Case Studies on

Mergers, Acquisitions and Alliances – Vol. II

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Seeking access to new markets or products, companies tend to grow through mergers and acquisitions or by entering into alliances or partnerships with other companies.

The reasons for mergers and acquisitions (M&A) include:

1. Synergy: It is the gains made by combining resources of two companies; for example, the cost savings that result from an acquisition or merger. By combining business activities, performance increases and costs decrease. The most common synergies are:

Cost synergies – savings generally may come from internal economies of scale or through purchasing.

Sales synergies – better reach through a larger sales force or expanded customer base, cross selling one product to buyers of another, etc.

Companies may also generate synergies through combining technologies.

2. Diversification/Sharpening Business Focus: A company that decides to diversify may acquire or merge with another company which is in unrelated industry, in order to reduce the impact of a particular industry's performance on its profitability. Companies which decide to sharpen focus, often merge with companies that have deeper market penetration in a key area of operation.

3. Growth: Mergers can provide the acquiring company an opportunity to increase the market share without making any additional investment because they buy a competitor's business for a price.

4. Increase Supply-Chain Pricing Power: By buying out one of its suppliers or one of the distributors, a business can eliminate at least one level of costs. If a company buys out one of its suppliers, it can save on the margins that the supplier was previously adding to its costs. If a company buys out a distributor, it may be able to ship its products at a lower cost.

5. Eliminate Competition: Mergers and acquisitions allow the acquirer to eliminate future competition and gain larger markets share in its product's market.

There are many steps involved in Mergers and Acquisitions (M&A):

A company starts with a tender offer to purchase another company.

Once the tender offer has been made, the target company can resort to one of the options: Accept the Terms of the Offer and go ahead with the deal; Attempt to Negotiate for a high price; Execute a Poison Pill or Some Other Hostile Takeover Defense – A poison pill scheme can be triggered by a target company when a hostile suitor acquires a predetermined percentage of company stock. To execute its defense, the target company grants all shareholders – except the acquiring company – options to buy additional stock at a huge discount. This dilutes the acquiring company's share and intercepts its control of the company.

Mergers and acquisitions can face scrutiny from regulatory bodies. For example, when the two biggest telecom companies in the US, AT&T and Sprint, wanted to merge, the deal had to get the approval of the Federal Communications Commission (FCC). The FCC would probably regard a merger of the two giants as the creation of a monopoly or, at the very least, a threat to competition in the industry.

Finally, once the target company agrees to the tender offer and regulatory requirements are completed, the deal will be executed. An M&A deal can be executed by means of a cash transaction, stock-for-stock transaction or a combination of both.

The completion of a merger does not necessarily offer advantages to the resulting organisation. After merging, the companies hope to benefit from the following: Staff reductions, economies of scale, acquiring new technology, improved market reach and industry visibility. But, many mergers or acquisitions sometimes do just the opposite and result in a net loss of value due to problems.

Correcting problems caused by incompatibility – whether of technology, equipment, or corporate culture – diverts resources away from new investment, and these problems may be exacerbated by inadequate research or by concealment of losses or liabilities by one of the partners. Overlapping subsidiaries or redundant staff may be allowed to continue, creating inefficiency, and conversely, the new management may cut too many operations or personnel, losing expertise and affecting employee morale. These problems are similar to those encountered during takeovers.

Regardless of their category or structure, all mergers and acquisitions have one common goal of creating synergy that makes the value of the combined companies greater than the sum of the two parts. The success of a merger or acquisition depends on whether this synergy is achieved. In other words, the success of a merger is measured by whether the value of the buyer is enhanced by the action.

Mergers, Acquisitions and Alliances: Why they can Fail

The chances of success are hindered if the corporate cultures of the companies are poles apart. When a company is acquired, it is typically based on product or market synergies, but cultural differences are often ignored. For example, employees at a target company might be accustomed to easy access to top management, flexible work schedules and a relaxed dress code. These aspects of a working environment may not seem significant, but if the new management removes them, the result can be resentment and shrinking productivity.

McKinsey, a global consultancy, has found from its research study that most mergers or acquisitions fail, because the companies often focus too intently on cutting costs following mergers, while revenues and profits suffer. Merging companies focus on integration and cost-cutting so much, that they neglect day-to-day business, thereby prompting nervous customers to flee. This loss in revenue momentum is one reason for its failure.

