

# Glaxo and smith kline's merges and acquisition



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## **Introduction**

We find always things through research which has not been and before in particular area or field . Researcher often does research to clarify the doubt that they have in the previous researches. This research examines the factors that encourage companies to do mergers and acquisition in general, and Glaxo & smith Kline in particular to go for mergers.

Merges and acquisition have been and continue to be a very popular strategic alternative for companies' expansion growth and diversification.

Merges and acquisition is not a simple process. It is a strategic decision in the life of a company a lot of work have already been done on M&A. my main research is on the issue of merges and acquisition as an expansion strategy for organization as well how we measure the performance of the company after Merges and Acquisitions.

## **Detailed description of proposed dissertation**

There are number of theories about why companies go for merges and acquisition. Different companies have different motives for

## **Background**

Mergers and acquisitions are often used to describe on thing; the coming together of two companies. However, although similar in meaning, they are technically different. An acquisition can be defined as the process in which an organization develops its current situation in terms of resources and competencies by taking over another firm (Johnson & Scholes, 1999). This can be effected by acquiring the shares of target company or by acquiring its assets, liabilities and trading activities (Bowman & Asch, 1996).

Companies are learning that they might need to be strategic partners if they expect to be effective. Even huge companies often can not attain leadership, either nationally or globally, without shaping strategic alliances with domestic and/or multinational companies that balance or leverage their abilities and resources. Just doing business in one more country may need the firm to license its product, form a joint venture with a local firm, and buy from local suppliers to meet “ domestic content” requirements, and so on. As a result of these difficulties, many firms rapidly develop global strategic networks (Coffey, Cook & Hunsaker, 1994).

“ The main reason of merging and acquiring novel firms is usually to get better overall performance (Lubatkin, 1983) by attaining synergy, or the more normally described as the “ 2 + 2 = 5” effect (Cartwright and Cooper, 1993a; Hovers, 1971) between two business units that will boost competitive benefit (Porter, 1985; Weber, 1996).”

However, the mere survival of potential synergism is no assurance that this possibility will be understood (Cartwright and Cooper, 1993a; Kitching, 1967). Recent research point out that these M&As have a unenthusiastic impact on the economic performance of the new body (Cartwright and Cooper, 1993a; 1993b; Marks, 1999; Tetenbaum, 1999). Estimates of their achievements rage from 20-60 percent (British Institute of Management, 1986; Hunt, 1988; Marks, 1988; Weber, 1996).

### **Literature review**

The merger and acquisition wave is not new in Europe; it is and has been constantly reforming the global financial landscape for the last three

decades. This movement has affected the whole world with the United States being in the leading position. Evidence reveals that more than \$ 1 trillion was spent on M&A activities in all fields, with the banking industry occupying a major part in the activity (Hitt et al. 1998).

There are four main type of mergers and acquisition

### **Horizontal Mergers**

“ A horizontal merger takes place between companies involved in the similar kind of business with about the same customers and suppliers, and is therefore a move inside the similar economic surroundings. As such, it may not add considerably to the flexibility and constancy of the firm. It has huge appeal because it happens in a business area that the acquirer understands. Since they decrease the figure of rival firms in an industry and focus big shares of the market in fewer hands, they are more likely to be subject to scrutiny by the Monopolies Commission (Jones, 1982).”

### **Vertical Mergers**

“ Vertical mergers concern two corporations operating at successive stages of manufacture so that one supplies or is supplied by the other. It usually gives better continuity of supply and may also get better the flow of making and reduce stockholding and handling stocks. If a market has arrived at diffusion level, it may there the only avenue for expansion, short of diversification (Jones, 1982).”

### **Conglomerate Mergers**

“ Conglomerate Merges involve the coming jointly of the firms in dissimilar businesses. The firms are not likely to have any normal trading interests and

the only tie may be centralized provision of certain particular managerial services, finance and management control (Jones. 1982).”

