

# Literature Review: Economic Analysis of Internet Enterprise M&A Motivation

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**Abstract:** With the Internet industry is becoming more mature and quickly into the mobile Internet era, the Internet business restructuring, transformation, merger becomes more and more realistic. On the one hand, each Internet companies should pay attention to the rational allocation of mobile terminal resources, on the other hand, face new market and technology needs in the future, Internet companies pay more attention to the strategic layout of the product. New investment, mergers and acquisitions, alliance cooperation and other means have become the Internet companies of frequent use of border expansion. This paper mainly analyzes the existing theories of mergers and acquisitions.

## 1. Introduction

China's Internet industry started in the late 90s and early 1980s, after a few years, the Internet, especially mobile Internet began to develop rapidly. According to the China Internet Network Information Center in August 3, 2016 released the thirty-eighth China Internet development statistics report shows that China's expansion of network scale, by the end of June 2016, China netizens reached 710 million, Internet penetration rate reached 51.7%. Visible, information and network are changing and subvert our lives, the Internet industry can be said to be the most dynamic and potential development of today's industry.

According to the clear Research Center released the "2015 annual China mergers and acquisitions Market Research Report" shows that in 2015 the domestic mergers and acquisitions to disclose the amount of a total of 2090 cases from the year rose 63.7%, in which the scale of mergers and acquisitions, Internet companies ranked first, 304 merger cases. Therefore, Internet mergers and acquisitions have become increasingly frequent, the amounts involved are larger than other industries, however exactly what mechanism, what factors drive the Internet companies continue to choose mergers and acquisitions strategy are worthy of our in-depth analysis.

## 2. Research on the theory of M & A Motivation

The traditional explanation of the theory of M & A is mainly from the perspective of management theory, the research of economics also has the basic explanation from the level of the enterprise itself or the manager.

### 2.1 Efficiency theory

Efficiency theory explains the M & A from the perspective of management. In the early 1980s, Jensen and Ruback (1983) as a representative of a group of scholars believe that access to efficiency is the main reason to promote mergers and acquisitions. This source of efficiency can be the difference between acquiring company and Target Corp management efficiency. When the acquiring company management efficiency than high management efficiency of the Target Corp, the merger of two companies to improve management efficiency of Target Corp and acquiring company to the same level, so the enterprise management efficiency obtained from the value added.

Another source of efficiency in M & A is from the economic considerations, the enterprises can obtain the synergistic effect in some form, This synergy can be allocated to a larger fixed cost, so as to reduce the average unit cost. Also from the economies of scale and scope, horizontal merger,

enterprises can choose to reduce the unit cost of production technology or organizational structure, re allocation of resources or sharing complementary resources, and improve the innovation ability of the enterprise and market coverage. Grossman, Hart and Moore (1986) put forward the incomplete contract theory to explain the efficiency sources of vertical merger. When there is an important complementary relationship between the assets of the enterprise, vertical merger can effectively reduce the problem of security and lack of funds. Waston (2004) also believes that in mergers and acquisitions, due to the presence of financial synergies, tax may be a strengthening factor, rather than the main force affecting mergers and acquisitions.

## **2.2 Agency theory**

Jensen and Mecking (1976) first proposed the agent theory, think that when managers shareholding ratio is small, it will produce managers to the agency problem of public favoritism. Fama and Jensen (1983) believe that We can control the agency problem by setting up the compensation mechanism and separating the ownership and management rights. When these mechanisms are not enough to control the agency problem, the executive members and ownership structure will be changed through the open acquisition or proxy contention. Manne also stressed that, if the poor performance of the agency or because of poor business performance, then M& A mechanism makes the threat of takeover has always existed.

## **2.3 Transaction cost theory**

Coase (1973) first proposed the concept of transaction cost in the nature of the firm. Later, Coase (1960) refined the transaction cost into the cost of finding the price, bargaining, signing the contract and supervising the strict performance of the contract terms. Arrow (1975) argues that horizontal mergers can reduce costs by merging sales outlets and functional departments, and vertical mergers can reduce the cost of negotiation and transaction costs, thereby achieving economies of scale. Houston, James and Ryngaert (2001) through the analysis of the United States and the banking industry mergers and acquisitions from 1985 to 1996, mergers and acquisitions motivation to reduce transaction costs.

## **2.4 information theory**

According to the theory of information, if the acquirer's management has the advantage of obtaining the internal information of a target enterprise, it is found that the market value of the target enterprise is undervalued. The main advantage of this information asymmetry, through mergers and acquisitions to obtain benefits, namely leveraged buyout. Usually, when a company is bought and sold, the market will assume that the value of the firm is undervalued, or that the company's future cash flow will increase, and the market will respond to it, pushing up stock prices. If the acquisition of information is leaked in advance, it will cause mergers and acquisitions business unprofitable. Dodd and Ruback (1977) and Bradley (1980) study shows that the acquisition is successful or not, will make the enterprise stock price overall upward trend, because the acquisition of behavior to the market show that, before the target enterprise's stock price is undervalued, more exaggeration to say that even if the target enterprise without any improvement the market will also be re evaluating the price.

