

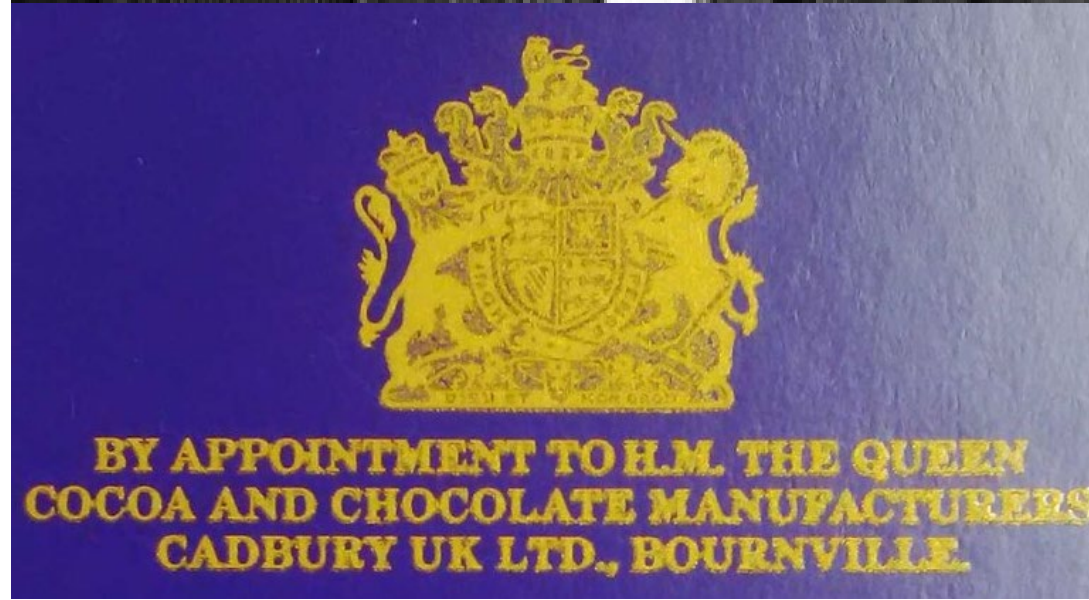
Mergers and Acquisitions: Do They Create Or Destroy Value?