### **Concentric Mergers**

“ Diversification may not engage moving into totally diverse businesses, as does the conglomerate merger. Instead, the firm may expand its activities at the same time as keeping a measure of unity with existing activities. This may be done by acquiring different technology which can be marketed to present customer types (concentric marketing) or by acquiring new customers for the existing technology (concentric technology) (Jones, 1982).”

Theories that what motives encourages organizations to go for mergers and acquisitions

### **Synergy**

Synergy is the quite simplistic idea that the mixture of two businesses can make better shareholder value than if they are worked separately (Donald, 2008).

There are two basic types of synergy

#### **Operating Synergy (Economies of Scale and Scope)**

Operating synergy consists of both economies of scale and economies of scope. Experimental studies propose that such synergies are important determinants of shareholder wealth creation (Houston, James & Ryngaert, 2001)

**Financial Synergy (Lowering the cost of capital)**

“ Financial synergy related to the affect of M&A on the cost of capital (i. e., the lowest return require by lenders and investors) of the firm which is going to be acquired or newly created firm resulting from M&A. Theoretically, the cost of capital could be reduced if the merged firms have uncorrelated cash flows (i. e., so-called co-insurance), understand financial economies of scale from inferior securities and transactions costs, or result in improved matching of investment opportunities with internally generated funds. Combining a firm with excess cash flows with one whose internally generated cash flow is inadequate to fund its investment opportunities may result in a lower cost of borrowing. A firm in mature industry may whose growth is slowing may produce cash flows well in excess of available investment opportunities. Another firm in a high firm growth industry may have more investment opportunities than the cash to fund them. Reflecting their diverse growth rates and risk levels, the firm in the mature industry may have a lower cost of capital than the one in the high-growth industry. Combining the two firms might result in a lower cost of capital for the merged firms (Donald, 2008).”

**Diversification**

Diversification refers to a plan of buying firms outside of a company’s existing primary line of business. There are two commonly used good reasons for diversification. The first narrates to the formation of financial synergy resulting in a reduced cost of capital. The second reason for diversification relates to moving of a firm from their core product line or markets to product line or market that have potential for expansion.

In this case diversification could be related or unrelated as well.

If a firm is facing slower growth in its current markets, it may be able to accelerate growth by selling its current products in new markets that are somewhat unfamiliar and, therefore, more risky. For example, pharmaceutical giant Johnson and Johnson announced unsuccessful takeover attempt of Guidant Corporation in late 2004 reflected its attempt to give its medical devices business an entry into fast growing market for implantable devices, a market in which it does not currently participate. Similarly a firm may attempt to attain higher growth rates by developing or acquiring new products, with which it is relatively unfamiliar, and selling them into well-known and less risky current markets. Examples of this strategy include retailer J. C. Penney's acquisition of the Eckerd Drugstore chain or J&J's \$16 billion acquisition of Pfizer's consumer health care product line in 2006. In each instance the firm is assuming additional risk. However, each of these related diversification strategies are usually less risky than an unrelated diversification strategy of developing new products for sale in new markets. Investors often perceive companies diversified in unrelated areas as riskier, because they are difficult for management to understand and management often fails to fully fund the most attractive investment opportunities (Morck, Shleifer, and Vishny, 1990).

### **Strategic Realignment**

The strategic realignment theory suggests that firms do M&A because it is the quick way of adjusting to changes related to their external environment.

Although change can come from many different sources, changes related only with regulatory environment and technological innovation is considered.

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### **Regulatory Change**

M&A activity in recent years is more likely to see in those industries where deregulation occurred. These industries comprise financial services, health care, utilities, media, telecommunication and defense. There is a proof which shows that takeover activity in deregulated industry is higher as compared to regulated (Jensen, 1993; Mitchell & Mulherin, 1996; Mulherin & Boone, 2000). Technological Change

Technological advances create new products and industries. The development of airplane created the passenger airline, avionics, and satellite industries. The vacuum tube, transistor, and microchip provided the basis for the television, radio, and personal computer. The emergence of satellite delivery of cable network to local systems ignited explosive growth in cable industry. Today, with the growth of technology like broadband, we can see the convergence of technologies like voice, data and video on the internet.

