# WHY MERGERS AND ACQUISITIONS FAIL?

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***Abstract :***

*Mergers and Acquisitions (M&A) are one of the fastest strategic that many companies prefer in order to leverage the global competitive market in the present scenario. The fundamental premise of any merger is that the merging entities will be more valuable together than they are separately. It doesn't matter if you define value as shareholder equity, impact on the world or basic happiness. A merger is supposed to be an exercise in value creation. Yet, many of mergers fail. However, many previous researches have highlighted the high rate of failure among M&A is increasing. Perhaps, historically mergers have occurred between companies that are similar in size and also have similar interests, yet acquisitions tend to facilitate larger organizations and companies acquiring smaller businesses. It is now common for mergers and acquisitions to be enacted across borders, often providing solutions for corporate to extend their influence from national into international markets. However, despite the financial expertise available to ascertain the viability of such business transactions, many of these business ventures fail, or at best do not perform according to expectation; reflected in adversely affected share prices. So a small effort has been done by studying the conceptual and theoretical backgrounds identifying the reasons for increasing the failure of M &A, and suggests some measures towards the successful of M&A.*

***Keywords:*** *Mergers and Acquisitions, Failed M & A, Classification of Mergers, Valuation.*

## Introduction

In present era, global competition hasdrive to leverage advantage, which resulted in both small and larger companies combining resources. Consolidations of markets are one of the main reasons for M&A's. Corporate possessing similar products and services are looking to both consolidate and expand; thereby utilizing joint interests to further their goals. Despite extensive 'due diligence' and research, there have been and still are many risks to venture into such business transactions.

Although mergers and acquisitions are motivated by different requirements, the end result is to**increasetheir size and capacity for growth.** Due to the increasing development of business systems and 'know how' coupled with advances in communication technology,

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speed of growth and efficiency of operational function have become essential to ensuring survival and continued sustainability. The present investors often look forward for the quicker returns on investment due to global complication and economic volatility; thereby driving the search for ways to extract optimal profitability. However, factors such as differences in management styles, cultural difference, leadership style, communication and continually changing market conditions can negatively impact projected profitability and growth trends; thereby negating the perceived benefits of mergers and acquisitions. This will turns to the methodology to analysis the research, following which the causation of successes and failures in these business transactions can be determined business environment.

Mergers and Acquisitions are two different business combinations, although they are thought of as a generic term. Both mergers and acquisitions can be classified further to differentiate the ways the companies can do business combinations.The mergers can be classified as follows on the basis of relatedness of the business activities:

- **Horizontal Merger:** A merger that happens between companies belonging to the same industry or sector. The companies have businesses in the same space and are generally competitors to each other. A horizontal merger is a feature of an industry which consists of a large number of small firms / fragmented industry. The level of competition is high and the post-merger synergies and gains are much higher for companies in such industries. The motivation behind such merger is economies of scale and control of bigger market share.
- **Vertical Merger:** A vertical merger is a merger between companies that produce different goods or offer different services for one common finished product. The companies operate at different levels in the supply chain of the same industry. The motivation behind such mergers is cost efficiency, operational efficiency, **increased margins** and more control over the production or the distribution process. There are two types of vertical mergers:
  - **Backward Integration:** A vertical integration where a company acquires the suppliers of its raw materials.
  - **Forward Integration:** A vertical integration where a company acquires the distribution channels of its products.
- **Conglomerate Merger:** A merger between companies that operate in completely different and unrelated industries. A pure conglomerate merger is between companies with totally nothing in common. A mixed conglomerate merger is between companies looking for market or product extensions.
- **Market Extension Mergers:** Mergers between companies that have same products to offer but the markets are different. The reason behind such mergers is access to bigger markets and an increase in client base.
- **Product Extension Mergers:** A merger between companies that have different but related products but the markets are same. Such mergers allow the companies to bundle their product offerings and approach more consumers.

