Reasons for mergers and acquisitions

Business

It was announced this week that Reckitt Benckiser, the multinational consumer goods group, is to merge its European and North America operations into a single business. Mergers and acquisitions are a common support for either growth or recovery strategies in many industry sectors. By and large, a number of companies which are seeking expansion need to grow by generating the capacity of its production (Sherman 2011, pp.

124-7). Companies achieve this kind of growth in many ways. For the purpose of growing incrementally, they introduce new products as well as enter to novel markets by investing in research and development. However, in this era of globalization and competitiveness, companies take huge leaps forward through mergers and acquisitions (M&A), in order to increase their existence in the marketplace as fast as possible. The idea behind mergers and acquisitions is that one plus one makes three. In essence, this equation is the unique alchemy of a merger and an acquisition.

In fact, the main belief behind purchasing a company is the sake of generating a shareholder value over and above that due to the summation of the two companis (Sherman 2011, pp. 145-9). When two companies come together, they become more valuable than when they are separate companies. This is the underlying principle that allures companies to get into M&A, especially when times are tough. In some cases, strong companies prefer buying other companies for the sake of creating a more viable and cost-efficient company.

One of the most familiar opinions behind mergers and acquisitions is the idea that synergies subsist; thus, permitting companies to operate more

proficiently jointly than either could perform independently. Such synergies are as a result of the combined ability of the firms to take advantage of economies of scale as well as do away with duplicated functions. Additionally, they do so to share managerial expertise as well as raise larger amounts of capital (Sherman 2011, pp. 124-7). In companies operating at the same level of production, ‘ horizontal’ mergers take place due to their desire for a greater market power. For instance, in theory, authorities like Britain’s Competition Commission ought to hinder tie-ups that are in a position of creating a monopoly that caan easily abuse power.

This happened when it prevented a large supermarket chain from buying the retailer Safeway. However, in most cases, such resolutions are usually contentious and highly politicized. Another argument behind mergers and acquisitions is to overcome entry barriers. In a competitive corporate environment, more often than not, entry barriers into a market like economies of scale, exclusive buyer or supplier contracts, brand equity and reputation, as well as product and technology patents become stumbling blocks. In this regard, firms seeking to expand globally encounter cultural challenges as well as regulatory limitations that compel them to induce an acquisition or a merger with local companies. In some cases, companies go for mergers and acquisitions so as to increase time to market a new product.

This is due to the fact that it is at times risky to internally develop novel products since approximately 85% of product research and developments end up failing. Again, approximately 60% of the victorious ones get duplicated within a period of four years. Therefore, acquisitions offer an increased time to market a product with more expected proceeds.