As the speed of technological change go faster, M&A often is viewed as a way of speedily rising new products and industries made possible by the convergence of new technologies. Large, more bureaucratic firms often are unable to exhibit the creativity and speed smaller, more nimble, niche players display. With the talent of engineering frequently in shortage of supply and shortening in product life cycles, firms often do not have enough time and resources for innovation. Consequently big companies frequently look to M&As as a way to acquire novel technologies quickly and even less expensive and proprietary know-how to fill gaps in their existing product offering or to go into completely new businesses. One reason for acquiring



technologies is that it is a defensive approach to keep important new technologies out of the hands of rival firms.

In 2006, eBay acquired SKype technologies, the internet phone provider, for \$2.6 billion in cash and stock. eBay hopes that move will boost trading on its online auction site and prevent competitors from gaining access to technology. Skype offers downloadable software that enables consumer to chat to on another over the internet through their computers. Skype's voice communication technology is expected to make online trading easier for eBay's 157 million users, mainly with transactions involving real estate, big-ticket items (Donald, 2008).

### **Buying Undervalued Assets (The Q-Ratio)**

The Q-ratio is the market value of acquiring firm's stock to the replacement cost of its assets. Firms interested in expansion have choice of investing in new plant or equipment or obtaining the assets by acquiring a company whose market value is less than the replacement cost of its assets (i. e., Q-ratio  $<1$ ). This theory was very helpful in explaining M&A activity during the 1970s when high inflation and interest rate depressed stock prices well below the book value of many firms. High inflation also cause the replacement cost of assets to be much higher than the book value of assets. More recently, gasoline refiner Valero Energy Corp. acquired Premcor Inc. in an \$8 billion transaction that created the largest refiner in North America. The estimated cost of building new refinery with capacity equivalent to Premcor would have cost 40% more than the acquisition price (Zellner, 2005).

## **Glaxo SmithKline History**

### **2. 10 Company Overview**

#### **2. 10. 1 History**

GlaxoSmithKline plc is a public limited company incorporated on 6th December 1999 under English law. Its shares are listed on the London Stock Exchange and the New York Stock Exchange. On 27th December 2000 the company acquired Glaxo Wellcome plc and SmithKline Beecham plc, both English public limited companies, by way of a scheme of arrangement for the merger of the two companies. Both Glaxo Wellcome and SmithKline Beecham were major global healthcare businesses. GSK plc and its subsidiary and associated undertakings constitute a major global healthcare group engaged in the creation, discovery, development, manufacture and marketing of pharmaceutical and consumer health-related products.

#### **GlaxoWellcome**

In 1880, Burroughs Wellcome & Company was founded in London by American pharmacists Henry Wellcome and Silas Brough. The Wellcome Tropical Research Laboratories opened in 1902. In 1959 the Wellcome Company bought McDougall & Robertson Inc. to become more active in animal health. The Wellcome Company production centre was moved from New York to North Carolina in 1970 and the following year another research centre was built.

Glaxo was founded in Bunnythorp, New Zealand in 1904. Originally Glaxo was a baby food manufacturer processing local milk into a baby food by the same name: the product was sold in the 1930s under the slogan “ Glaxo builds bonny babies”. Still visible on the main street of Bunnythorpe is a derelict dairy factory (factory for drying and processing cows’ milk into <https://assignbuster.com/glaxo-smith-klines-merges-and-acquisition/>

powder) with the original Glaxo logo clearly visible, but nothing to indicate that this was the start of a major multinational company.

