China, India and Southeast Asia are the most desirable regions for foreign investment, but are almost as risky

Executives at multinational companies consider investing in China, India and South East Asia almost as risky as investing in Africa, according to a survey commissioned by Marsh, Mercer and Kroll for their report M&A Beyond Borders: Opportunities and Risks. Despite the perceived risks, China, India and South East Asia were identified as the most attractive destinations globally for M&A activity over the next 18 months, with 57% of deal makers surveyed describing potential interest as significant or very significant.

The issues identified as the most risky in the China, India and South East Asia region were questionable business practices, environment, intellectual property protection, and insufficient financial recourse. For North America, the figure was 43%, Western Europe 41%, Eastern Europe 31%, Latin America 29%, Middle East 27%, Australia, Japan and Korea 25% and Africa 19%. Litigation culture in North America is a significant caveat to the relatively lower M&A deal making risks in the region. Seen as particularly worrisome in the US, litigation risk has substantial implications for the current and future liabilities deal makers should consider when evaluating North American opportunities. North America was also seen as having a higher protectionist sentiment, similar to that of Western Europe.

Surveyed earlier this year about their attitudes to cross-border deals, executives at multinationals based around the world gave China, India and South East Asia an average risk rating of 5.3 out of a maximum 8 for a range of business-critical risks. The average rating for Africa was 5.5, Latin America 3.8, the Middle East 3.5, Eastern Europe 2.8, North America 2.1 and Western Europe 1.9. The Australia, Japan and Korea region was considered the least risky place to invest, with an average risk rating of just 1.6. While intellectual property risks, especially in China, are widely acknowledged, the report makes clear that the opening up of the economy in other sectors raises new concerns, especially around the environment. The Chinese government has introduced a raft of measures designed to improve environmental quality. While the degree of environmental litigation and statutory enforcement in China still lags well behind North America and Europe, companies need to be aware of the increased regulatory scrutiny of their operations and the stricter enforcement of environmental legislation.

Commenting on the findings of the survey, Karen Beldy Torborg, Global Head of Marsh's Private Equity and M&A Practice, said: "Despite the perceived risks of investing in this region, the level of M&A activity in recent years suggests that the expected reward is much stronger. We are witnessing a fundamental shift of the global business landscape, with companies all around the world eyeing the potential of these countries and ramping up their investment and presence, accordingly. Having a thorough understanding of the risks will help lead to a more successful investment." "Human capital-related risks are often magnified in cross-border M&A, and must be taken into account in every phase of the deal process," noted Bob Bundy, global head of Mercer's M&A consulting business. "Given how much is at stake and how difficult and complex it can be to turn two organisations that come from different geographies and cultures into one, forgetting that business is at the end of the day a human activity can prove costly indeed."

In Japan, M&A activity has jumped after the government further eased regulation of foreign investment. In so-called triangular mergers, the law now makes it possible for foreign-owned companies to invest in Japanese companies by means of stock-for-stock exchanges with the Japanese subsidiaries of those companies. Coupled with the country's low interest rates, a favourable financing condition has ensued, attracting more foreign investors.

In Western Europe, 44% of respondents had either significant or very significant appetites for investment into Eastern Europe. Chris Morgan Jones, Head of Kroll's Private Equity and M&A Practice in Europe, the Middle East and Africa, said: "Central Eastern Europe is perceived by many as one of the most fertile areas of investment opportunity. Confidence in the region is strong among both domestic corporations and multinationals contemplating investments. Nevertheless, a number of significant issues including dependable judicial systems and political influence on business do require more attention if Eastern Europe wants to have a risk profile similar to those of its Western neighbors and other developed states."