## REVIEW OF LITERATURE

- Marina Marty nova, Sjoerd Oosting and Luc Renneboo‰(2007) studied the long-term profitability of corporate takeovers in Europe, and found that both acquiring and target companies significantly outperformed the median peers in their industry prior to the takeovers, but the profitability of the combined firm decreased significantly following takeover. However, the decrease became insignificant after controlling for the performance of the control sample of peer companies.
- Raymond No‡2002) studied that 60-80% of all mergers are financial failures when measured by their ability to outperform the stock market or to deliver profit increases.
- Anne Freedma•(2002). Those findings are further supported in a study by A.T Kearney that shows 58% of mergers failing to achieve their stated goals,
- Suh-kyung Yoo (2001) studied that a survey of 1,000 companies revealed that more than two-thirds of companies failed.

### Objectives of the Study

- To analysis the causes and reasons for the increase in failure of Mergers & Acquisitions.
- To offer suggestions to reduce the failure in M & A.

### Data for the Study

Secondary data is used for the study; the nature of analysis is descriptive and conceptual.

### Global M&A Deal Volume

US targeted withdrawn M&A volume is up 64% on full year 2015 ($231.1bn) to $378.2bn in 2016 YTD(year to date), already the largest annual volume on record. Despite record high volume boosted by jumbo deals, activity (34 deals) has dropped to the lowest YTD level in 21 years. Average annual volume and activity of US withdrawn deals over the last five years is $243.4bn via 101 deals Global withdrawn M&A volume stands at $465.5bn in 2016 YTD, up more than double the same 2015 period ($189.9bn). The average YTD level for withdrawn deals is $199.4bn via 333 deals in the last five years. 2007 was peak year for such deals globally with $1.1tr via 826 deals.

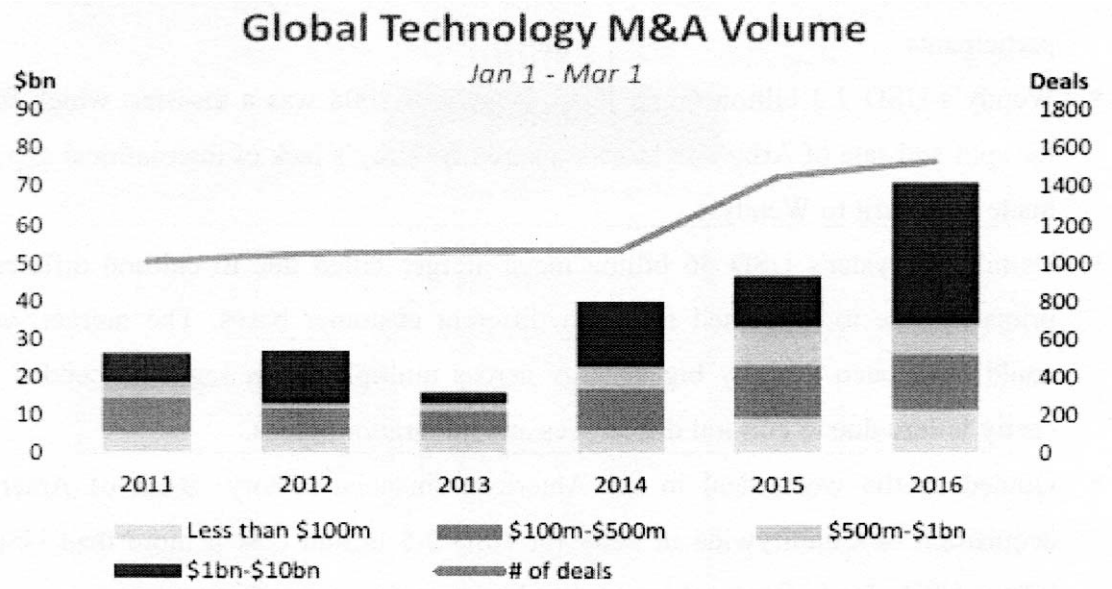
### Five Withdrawn jumbo deals in 2016 YTD

Five jumbo deals* have boosted US withdrawn M&A to a record high volume ($357.8bn), accounting for a 95% share. Seven deals is the annual record for jumbo deal activity which occurred in 2001, 2007 and 2014. Average jumbo activity over the last 10 years is four deals.