Glaxo became Glaxo Laboratories, and opened new units in London in 1935. Glaxo Laboratories bought two companies called Joseph Nathan and Allen & Hanburys in 1947 and 1958 respectively. After the Company bought Meyer Laboratories in 1978, it started to play an important role in the US market. In 1983 the American arm Glaxo Inc. moved to Research Triangle Park (US headquarters/research) and Zebulon (US manufacturing) in North Carolina. Burroughs Wellcome and Glaxo merged in 1995 to form GlaxoWellcome. In the same year, GlaxoWellcome opened their Medicine Research Centre in Stevenage, England. Three years later GlaxoWellcome bought Polfa Poznan Company in Poland.

### **SmithKline Beecham**

In 1843, Thomas Beecham launched his Beecham's Pills laxative in England giving birth to the Beecham Group. Beecham opened its first factory in St Helens, Lancashire, England for rapid production of medicines in 1859. By the 1960s it was extensively involved in pharmaceuticals.

In 1830, John K. Smith opened its first pharmacy in Philadelphia.

Subsequently, in 1891, Smith, Kline and Company merged with French, Richard and Company. It changed its name to Smith Kline & French Laboratories as it focused more on research in 1929. Years later, SmithKline & French Laboratories opened a new laboratory in Philadelphia; it then bought Norden Laboratories, a business doing research into animal health.

Smith Kline & French Laboratories bought Recherche et Industrie Therapeutiques (Belgium) in 1963 in order to focus on vaccines. The Company started to expand globally buying seven laboratories in Canada and the US in 1969. In 1982, it bought Allergan, a manufacturer of eye and skincare products. The Company merged with Beckman Inc. later that year and then changed its name to SmithKline Beckman.

In 1988, SmithKline Beckman bought its biggest competitor, International Clinical Laboratories, and in 1989 merged with Beecham to form SmithKline Beecham plc. The headquarters of the Company were then moved to England. To expand research & development in the US, SmithKline Beecham bought a new research center in 1995. Another new research centre at New Frontiers Science Park in Harlow, England was opened in 1997. But the main centre of focus operates in Dumfriesshire, Scotland.

GSK has its corporate head office in London. It also has operational headquarters in Philadelphia and Research Triangle Park, USA, and operations in some 119 countries, with products sold in over 130 countries. The principal research and development (R&D) facilities are in the UK, the USA, Japan, Italy, Spain and Belgium. Products are currently manufactured in some 37 countries. The major markets for the Group's products are the USA, France, Japan, the UK, Italy, Germany and Spain.

## **2. 10. 2 Business Segment**

GSK operates principally in two industry segments:

1. Pharmaceuticals (prescription pharmaceuticals and vaccines)

2. Consumer Healthcare (over-the-counter medicines, oral care and nutritional healthcare).

### **Aims and objectives**

The research have several aims regarding mergers and acquisitions of companies, specially Glaxo and SmithKilne.

### **Methodologies**

I will use the quantitative as well as qualitative research method . The methodology I use is the analysis of financial statements of a company so that it comes to know that their M&A is successful or not. The intention of use of quantitative method is that it is helpful in drawing the tables, graphs, and figures upon which the performance of a company can be measured. Quantitative method is applied for numbers and other statistical techniques so I can refine my research. I will use qualitative method as well like interviewing so that I will come to know that what factors, a company has to take into consideration while going for mergers and acquisitions.

Quantitative method is used for

- Generation of interpretation
- Development of tools and methods for measurement
- Analyzing of data
- Evaluation of result

It is hard to know immediately whether the companies are going well or not after M&A's because we can not precise on word of mouth about company's

performance. But after few years we can know the situation of company by empirical data which shows their performance.

I have chosen comparative research design for my research completion as this design is appropriate according to research. I am using secondary data for comparative research, I need to use the three years annual reports of company to identify their performance whither M&A was useful or not. Company has annual reports to show their financial statistics but I am using their reports as secondary data for analysis. I am doing comparison of the reports based on statistical and other quantitative methods for findings and analysis. Result will give evidence of their success or failures.