

TENDENCIES, PURPOSES AND SUCCESS FACTORS OF MERGERS AND ACQUISITIONS

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MERGER AND ACQUISITION TENDENCIES TODAY

The presently seen merger and acquisition processes mean a possible way of increasing the company sizes. But according to the latest theories, nowadays the key factors of the growth are not the capital or the raw materials but rather knowledge. Examining the different cases we can get to the conclusion that four types of strategy can be connected to the growth of companies:

- company regeneration
- growth based on innovation
- growth by extending the abilities
- company growth by market expansion.

Hungarian tendencies

The value of company forestalling and acquisitions done by foreigners in Hungary in the first 11 month of 2004 took 250 Mrd forints (1346 M dollars). After many years of intermission, our country jumped to the first place of the Eastern – Central European region again with it. Only Bulgaria foreruns us with 1489 M dollars but it deducts a lot from the performance of the Balkan country that from this amount 1318 M dollars comes only from one business, the acquisition of MobilTel mobile service company in July. The Czech Republic is on the third place with a 1089 M dollar value and the fourth is Poland with 1049 M dollars. Based on the number of transactions Poland is on the first place with 78 transactions, Hungary is the second with 42 transactions and the Czech Republic is the third with 40 transactions. Bulgaria is only the third with its 11 transactions.

Hungary performed significantly better in the last years than before: foreigners invested exactly 1 Mrd dollars in 2003, 1340 M dollars in 2002 and 850 M dollars in 2001 as mergers and acquisitions in Hungary. Table 1 contains the biggest company acquisitions referring to the first 11 month of 2004:

Table 1

The biggest company acquisitions in Hungary in the first 11 month of 2004

Object of selling and buy	Purchaser	Purchase price (million dollar)
AKA Rt. 40%	Hungarian State	105,03
TVK Rt. 15,52%	CE Oil & Gas	103,2
AKA Rt. 39,5%	Hungarian State	99,42
Irodaház Budapest	Landesbank Sachsen	85,57
Eural Trans Gas Kft.	Atlantic Caspian Resources plc.	56,75
Égáz Rt., Dégáz Rt.	Gaz de France	54,73

It is a curiosity that the Hungarian companies already act as buyers in the region: Hungarian companies invested 223 M dollars as forestalling and acquisitions in the first 11 month of 2004. So the value of transactions done by Hungarian companies in the region increased to 1143 M dollars with it.

The biggest Hungarian transaction was the ownership change at BorsodChem company on the stock exchange: the value of transaction was 432 M dollars. The value of the second biggest transaction was almost 339 M dollars when the Klepierre-group, which was in the majority ownership of the French BNP Paribas, bought 12 Hungarian hypermarkets that were owned and operated by the subsidiary companies of Plaza Centers. By contrast, the whole of the Eastern-Central region performed really badly: in opposition to the 11,7 M dollars that was registered in the same time last year, the value of mergers and acquisitions was only 9,7 M dollars this year. The decline can be also seen in the number of transactions: in opposition to the 871 transactions done last year, there were only 522 transactions this year. But analyzing the processes globally we can recognize a huge increase this year after a four-year indisposition: the number of transactions increased from 16808 to 18481 and their value also increased from 1047 Mrd dollars to 1536 Mrd dollars. The number and value of mergers and acquisitions increased to their multiple in the last 10-15 years. For example, only in 1998 there were 20448 transactions done altogether in value of 2 billion dollars.

But according to the experiences, most of the business transactions do not hold out the best hopes. The surveys that analyzed the financial indexes of mergers and acquisitions in the last 75 years showed that more than half of the businesses did not fulfill the budget. In several cases there were loss of value and the performance of the company significantly decreased after making the transaction. In spite of that a lot of published survey examined the extremely high rate of unsuccessful transactions, this rate is still not better than 75 years ago.

It can be an interesting phenomenon that the company managers think that one of the most important steps of long survival is to increase the company sizes so they make efforts for mergers and acquisitions. But on the other hand the practice shows that in spite of the big company mergers and acquisitions, the market concentration decreased, so more and more smaller companies also appeared on the markets and, in all probability, these are also capable of living.

THE MOTIVATING FACTORS OF MERGER AND ACQUISITION TRANSACTIONS

About the motivating factors of company merges and acquisitions in general

According to all indications the managers of large companies feel a huge attraction for the mega-mergers and it drives them to such irrational decisions that unavoidably result in the large-scale destruction of company interests. It's worth analyzing the efficient causes of these unhealthy attractions because the diagnosis can be the first step on the way of fighting against the illness.

