

Theoretically mergers  
and acquisitions  
increase  
shareholders value



On the evidence, acquiring firms give their shareholders poorer return on average than target company shareholder. The poor performance indicates that acquirers remain over-optimistic about their performance and many still fail maximizing shareholder value through their acquisitions. The argument is that M&A activities in ordinary create synergy through achieving economies of scale or creating some sort of market power. However, some M&A may happen due to the managers motivated by personal objectives, where the managers have conflict of interest between maximizing shareholders' wealth and their own interest. For example, the case of Xstrata's bid that happened earlier, which was disclosed to be inappropriate and therefore the M&A deal did not happen. The others reason of M&A deals fail may due to over paid, the bid premium offering to the target company is over the pre-bid share price and the synergy did not come through. In fact, the firm can over paid in the right target company and recover in the long run, but if the firm over paid in a wrong target company, it never be recover. Thus, target shareholder gain from mergers. Although each deal is different, much benefit can be gained by learning from the experience of others. More insight into the case of mergers is found in the acquisition of Safeway supermarket by Morrison.

In 2003, Morrison Supermarkets, a small but profitably supermarket located in the North of England, offered a £3bn bid for Safeway, a supermarket with particular strength in Scotland the South of England. Morrison's objective of the acquisition is tending to sustainable growth as a broad supermarket leader in England. At that moment, Morrison's share price drove up because investors believed that the merger could bring many benefits. The merged

for both businesses is practically results in economies of scale were in the same field as supermarkets. Morrison's had a positive goodwill due to the good cost controls and these skills could be applied to Safeway as well. Morrison Supermarkets won the bidding and the takeover was accomplished in early 2004. Within the next 15 months, Morrison had to issue five profit warnings. In the year to the end of January 2006, the group made a pre-tax loss of around £300m compared to combined profit of about £650m before the merger. (2) The merger destroyed Morrison's shareholder value may due to the poor management by Ken Morrison and the change of management. Besides that, Morrison's was the only company on the FTSE to have no non-executive directors until investors forced the issue in May 2004. As was reported at the time<sup>2</sup>, at an initial meeting with 300 Safeway staff at their head office, Mr Morrison derided the Safeway's performance and profit record, severely damaging morale. Safeway's operations director and trading director resigned and Morrison's failed to persuade many Safeway staff to move north to the group's headquarters.<sup>(3)</sup> Others reason may due to the expertise in the Safeway IT system. Thus, consumers were confused and the margins were damaged. The stores no longer accurately addressed what their customers wanted and many customers moved elsewhere. The takeover of Morrisons Supermarkets over Safeway indicated very significant effects, but the operations management of Morrisons Supermarkets could still be expected to improve faster than average in the future.

On average, some mergers and acquisitions are good. By using the benchmark, successful companies achieved long-term success by prioritising three key activities in the pre-deal phase which could impact on the ability to

deliver financial benefits from the deal. There were included the synergy evaluation, integration project planning and due diligence. The market growth by taking over a competitor could produce synergy through economies of scale and efficiency gains, and can decrease the threat from competitors. Theoretically, mergers create value by creating operating synergies, typically in the form of economies of scale or economies of scope. Economies of scale are most likely to be realized when firms engaged in the same line of business combine operations. For example, in horizontal mergers economies of scope are most likely to be realized when firms in the same chain of supply combine operations. In vertical mergers, firms in unrelated businesses combine operations and conglomerate mergers; there is less theoretical reason for value creation. Many researchers have theorized that financial synergies are created in conglomerate mergers. Both of these should help to increase shareholder wealth. For Example Sony Corporation And LM Ericsson Have Merged Their Mobile Phone. The new company “ Sony Ericsson Mobile Communications”

## **CONCLUSION**

Anyway, it seems that M&A activities should be accompanied by a lot of risks. Why are they willing to take the high risks and pursuit M&A? Although M&A can destroy value, but it can also create very substantial value. Second and more importantly, aggressive deal making just reflects the increasingly shared belief that corporate partnering programs are clearly superior over organic growth strategies. Indeed, the competition for market share and the resulting shrinking of profit margins reduce the number of opportunities for high rates of return with organic business growth. Nowadays, the trend is for

businesses to enter the world market in which larger target market is available and growth is assured given that the general management has the capacity to launch such plan and come up with strategic business procedures and tactics in dealing and transacting with other business individuals. Big business industries compete painstakingly with other brands in order to increase the value of the products or service they offer to the prospect consumers and clients by challenging the strong brands and joining in the international competition that will generate high margins and substantial cash flows. All this will be possible if the product manufacturer or the service provider has the capacity to grow the volume and market share of the product or service, its presentation and packaging and the market routes and distribution through inventive and creative innovation.

Strategic planning could be only successful if the circumstances of the investment that will be made are well examined and researched. This will prepare the whole business in the problems and issues that the company may confront during the execution of the project or plan. However, this does not assure that there will be no problems that will exist and confront the business venture. The above discussion provides the advantages and disadvantages of merger and acquisitions.

The current global trends are driving the need for change with the critical purpose of gaining competitive advantage. Proactive management and leaders think change by recognizing that “ change” challenges people to adapt and grow, or be swept away aside as complacent and obsolete. To compete in the world today, companies must strive to be different and must expand their knowledge base, sharpen skills, and finally, manage time and <https://assignbuster.com/theoretically-mergers-and-acquisitions-increase-shareholders-value/>

resources more efficiently. In merger and takeover, change is not something to fear or resist, it is the essence of business operation itself. By embracing and promoting positive change, companies learn more about their capabilities. With merger and takeover, companies are given the chance and power to turn today's pain into tomorrow's gains.

#### Book

Glen Arnold. (2005) Corporate Financial Management. text. 3th ed., Harlow: Financial Times Prentice Hall.