### Pfizer Largest Withdrawn deal on Record

Allergan and Pfizer's $160.0bn bid became the biggest withdrawn deal on record on April 6, two days after the US Treasury Department announced stricter rules for tax inversions on April 4, 2016 .On April 30, Halliburton withdrew its $38.7bn bid for Baker Hughes, becoming the largest withdrawn Oil & Gas M&A deal on record. Before withdrawing the deal, the US Department of Justice sought to block the bid citing it as anti-competitive.

Global M&A volume stands at $1.04tr, reaching the $1tr mark on April 29, down 19% to the lowest volume since the same period of 2013 ($834.5bn). US targeted M&A is down 21% to the lowest YTD volume since 2014 ($368.3bn).




| Global Technology M&A Advisor Ranking 2016 YTD | | | | |
|---|---|---|---|---|
| Pos. | All Advisor Parent | Value $m | % Share | No. |
| 1 | China International Capital Corp | 10,092 | 14.1 | 3 |
| 2 | Morgan Stanley | 8,717 | 12.2 | 6 |
| 3 | Goldman Sachs | 8,446 | 11.8 | 6 |
| 4 | JPMorgan | 6,563 | 9.2 | 5 |
| 5 | Bravia Capital Hong Kong | 6,349 | 8.9 | 1 |
| 6 | Barclays | 5,819 | 8.2 | 4 |
| 7 | Qatalyst Partners | 3,568 | 5.0 | 1 |
| 8 | Haitong Securities | 3,378 | 4.7 | 3 |
| 9 | Southwest Securities | 3,252 | 4.6 | 7 |
| 10 | Huarong Securities | 3,008 | 4.2 | 1 |

**(Source: *Thomson International Securities and Dealogic)***

**Why Mergers and Acquisitions in India?**

The factors responsible for making the merger and acquisition deals favorable in India are:

- Dynamic government policies
- Corporate investments in industry
- Economic stability
- "Ready to experiment" attitude of Indian industrialists

Sectors like pharmaceuticals, IT, ITES, telecommunications, steel, construction, etc, have proved their worth in the international scenario and the rising participation of Indian firms in signing M&A deals has further triggered the acquisition activities in India.

In spite of the massive downturn in 2009, the future of M&A deals in India looks promising. Indian telecom major Bharti Airtel is all set to merge with its South African counterpart MTN, with a deal worth USD 23 billion. According to the agreement Bharti Airtel would obtain 49% of stake in MTN and the South African telecom major would acquire 36% of stake in Bharti Airtel.

**What went wrong in M&A**

When you merge cultures well, value is created. When you don't, value is destroyed. While some will suggest other factors – silly things like objectives and strategies and implementation – they are all derivative. The game is won or lost on the field of cultural integration. Get that wrong and nothing else matters.

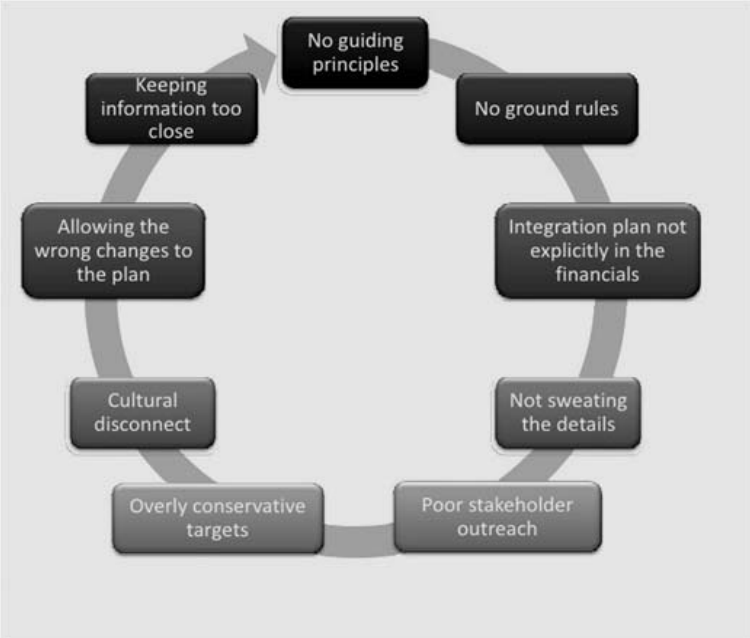
The fundamental premise of any merger is that the merging entities will be more valuable together than they are separately. It doesn't matter if you define value as shareholder equity, impact on the world or basic happiness. A merger is supposed to be an exercise in value creation. Yet, many of mergers fail. The vast majority of leaders get something very wrong along the way.