The company mergers and acquisitions can be motivated by the followings:

- *The desire for leading position:* presently the importance of increase of incomes is over emphasized at the companies, it is even more important than the increase of the profit. This view often appears as a target point of the company: the managers hope a 10-15% increase although the average increase is only 2-3%.
- *Increasing the prices of stocks:* the exploitation of high stock rate of a company also can be a purpose for a certain merger. There can be two reasons for it: one of them is if the stock prices of a company are overvaluated than this means an investment capital for it to finance a merger for establishing a global company. The other reason is that the companies hope to keep the attraction of their stocks from these huge mergers. The same thing happened in the drug industry where significant mergers took place.
- *Stereotyped way of thinking:* maybe a company does not even want to grow but it can not back out of the way of thinking of the whole industry. In the telecommunication industry, for example, it is a general wish for a company to have as much telephone lines as possible. This way of thinking (outlook) itself drove to many company mergers in the near past. But regarding the future, the advantages of these mergers have not been proved yet.
- *Peer pressure:* in some industries the companies tend to follow the leading companies. For example it is hard for a national bank to be out of the European bank merger wave even if a lot of surveys prove that rather the difficulty of transactions is increasing and not the number of clients.
- *Personal commitment:* the personal commitment of the top management that is connected to a theory often drives the company towards wrong strategies even if the performance of the company is persistently weak during the execution of the given strategy.
- *Excessive confidence with the partners:* the managers must examine the motivation of the participants very carefully during a possible merger or acquisition. Often the commission and the expected increase of stock exchange motivate a lot of people and not the common interest.

Purposes of merger and acquisition transactions in Hungary

Between January and March of 2001, the *GKI Economic Research Institution* and the Ernst & Young together made a survey about the experiences and expectations of Hungarian businesses connected to mergers and acquisitions. Most of the questions focused on the purposes of these transactions.

According to those who were asked, the companies want to increase especially the market share and the competitiveness with the merger and acquisition transactions, but at the same time these transactions are less suitable to exploit tax advantages or parry any hostile acquisitions. The transactions were supported mostly by the management and the customers and banks came after. According to the answers the polity is supporting the acquisition and merger transactions least of all. Table 2 shows the purpose of merger and acquisition transactions in percentage of answers. Anyway it must be mentioned that the sum of percentages in the table is not definitely 100 since more answers could be given.

Table 2
Purposes of merger and acquisition transactions in Hungary

Purpose of transaction	Rate in case of acquisitions (%)	Rate in case of mergers (%)
Increase of market share	46,8	18,6
Strategic decision	38,7	18,6
Increase in rate of growth	25,8	15,3
Extension of range of activities	21,0	6,8
Forming economies of scale	17,7	11,9
Reduction of costs	12,9	15,3
Restriction of the competitors	11,3	11,9
Rationalization of organizational structure	11,3	8,5
Technology receiving	8,1	0,0
Protection against opposed buying-up	8,1	5,1
Non-technological improvement of competitiveness	8,1	10,2
Utilization of tax advantages	8,1	1,7

As it is well shown in the above table the increase of market shares plays role almost in the half of acquisition transactions; almost 40% of those are a result of some kind of strategic decision. In the quarter of cases the rate of growth is wished to increase by the merger, but at one fifth of the transactions the extension of the range of activity also plays an important role. During the mergers the increase of the market share, strategic decisions and the rate of growth has an important role, but these are completed by the effort to reduce costs.

THE SUCCESS FACTORS OF MERGERS AND ACQUISITIONS

The McKinsey consulting firm has been dealing with company mergers for years. The consultants of the firm analyzed the share-list of 200 public associations, which had made mergers. It came out, that only 23 per cent of these mergers were successful, in so far as we measure the success with the increase of the share values. Mainly those mergers were successful, where small companies being in connection with the main business of the organization merged into organizations (in this case the value of 33 per cent of the shares increased), and the less successful transaction was, when large companies were taken over with no connection to the main business.

In the following we would like to emphasize the importance of two factors, which could contribute to the success or the failure of mergers and acquisitions with a great possibility.

Role of the human factor

Decisions regarding the occupation of the different scopes of activities involve the possibilities of many conflicts, especially when it means a radical change of the former operational system. To give express and creditable information may give help to avoid conflict situations.

When the question is set to the workers what their opinion is about the merger, everybody, or the most of them is against it. Everybody imagines the effects of the change on them. This behavior is absolutely normal. The reason is that everybody is afraid of new and unknown things, so it takes a while until they understand the importance of the changes. Conversations play an important role in it. In those cases, where lay-offs are unavoidable, discharged employees should be taken care of, since it can help to form an advantageous image of the company, and on the other hand it could motivate those, who stayed at the company.

Role of organizational culture

Organizational culture basically determines the operation of the people within the company and in the environment of the firm. This organizational culture comprises the different elements of the organization: from the applied systems to the procedures, from the values to the communicational techniques, from the range of products to the nationality of the members of the managerial board.