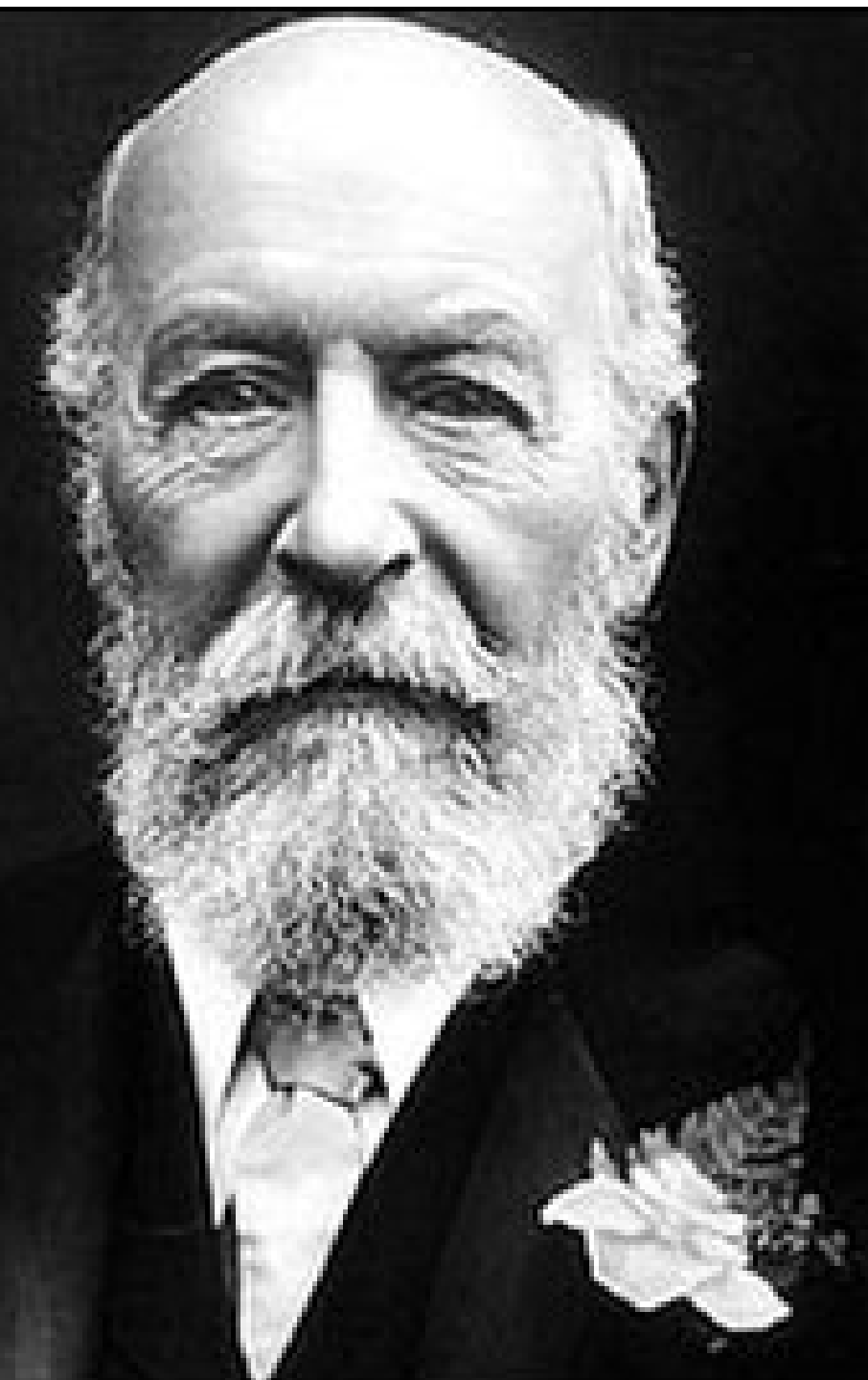


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The Kraft logo consists of the word "Kraft" in a bold, blue, sans-serif font, centered within a white, rounded rectangular shape. This white shape is enclosed by a thick, red, rounded border that has a slight 3D effect, giving it the appearance of a red ring or a thick red outline.

Kraft

745p 840p + 10p = £11.9b
50% 31% (up from 5%)







The Remedies

- 2011 changes to Takeover Code:
 - Bidder needs to state intentions after the takeover
 - Staff representatives can give views on takeover
- Other suggestions
 - Disenfranchise “short-term” shareholders
 - National interest test: “too easy for foreign firms to buy UK rivals”