78% of mergers and acquisitions fall apart within three years of their inception. About 70% of alliances fail outright, fall captive to shifting priorities, or achieve only initial goals, and 55% fall apart within three years of their creation.

Internal alignment and understanding are important for mergers, acquisitions and alliances. Having the capability to build and maintain internal alignment is defined as having an effective implementation process for identifying key decisions and issues related to a partnership, knowing who the relevant stakeholders are, and consulting with stakeholders to keep the organisation informed and involved throughout the lifespan of a partnership.

Lack of internal alignment and understanding leads to:

- Poor or uninformed decisions about whether to enter into an alliance
- Significant risk of sending confusing messages to, or acting inconsistently toward, its partners, misleading or confusing them, and jeopardising trust between them
- Internal bickering, non-delivery, and strain on internal resources as people are left unclear about priorities and focus.

Companies follow either all or any one of the inorganic growth strategies at a given time.

This book provides the reader an insight into the growth strategies of various companies and how these companies attempt to sustain their profitability through mergers or acquisitions or alliances. These case studies enable an understanding of the concept of inorganic growth strategies.

This book attempts illustration of in-depth inorganic growth strategies through case studies of 19 companies spanning across 14 different industries. The table provided lists the case studies in the book and relates them to the conceptual framework, giving the primary issues each case study is designed to highlight.

There are six case studies in the book that deal with 'alliances' strategy, providing insight into issues like how companies benefit through alliances. *Sony Ericsson's Alliance: The Synergies,* highlights how Sony Ericsson's 50-50 joint venture, with Sony's experience in consumer electronics and Ericsson's expertise in mobile handset manufacturing, envisaged dominating the global mobile handset market. However, the alliance had been incurring losses and could grab only a meagre 5.5% global market share by mid-2003. The case study also outlines under such circumstances, how Sony Ericsson reconsidered its initial strategy of targeting the high-end, low-volume segment by announcing its foray into the low-end, high-volume segment in the fourth quarter of 2003.

Readers would also find seven case studies dealing with 'acquisitions'. *IBM's Acquisition of PwCC: The Synergies* outlines the potential benefits of IBM and PwCC acquisition and the primary reasons behind the acquisition. The concept is also illustrated through other case studies.

While the four case studies talk about how mergers create synergies, *Sanofi-Synthelabo's Growth Strategies* discusses how both mergers and acquisitions helped the company to emerge as the world's second largest drug company.

Sl. No.	Industry	Case Studies	Primary Concept
1	Banking	Bank of America – FleetBoston Merger	Mergers
2	Banking	Bank One and JPMorgan Merger: Building an Empire or Adding Value?	Mergers
3	Automobile	Breaking Alliance with Fiat: Gain for GM?	Alliances
4	Business Intelligence Software	Business Objects – Crystal Decisions: The Synergies	Acquisitions
5	Commercial Aircraft Manufacturing	EADS: The Evolution and Growth of the European Aircraft Manufacturing Alliance	Alliances
6	Automobile	Fiat and GM: The Troubled Alliance	Alliances
7	Pharmaceutical	GlaxoSmithKline (GSK): Post-merger Growth Strategies	Mergers and Alliances
8	Information Technology Services	IBM's Acquisition of PwCC: The Synergies	Acquisitions
9	Internet and On-line Services Provider	Japan's Livedoor Co. Ltd: Growing through Unrelated Acquisitions	Acquisitions
10	Banking and Financial Services	Merger of MTFG and UFJ Holdings: The Potential Synergies	Mergers
11	Computer Software	Microsoft and Sun Microsystems: Sleeping with the Enemy?	Alliances
12	Media	News Corporation's Acquisition of DirecTV: A Strategic Fit	Acquisitions
13	Pharmaceutical	Novartis' Acquisitions of Aventis: The Potential Synergies	Acquisitions
14	Database and Enterprise Software	Oracle's Bid for PeopleSoft: The Strategic Fit	Acquisitions
15	Media	Pixar-Disney: Parting Ways	Alliances
16	Pharmaceutical	Sanofi-Synthelabo's Growth Strategies	Acquisitions and Mergers
17	Retailing	Sears-Kmart Merger: The Potential Synergies	Mergers
18	Wireless Telephone Handsets	Sony Ericsson's Alliance: The Synergies	Alliances
19	Motion Picture Production & Distribution	Sony's Film Studios' Acquisitions: The Strategic Fit	Acquisitions