zurawicki, 2001, 2002). These papers argue that corruption in the host country increases the cost of entering a country and thus acts as a market barrier. However, the relationship also goes in the other direction: FDI can introduce new norms and policies to the corrupt environment and decrease the level of corruption.

Mergers and acquisitions (M&A), joint ventures, green-field investments, licensing agreements, etc. are all various forms of FDI. Foreign investors have their choice of FDI when they want to enter a new economy. Although there are many studies that investigate the effect of corruption on foreign direct investment, the literature on the effect of corruption on M&A is scarce. As the largest component of foreign direct investment, mergers and acquisitions are expected to be negatively affected by

corruption. Weitzel and Berns (2006) are among the few who have examined such a relationship and add depth to the understanding of the familiar negative relationship between FDI and corruption. They find that higher corruption in the host country is associated with lower target premiums. They also show that corruption is a market barrier to entry and is a discount on merger synergies. In a separate study, Javorcik and Wei (2009) find that corruption in the host country shifts ownership from whole ownership to joint ventures, and that investors prefer to form a joint venture rather than merge when they want to enter a corrupt country. On the other hand, M&A activity, as the most important part of FDI, can lead to a less corrupt environment since M&A can introduce new strategies, tactics and policies.

Essay one investigates the effects of M&A activity on the corruption level of the host country. Our hypothesis is that cross-border M&A activity can introduce new norms and strategies to the target companies. Competition and domestic mergers can help the spread of these new norms to the environment, which can lead to a less corrupt environment. I test this hypothesis on a sample of 50 countries over a 16-year period, and I empirically find that M&A activity (both domestic and cross-border) can decrease a country's level of corruption. I utilize different methods to check the robustness of the results. I use an alternate measure of corruption; I divide the sample to regional sub samples; I use panel and pooled regressions; and finally I use longer lags. The results of the robustness tests confirm the hypothesis.

Essay two studies the effect of corruption distance on the M&A activity between country pairs. Corruption distance is defined as the absolute gap between the two countries engaging in M&A activity: the acquirer and the target. The literature provides empirical evidence that the amount of M&A activity between the acquirer and the target depends on the geographical distance between the two countries, on their masses, and on some target-specific factors such as corruption. Exposure to

corruption in the home country provides a learning experience, preparing potential investors to better handle corruption in markets abroad. Therefore, acquiring skills in managing corruption helps develop a certain competitive advantage. Andvig (2002) suggests that multinational firms exposed to corrupt environments typically have learned the organizational and financial techniques required to keep bribes and illegal transactions secret. This competitive advantage of expertise in managing corruption turns into a disadvantage and becomes useless in transparent markets. On the other hand, firms from clean countries have a comparative disadvantage in dealing with corruption, so they face an additional challenge in conducting business in corrupt countries. Inability to handle corruption makes cross-border investment challenging for companies from less corrupt countries and can result in a negative investment decision. Therefore, this essay hypothesizes that companies from corrupt countries have a stronger tendency to invest in corrupt countries than their counterparts from less corrupt countries, and firms from cleaner countries prefer to invest in other clean countries to avoid additional costs associated with the difference in corruption levels. I test the hypotheses utilizing a Probit model, in a sample of 61 countries over a 19-year period, to investigate whether corruption distance has an effect on M&A decisions, and then I use a panel model to gauge the effect of corruption distance on the number and value of M&A between country pairs. The results empirically confirm the hypotheses. Corruption distance has a negative effect on the M&A location decision and also has a negative effect on the number and volume of M&A between country pairs. I also find that firms in corrupt countries prefer to merge with companies in similarly corrupt countries whose corruption levels are slightly lower than theirs.

Essay three looks at corruption from a different angle. I gauge the media's opinion about corruption in a country by constructing Media Corruption Perceptions in the US. I then study their effects on US foreign direct investment outflows to that

country. To construct such a variable, I count the number of US media stories that cover corruption in a specific country, and to construct a standardized variable, I discount it by the number of US media stories that cover trades in that country. Since the media have a great impact on how I view other countries, this essay hypothesizes that Media Corruption Perceptions have a negative effect on outward US foreign direct investment towards that country. I test the hypothesis by using a panel of 46 countries spanning from 2000 to 2015, and I empirically find that Media Corruption Perceptions are a strong determinant of US foreign direct investment, even after introducing the Corruption Perceptions Index in the equation. Media bombard us with all sorts of stories about foreign countries and can affect our decisions both consciously and unconsciously. The abundance of stories covering corruption in foreign countries can have an impact on the managers' decision to invest in another country.

This thesis aims to study the mutual relationship between corruption and investment. Investment activity can reduce corruption in a country, whereas corruption can also negatively impact inward investment.

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