## **2.5 Transitional confidence hypothesis**

Roll (1986) explains the merger and acquisition from the perspective of managers' behavior. Think managers always overestimate their business ability, in the assessment of future earnings generated by Target Corp too optimistic, in the acquisition of low income, or even when there is no return to make acquisitions. If the overconfidence hypothesis is established, then the excessive payment of the acquisition of the company will transfer the interests of its shareholders to the shareholders of the target company. Most of the empirical studies show that mergers and acquisitions of listed companies fell, while the acquisition of enterprises can not provide similar data M.Bradley (1980). Therefore, there is still a lack of consistent conclusions for the full support of overconfidence hypothesis. However, the overconfidence hypothesis provides us a new way to understand the

phenomenon of mergers and acquisitions.

## **2.6 Market power theory**

That market forces theory, M & A can increase the merger in the market to market forces, merger competitors can reduce the competition within the industry, therefore, mergers can control or influence the market price, high profit. If the takeover strengthens the anti competitive effect and increases the market price of the product, the competitor should also benefit from the merger. According to this view, Eckbo (1983) examines the stock reaction of competitors at the time of the merger announcement, which results in the rejection of the market power hypothesis, while Mullin et al (1995) confirms the existence of market forces in subsequent studies. It can be seen that there is no consistent conclusion on the empirical evidence of market forces.

## **2.7 Redistribution theory**

The redistribution theory suggests that mergers and acquisitions will make the redistribution of interests between owners and stakeholders, this is a pure interest flow, and did not bring value-added. Benefits may from creditors into shareholder, or from the general staff, the tax authorities in the hands of the owners to.,this is also the source of tax effect. The enterprise can expand the asset depreciation, carry forward the loss, credit the taxable amount through the merger and acquisition, or replace the ordinary income with the asset income.

## **2.8 An empirical study on the motives of some mergers and acquisitions**

Berkovitch and Narayanan (1993) Through empirical research to investigate the correlation between the total income of the merged enterprise and the M & A, that Synergy、agency costs and mixed overconfidence hypothesis can explain the acquisitions in a certain extent. Gugler (2003) analysis of the last 15 years through mergers and acquisitions to distinguish the increase in profit of mergers and acquisitions and reduce profits on mergers and acquisitions, and increased sales for further distinction can be displayed about merger & acquisition. If the profit and sales increased at the same time, then the merger motivation is to increase efficiency; if the increase in profits and sales decline, then the merger is the motivation of market power; if the decline in profits and sales at the same time, so the acquisition is not successful. Hien et al. (2013) analyzed the sample of the United States of America, found that the merger and acquisition of the market timing of the 73%, while the study shows that there are many reasons for the merger of 80%, it is difficult to explain with a theory.

## **3. Research on the motivation of Internet enterprise merger and acquisition in China**

The domestic research on the motivation of mergers and acquisitions of Internet companies are mainly single angle for the acquisition of specific behavior analysis, and cannot explain the activity of mergers and acquisitions of all Internet companies, Internet companies also ignore the traditional enterprises with economic attribute and space-time change relationship. Ruan Fei (2011) that the motivation of China's Internet acquisitions are mainly the following five points: user preference to pursuit of increasing returns to scale, the Matthew effect, promote the network economy and traditional economy to promote integration, seize the Internet market share. Liu Xin, Li Chenyun (2012) acquisition motivation based on the theory of the mobile Internet industry merger and acquisition is a strategic layout, mergers and acquisitions can also make the enterprise to find new growth opportunities and potential in the industrial chain, improve efficiency, it may just be because managers Yelang arrogance has led to a merger occurs. The main idea of this paper comes from the theory of synergetic effect. Zhao Jing (2014) Sina micro-blog Alibaba MampA motivation analysis of the event from the perspective of transaction cost, the size of transaction costs compared to self social media platform in cooperation with social media platforms and social media platform acquisition in three ways, the minimum transaction cost in M & a social media platform in this way results.

#### 4. Conclusion

This paper is mainly several classic theories of enterprise merger and part of the research of the existing Internet MampA, currently on the merger and acquisition theory is relatively mature, and most of them are related to research in management science, economics research is to analysis based on the existing management or enterprise level, however, different industries have significant difference. That led to a lot of theory can not explain the existing variety of corporate mergers and acquisitions, system and fully explain the enterprise merger theory is rare. In particular, the emerging Internet companies, different from the traditional enterprises, making the theory of Internet business mergers and acquisitions in the interpretation of the reasons for the existence of limitations and one sidedness.

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