Mergers and Acquisitions

Mergers and Acquisitions part 5

Narrator:

It's widely accepted that in roughly 80% of deals the value lies with the seller. In order words in purely financial terms the buyer tends to lose out. Yet despite this there seems to be a growing appetite by companies that the people who run them to take the risk. In Part 5 of this interview Ian Wilson discusses why that is. First Chief Executive Officers.

Ian Wilson:

CEOs of public companies are incentivised to grow the share price. And acquisitions are one way of doing this. Acquisitions are also part of strategy in action. It's a tool for re-shaping portfolios.

And of course they involve significant resources and once they're enacted they're not easily reversible.

It is a way of growing the top line of a business. Its also quite high profile because the CEO will be intimately associated with the deal. And the analysts are looking to CEOs to demonstrate their credibility to grow the share price and to demonstrate that they understand how the markets are progressing.

There's a lot of ego involved because the CEOs are very much in the spotlight of the analyst. And when a business comes in to play for being acquired and target companies are involved in that deal they won't want to lose out.

Narrator:

Second, Internal Pressures.

Ian Wilson:

Remember that the management associated with the deal are normally on a fairly substantial incentive to get that transaction to close. And that can typically equate to a year's salary for the senior management and key people. Now once the deal's been done and they are part of the vendor's organisation of course life can be very different.

Narrator:

Third Pressure from Advisers.

Ian Wilson:

The reason that the seller ends up invariably willing in around 80% of deals is the role of advisers and the competitive element. That the seller's advisers will be incentivised to maximise the price of the deal in terms of their own remuneration.

There's a strong competitive element from purchasers where CEOs don't want to be seen to have lost an important strategic deal in their sector. And so they're looking for every opportunity to get that deal to justify the price.

And they're putting in synergies that are just not realistic.

The advisers are uniquely compensated really for getting deals done. For example the advisers who advise the selling company will be compensated according to the value of the eventual transaction.

And quite often there's a ratchet involved such that they're heavily compensated for squeezing out the last little bit of additional value.

Similarly on the acquirer's side they will have advisers looking at financial models, various risks associated with environmental liability and pension liabilities.

And all these people will only get paid if the deal actually gets done. Undoubtedly there's a lot of snouts in the trough.

Particularly with the banks who would be involved not only in advising a purchaser on the deal but they may get involved with the rights issue for the funding. They might get involved with debt finance, a private placement or issuing bonds.

And all these additional services have fat fees associated with them.

Then of course there are financial advisers who are often auditors to the company although in recent times there's been a need to separate those two functions.

There are environmental advisers. There will be actuaries advising on pensions. Then of course there are the law firms who have got specialist advisers on HR. You'll also have people looking at the assets of the company to decide in what condition they are.

So there's a whole raft of people. And all these people will only get paid or at least they'll make their most money if the deal actually gets done.