1. **Create clearly the specific value from the merger.** O'Flaherty told me that "AOL and Time Warner wanted something specific from each other – but the outcome of what that actually looked like for customers was never thought through, nor delivered." And he questions whether Verizon and AOL are "poised to make the same mistakes again." Specificity around how new value is created is key.
2. **Complete integrate the two businesses.** We've all seen organizations that acquire another organization and then run them as wholly owned, separate entities. You can't possibly realize synergies out of separate organizations. Synergies must be created together by teams looking beyond themselves to new problems they can solve for others.
3. **Cultural Compatibility**. O'Flaherty pointed out the cultural clash that occurred between AOL and Time Warner may happen again. Verizon is all about engineering while AOL is "more creative, more salesy." No way those two can come together well without some intensive therapy.
4. **A few examples of failed M&A deals:**
   - Ebay's (EBAY) purchase of Skype for USD 2.6 billion, later to be sold at just USD 1.9 billion after four years, was a failure due to challenges in technical integration and over-expectations from customers. Ebay expected synergy coming from Skype being established as the communication medium between buyers & sellers on its marketplace platform, which unfortunately did not become popular among its market participants.
   - Wendy's USD 2.3 billion merger with Arby's in 2008 was a disaster, which forced the split and sale of Arby's in 2011. Apparently, Arby's lack of international exposure made it a misfit to Wendy's.
   - Daimler Chrysler's USD 36 billion mega merger failed due to cultural differences, primarily due to continued focus on different customer bases. The merger,

which could have been a really big synergy across multiple client segments, ended up a costly failure due to cultural differences and integration issues.

- Quoted as the worst deal in the American financial history, Bank of America's acquisition of Countrywide in 2008 for USD 2.5 billion cost it more than USD 40 billion USD, due to financial losses, legal costs and associated expenses.

**Signs of Mergers Failure**




(Source: http://strategy insight blog spot .com)

**Theoretical Valuation V/S the Practical Proposition of Future Benefits**:

The numbers and assets that look good on paper may not be the real winning factors once the deal is through. The failed case of Bank of America's acquisition of Countrywide is a typical example.

- **Lack of clarity and execution of the integration process**: A major challenge for any M&A deal is the post-merger integration. A careful appraisal can help to identified key employees, crucial projects and products, sensitive processes and matters, impacting bottlenecks, etc. Using these identified critical areas, efficient processes for clear integration should be designed, aided by consulting, automation or even outsourcing options being fully explored.
- **Issues on Cultural integration:** The Daimler Chrysler case is a study of the challenges inherent in cultural and integration

issues. This factor is also quite evident in global M&A deals, and a proper strategy should be devised either to go for hard-decision forceful integration setting aside cultural differences, or allowing the regional/ local businesses run their respective units, with clear targets and strategy on profit making.

- **Capacity potential vs. current bandwidth**: The deals with purpose of expansion require an assessment of current firm's capacity to integrate and build upon the larger business. Are your existing firm's resources already fully or over utilized, leaving no bandwidth for the future to make the deal a success? Have you allocated dedicated resources (including yourself) to fill in the necessary gaps, as per the need? Have you accounted for time, effort and money needed for unknown challenges which may be identified in the future?

- **Actual cost of a difficult integration & high cost of recovery:** The Daimler Chrysler case also ran up high costs toward the expected integration attempts, which could not sail through. Keeping bandwidth and resources ready with correct strategies which can surpass the potential costs and challenges of integration could have helped. Investments today in a difficult integration spread over the next few years may be difficult to recover in the long run.

- **Negotiations errors:** Cases of overpaying for an acquisition (with high advisory fee) are also rampant in executing M&A deals, leading to financial losses and hence failures.

- **External factors and changes to the business environment**: The Bank of America/Countrywide failure was also due to the overall financial sector collapsing, with mortgage companies being the worst hit. External factors may not be fully controllable, and the best approach in such situations is to look forward and cut further losses, which may include completely shutting down the business or taking similar hard decisions.