Let us put aside the fact, that change itself and the unknown future can also cause distress. Imagine the merger of those companies, where one of them increases the skills of the employees, responsibilities and decision-making were delivered to the subordinates, but the other, on the contrary, tries to lengthen the decision-making process in order to make decisions on higher levels. This difference alone could lead to conflict situations. In several cases national culture only steps up the current. In each national culture some upper values are coded, for example common goals are subordinated to personal goals- or vice-versa.

Usually the inappropriate management of organizational culture changes is the main reason of the failures of mergers and acquisition processes. Mergers always go together with cultural changes, since two or more companies cannot be the same in this respect. Additionally, two changing processes happen at the same time: besides forming the operation suitable for the needs of the new organization, the cultures of the former organizations should be harmonized.

Three factors play an important role in the development of failure or success. First we can mention cultural assimilation, which refers to the differences between the merging companies. The success of the integration could be influenced by the degree of differences in the management style, the compensation and penalty system, the methods of planning or in the relation to growth. The biggest similarities cause fewer conflicts, but they reduce the advantageous synergy effects at the same time. Another important factor is cultural potential, which includes openness to diversity, liability for trust and innovational skills. We can mention in third place the competent and committed management. This task requires serious skills and a high level of sensibility, so we can consider it rather an artistic than scientific category. Management needs to concentrate on three main fields during the mergers: strategies most suitable for environmental challenges have to be formed, inner integration has to be accomplished and employees have to be made committed to the changes.

The KPMG consultation firm made a model, which could help companies to maximize their share values during mergers and acquisitions. Seven key steps were conceptualized by the KPMG, which are the following: early steps, responsibility of the management, evaluation before tenders, planning the transaction, managing the procedure, authorization of the manager, independent evaluation of the closed transaction.

SUMMARY

After many years of leaning and reorganization companies discovered the fascination of growth again in the nineties. Although the growth of world economy has slowed down, managers and researchers thought it important to find out how and why companies grow. The following experiences regarding growth should be taken to heart: first of all, growth is an important and obtainable goal, even within stagnating industries. Secondly, growth can make it possible to activate the inner skills and abilities, but the outside world, for example the extension of the market can also establish growth. Companies must though acknowledge that growth can produce different and individual cases, and there is no one settled method. Companies must choose the solution, which can synchronize the domination of abilities and the costumers' needs.

Many managers believe that in order to keep the company's leading position, the company must grow, and therefore they make a decision of mergers and acquisitions. It is true, that a healthy growth is usually an essential part of the company's strategy, so upper management has to deal with this question, but it should also be kept in mind that growth bears some risks. The main importance of

growth is to find and train talented people, to get invested capital, to bring new products to the market and to manage the influences of the given industry's aspects. During the preparation of a merger the key factor of success is the clear-cut aspect of the problems connected with the merger. Holding to measurable factors and forgetting about the human resources probably will lead to the declination of business outcome of the new organization.

If we would like to support the organizational and managerial development with mergers and acquisitions, than it should be based on an accurate and reliable knowledge of the participants of the transaction and the workers. An ideal solution could be reached by examining the organizational culture, including its planned final version- embodied in the new company. The new model has to take into consideration the desires of not only the shareholders and the members of the managerial board but also the market position and strategy of the organization, and sometimes even the macroeconomic factors. The next step is determining the values and organizational behaviors, which should be maintained in favor of the ambitions. Some non-desired elements also may occur, which should be renounced.

In the next phase it should be thought over what kind of changes should be made regarding the elements mentioned earlier: should the premiate system or the efficiency managing system be changed, what kind of selection procedures should be applied, should the advancements within the company be encouraged or not, are there any infrastructural restrictions (for example in the field of IT)?

A small team can hardly manage all the arising tasks. The key of success is, also in long term, the participation of all the employees of the new organization. For this we need to know the fears, opinions and level of satisfaction of the workers, i.e. the atmosphere dominating within the organization. This way the management and the personnel department are able to determine those fields, which can count on support or resistance of the employees, so they can utilize support or counteract resistance. Determining the aspects of assignment for leading positions on time has a great importance. These aspects should consider what kind of culture the company would like to form, what the strategic goals of the company are, how the market position of the company moves, etc. The organizational culture is influenced by the availability of information, the perspicuity of goals and by a suitable communication (not only before and during the merger and acquisition, but also after the closing).

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Szücs Markovics, Klára: Tendencias, purposes and success factors of mergers and acquisitions; Lehoczky László, Kalmár László (ed.): 5th International Conference of PhD Students, Miskolc (Hungary): Miskolci Egyetem Innovációs és Technológia Transzfer Centrum, 2005. pp. 357-363. (ISBN:963-661-677-9)

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