Two Sides To (Almost) Every Story

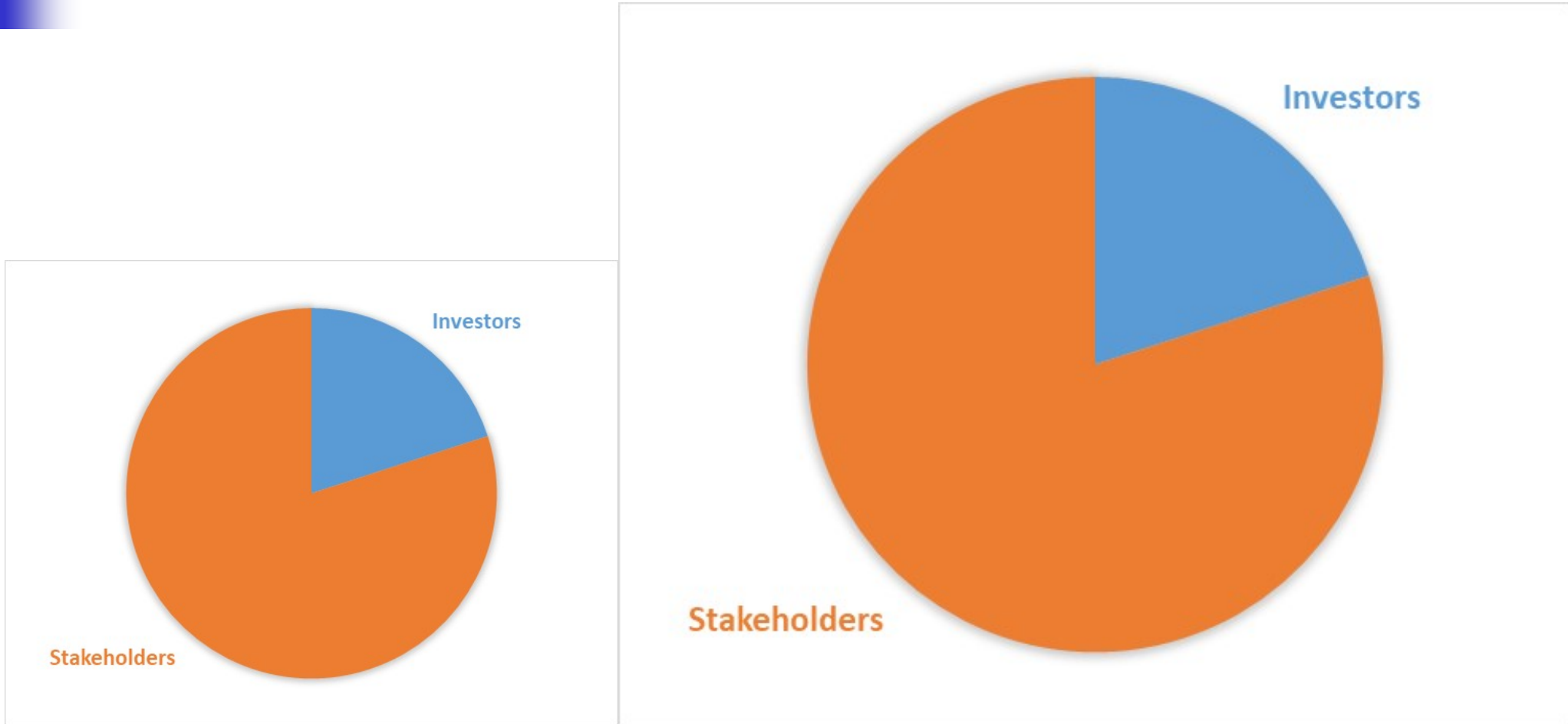
- Cadbury had announced closure of Somerdale in 2007
- Bournville headcount had fallen from 2,000 in 2007 to 1,000 in 2009; operating costs 3x German comparables
 - 2017: Mondelez completed a £75m modernisation; £18m new global research operation
 - Pay rise praised by Unite: “set the benchmark within the food, drink, and agriculture industries for other employers to follow”
 - Maternity pay increased from 4 to 9 months