- **Assessment of alternatives**: Instead of buying to expand with an aim to surpass competitors, is it worth considering being a sale target and exit with better returns to start something new? It helps to consider extreme options which may prove more profitable, instead of holding onto the traditional thoughts.

- **The backup plan**: With more than 50% of M&A deals failing, it's always better to keep a backup plan to disengage in a timely manner (with/without a loss), to avoid further losses. The above mentioned examples although are cited as failed, but they do seem to have executed the de-merger in a timely manner.

**Causes of Failure of M & A**

- **Overpayment:** This is very common cause of failure of acquisition & mergers.

  De Pamphilis D. (2005) found that overpayment often has destroys consequences. Overpayment leads to expectation of higher profitability which is not possible. Excessive goodwill as a result of overpaying needs to be written off which reduces the profitability of the firm.

- **Issues on Integration:** Strau(2007) studied that business cultures, work ethics, etc. needs to be flexible and adaptable.

Inefficiencies or administrative problems are a very common occurrence in a merger which often nullifies the advantages of the mergers.

- **Faulty Strategic Planning and unskilled execution:**
  - Schuler, R.S. Jackson, S.E. Luo,(2004): Faulty Strategic Planning and unskilled execution often leads to problems over expectation of strategic benefits is another area of concern surrounding mergers. These issues lead to failures of mergers.
  - Mike Harriso (2001) found that planning is a crucial exercise that will help determine the success or failure of a merging organization. However, many merging organizations do not have adequate or complete integration and implementation plans in place. Only one out of five companies that have acquired another has developed a clear and satisfactory implementation plan.
- **Corporate Culture Differences:**Irene Rodger(1999) Business International states that poor communications and inability to manage cultural differences are the two main causes of failed mergers.
- **Cultural differences:** Maria Koul, that cannot be resolved affect communications, decision-making, productivity and employee turnover at all levels of the organization. All the best laid plans – exhaustive analyses of strategies, marketing tactics, legal issues, etc. – can fall apart if the people cannot work together. If the two workforces fail to unite behind the strategic goals underlying the consolidation, even the best financial deals and most rigorous legal contracts fail to guarantee success.
- **Loss of Customers:**Wayne R. Pinnel (2001) found that all companies need to remember: it's the people who produce profits, represent the company, establish rapport with the customers, and, ultimately, are the ones that will make the combined company succeed."
- **Power Politics:**Randall S. Schuler, Susan E. Jackso (2001) observed that there is a tendency to assume that power disputes are more common in the case of acquisitions than mergers, there is no such thing as "a merger of equals". Further, it was clear that the distribution of power was not equally spread out. "We felt like we were marrying up, and it was clear that they thought they were marrying down."
- **Personnel motives:**Kellor R. Dixo(2000) found that managers often enters into Personnel motives: Kellor R. Dixo mergers to satisfy their own personnel motives like emire building, fame higher managerial compensation, etc. As a result they often lose focus on the fact that they need to look at the strategic benefits of the mergers. As a result, mergers that don't necessarily benefit the organization are entered into. These executives enter into these mergers for the purpose of seeking glory and satisfying their executive ego; leading to failure of mergers.
- **Lack of Communication:**Peter Dixo(1998)**,** a merger expert at Braxton Associates, found that lack of information, no clear direction and confusing messages, all boil down to uncertainty, which is destructive. It is really very important to be

clear and consistent, even if the messages may not always be positive for everyone.

- **Ignorance:** While the parties to a merger or acquisition cannot exchange commercially sensitive information prior to being under common ownership, there is enough crucially important and legally permissible preparation work to keep an integration team busy for several months before day one. Most chief executives don't know this and they waste the time that could be put to good use while they await clearance from the regulatory authorities. Good preparation means the integration can kick off on day one. Speed matters.

- **No common vision:** In the absence of a clear statement of what the merged company will stand for, how the organisation will operate, what it will feel like, and what will be different compared to how things are today, there is no point of the convergence on the horizon and the organisations will never blend.

- **Nasty surprises resulting from poor due diligence:** This sounds basic, but happens so often.