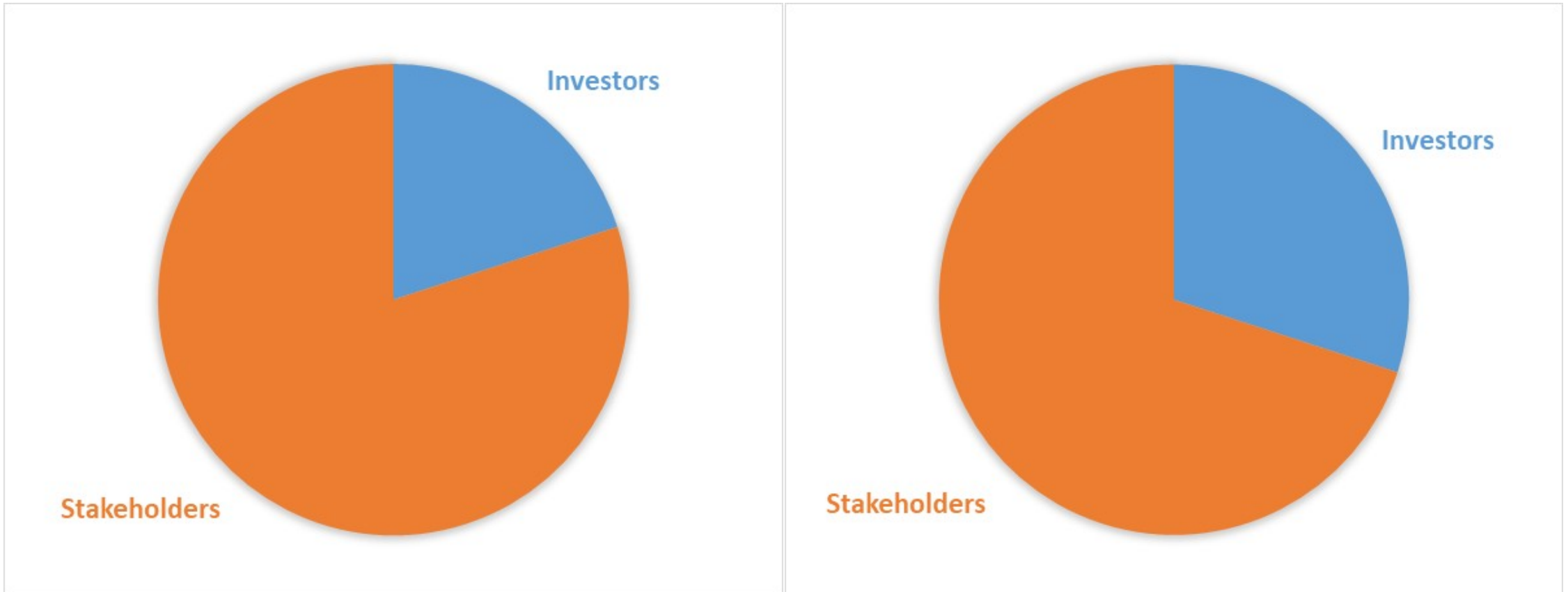
The Evidence

- US targets, 1980-2005
 - Target: 7% runup, 15% announcement
 - Bidder: 0.5% runup, 0.7% announcement
 - Overall: 7% runup, 11% announcement
- So shareholders gain overall, *on average*

Pie-Growing Mergers



Pie-Splitting Mergers





Potential Losers From Pie-Splitting

- Customers

- Zero or negative effects on rivals, suggesting no collusion; increased efficiency of merged firm
- Positive effects on corporate customers
- “Taken together, the customer and rival results are strongly inconsistent with the monopolistic collusion hypothesis”

- Suppliers

- Only non-retained suppliers lose; retained suppliers increase market share
- Efficiency gains from mergers passed onto suppliers (and customers)

Potential Losers From Pie-Splitting (cont'd)



- Employees
 - Wages and employment rise
- Taxpayers
 - Minor role
- Bondholders
 - Mixed effects on bidder bonds, positive effects on target bonds
- Target shareholders, if market myopic
 - Most mergers targeted at firms and industries with little R&D
 - After a failed merger, target returns to original price)



Effects of Takeover Probability

- Encourages R&D
 - To increase efficiency and ward off (hostile) takeovers
 - To become more attractive and encourage (friendly) takeovers
- Improves efficiency
 - Combats “quiet life”; spurs creation of new plants and destruction of old plants



Bidder Gains Revisited

- Average gains of 0.5% (runup), 0.7% (markup) mask huge variation
- 1998-2001: US acquirers lost \$240bn through M&A
 - Small number of bad deals by very large acquirers. Without them, acquirers would have gained overall



Why Might Acquirers Undertake Bad Deals?

- Deliberate
 - Paid for deals (Chris Gent's £10m, William Harrison's \$20m)
 - Paid for size
 - Prestige, empire-building (Daewoo)
 - Bidder returns related to CEO's stake, corporate governance
- Unintentional
 - Bidder returns related to overconfidence



The Role of M&A Advisors

- Critical, since CEOs have limited expertise
- Paid only a success fee, but success \neq announcement
 - Is reputation a mitigant?
- Investment banks matter (IQ range of 1.26% of \$10bn)
 - Not just execution houses
- Past performance doesn't affect market share
 - Even though it significantly predicts future performance
- But past market share affects future market share
 - Even though it *negatively* predicts future performance
- Potential culprit: market share league tables. Replace with performance league tables



The Role of Short-Term Traders

- Recall from Lecture 4: holding period \neq orientation
- “Short-term” investors will have acquired their shares from “long-term” investors
- Activist arbitrageurs
 - Target deals with low premiums and where CEOs receive outsized payments
 - Significantly *reduce* the probability of a takeover; increase premium if takeover still occurs
- But case for preventing voting with borrowed stock in an M&A deal



A National Interest Test?

- Foreign investors import
 - Superior governance
 - Superior social norms
- Potentially subject to substantial lobbying; driven by errors of commission not omission
- Takeovers *can* split or shrink the pie, but nothing specific to foreign takeovers
- National interest should be to promote great companies, which discipline helps
 - Tariffs (which reduce discipline) need not be in national interest



Going Forwards

- “Grow the Pie: Creating Profit for Investors and Value for Society” (Cambridge University Press, 2020)
- Twitter/LinkedIn: @aedmans
- 2019/20 Lecture Series: “Business Skills for the 21st Century”
 - Time Management in the Digital Age
 - Finding Purpose in Your Career
 - Public Speaking Without Fear
 - Mental and Physical Wellness
 - Facts, Data, and Evidence: Knowing What To Trust
 - The Growth Mindset and the Abundance Mentality