- **Team resourcing:** Resource requirements are very often underestimated. It can take two or three months to release the best players from daily business to join the integration team(s), find a backfill for them, sign up contractors to fill the gaps and set up the team's infrastructure. Most companies start too late and are not ready on once the deal is completed.

- **Poor governance:** Lack of clarity as to who decides what, and no clear issue resolution process. Integrating organisations brings up a myriad of issues that need fast resolution or else the project comes to a stand-still. Again: speed matters, but with a sound decision-making process.

- **Poor communication:** Messages too frequently lack relevance to their audience and often hover at the strategic level when what employees want to know is why the organisation is merging, why a merger is the best course action it could take, in what way the company will be better after the merger, how it will "feel", how the merger will affect their work and what support they will receive if they are adversely impacted.

- **Poor programme management:** Insufficiently detailed implementation plans and failure to identify key interdependencies between the many workstreams brings the project to a halt, or requires costly rework, extends the integration timeline and causes frustration.

- **Lack of courage:** Delaying some of the tough decisions that are required to integrate two organisations can only result in a disappointing outcome. Making those decisions will not please everyone, but it has the advantage of clarity and honesty, and allows those who do not find the journey and destination appealing to step off before the train gathers too much speed.

- **Weak leadership:** Integrating two organisations is like sailing through a storm: you need a strong captain, someone whom everyone can trust to bring the ship to its destination, someone who projects energy, enthusiasm, clarity, and who communicates that energy to everyone. If senior managers do not walk the talk, if their behaviours and

ways of working do not match the vision and values the company aspires to, all credibility is lost and the merger's mission is reduced to meaningless words.

**Suggestions for Successful M&A's**

Several initiatives can be undertaken in order to prevent the failure of mergers and acquisitions. Following are those:

- Continuous communication is of utmost necessary across all levels – employees, stakeholders, customers, suppliers and government leaders.
- Managers have to be transparent and should always tell the truth. By this way, they can win the trust of the employees and others and maintain a healthy environment.
- During the merger process, higher management professionals must be ready to greet a new or modified culture. They need to be very patient in hearing the concerns of other people and employees.
- Management need to identify the talents in both the organizations who may play major roles in the restructuring of the organization
- Identifying opportunities for providing competitive benchmarking measurements for fast improvement in company.
- Measuring market and technical trends to forecast future growth potential of company's technology.
- Personal ambition/motives of industry & financial reward which the firm will earn due to M&A should be targeted.
- Big takeover attract media and boosts up reputation but companies should link reward to growth. Peer Pressure and Pressure from advisers & media to do takeovers should be taken care of.
- Over-confidence should be taken care ofand concern that firm may be left behind.
- The surplus cash and high share price and Bargain hunting & asset stripping should be taken care.
- Motive should be to extend the business-locations, markets, and globalisation
- Improving negotiation and price by knowing the company's exact market position.
- Providing credibility and insurance to investors and bankers.
- Measuring customer attitudes on company's products to indicate their image in market.

**Managerial Implication**

Mergers and Acquisitions are risky; they can fail for any one of the above reasons. In reality it is a combination of mistakes that lead to most failures. Success requires planning, strong management and good advice. Putting the gloom to one side for a moment, the upside of successful acquisitions can be substantial. They can make money in their own right, and they can also bring commercial or tactical advantage to the enlarged acquirer. The proof lies in the highest rated companies. Very few of the world's top businesses have achieved success without acquisition. A healthy balance of buying – and selling – companies, entering into joint ventures, licence or distribution agreements and organic growth lay the foundation for success.Both the volume of deals and value at stake make M&A at once an important

phenomenon in business. In this context, understanding and gaining an insight into M&A becomes not only important but imperative as well. For this, an integrated view towards doing deals that extends beyond the pure finance-based elements of deal making is essentially needed. The firm first strategizes about a deal, executes the deal, and then realizes the value is used. While the areas of focus for successful Mergers &Acquisitions are: Strategy,Finance, Marketing, Operations, Human Resources, and Systems, there are scores of Cross-Enterprise Considerations for their success also that need to be taken into account. Acomprehensive theoretical framework that helps gain a real insight to M&A should touchupon the roles, duties, and governance aspects of the primary stakeholders involved.

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