

MOTIVATIONS OF MERGER AND ACQUISITIONS (M&A)

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ABSTRACT

This study was carried out to gain more understanding on Merger and Acquisitions (M&A) and secondly to identify the drivers that motivates companies to go for M&A. The authors reviewed 13 related journals and found that one of the main reason companies decided to enter M&A was because to increase management effectiveness and efficiency. The authors also found that the term synergy is variously being used in M&A. Basically, in a simple word synergy can be expressed as one plus one equal to three. It can be also defined as the potential financial benefit can be accomplished through the merging of companies. As we know, mergers and acquisitions (M&A) activity can also rebalance and enhance firm business operation either in term of product and services offered and market portfolio.

Keywords: Mergers and Acquisitions (M&A), Motivations and Synergy.

1. Introduction

Merger and Acquisition (M&A) activities in Malaysia obviously started in the 1970's which were largely confined to oil palm and rubber plantation companies. The involvement of foreign companies in the M&A activity was also noted to be quite significant especially in the plantation sector. In the 1980's, rapid growths particularly in the industrial sector coupled with the privatisation policy have boosted many companies to become more acquisitive in diversifying their businesses. Among the major acquisitions in the 1980's was UEM took over the North South Highway Project (PLUS) in 1987 (Maran, 2008).

In finance sector, Bank Negara Malaysia (BNM) has set 31 March 1998 as the deadline for the finance companies to identify their merger partners and agree in principle to the terms and conditions of the merger. During that time, there were 6 anchor finance companies that have agreed to merge with other small finance companies. The 6 anchor finance companies are Mayban Finance Bhd, Public Finance Bhd, Hong-Leong Finance Bhd, Arab Malaysian finance Bhd, EON Finance Bhd and Credit Corporation (Malaysia) Bhd and United Merchant Finance Bhd.

Besides finance companies, two other banks that involved in acquiring finance companies were Affin Holdings Bhd and Bank of Commerce. However nowadays, not only finance and

bank going for M&A, but also other sectors. For example Hicom Holdings Bhd merged with Diversified Resources Bhd (DRB) and DRB-Hicom and Proton going for acquisition. E&Y (The Sun Daily, 22 Oct 2013) also reported that by end of 2013, the local takaful industry is expected to see some (M&A) activities over the next few years.

According to the World Economic Forum data, the three-year average (2009-2011) of the dollar value of mergers and acquisitions occurring in Malaysia as a percent of the total global value is 0.54. From 2009-2011, Malaysia's share of the total number of M&A deals worldwide was 1.7%. For the same time period, the mergers and acquisitions transactions value as a percentage of the Gross Domestic Product in Malaysia was 5.76 (Chang and Teo, Global Legal Insight).

Thus, this paper seeks to provide further understanding on M&A and the motivations of companies going merger and acquisitions (M&A).

2. Literature Review

2.1 Definition of Merger and Acquisitions

The term of merger and acquisitions had been used interchangeably. Basically merger is the combining of two firms which is known as acquiring firm and targeted firm. The acquiring firm will remain to exist while the targeted firm or basically the weak firm will come to an ends. Gaughan (2002) defined merger as a combination of two companies in which only one company survives and the merged company ceases to exist, whereby the acquiring company assumes the assets and liabilities of the merged company. Gaughan (2007) also defines merger as 'a combination of two or more corporations in which only one corporation survives'. He further stated that the acquiring company assumes the assets and liabilities of the merged firm. Motis (2007) refer to corporate reorganizations that serve to transfer ownership control from one firm (the target) to the other (the acquirer), strictly speaking, they are different. Alexander et al (2003) defined as the combination of two or more companies into one new company or corporation. The main difference between a merger and an acquisition lies in the way in which the combination of the two companies is brought about.

2.2 Definition of Synergy

One important thing that can be said about M&A is synergy. Many books identify one of the advantages of going M&A it can create synergy. Vijgen (2007) defined synergy as the value of the merged part is greater than the sum of the target and bidder alone and Charles et al (2008) explained synergistic acquisitions as acquisitions where the value of the combined firm is larger than the sum of its parts.

2.3 Motivations of Mergers and Acquisitions

According to Alexander et al (2003), there were several drivers that motivate companies go for M&A. Some were discussed below:

2.3.1 A requirement for specialist skills and/or resources.

A company sometimes seeks to merge with or acquire another company because the company is keen to acquire a specific skill or resource owned by the other company. This type of merger or acquisition often occurs where a smaller company has developed high-value specific skills over a number of years and where it would take an acquiring company a long time and a great deal of investment to develop these same skills.

2.3.2 Globalisation drivers.

Increasing globalisation, facilitated to a considerable extent by the growth and development of IT, tends to encourage mergers as the geographical separation between individual companies becomes less of an obstacle to organisations working together as single entities, both within the same countries and across international boundaries. In the UK several large high street banks have been successfully acquired by a major Australian bank.

2.3.3 Diversification drivers.

A company may want to diversify into new areas or sectors as a means of balancing the risk profile of its portfolio. Diversification was a primary driver of many mergers and acquisitions in the 1960s, 1970s and 1980s. More recently there has been a discernible move away from diversification as a risk-management strategy. Numerous researchers and practitioners have argued that diversification and non-related acquisition does not in fact reduce the risk profile faced by an organisation. This argument is supported by the assertion that the more diversified an organisation is, the less it has developed the specific tools and techniques needed to address individual problems relating to any one of its range of business activities.

2.3.4 Capacity reduction.

The total production in a given sector may exceed or be near to demand so that the value of the product is low. In some cases it may be desirable for a company to merge with or acquire a competitor in order to secure a greater degree of control over total sector output. If company A acquires company B, company A has achieved greater control over total sector production and also has the opportunity to maintain more of its own production facilities and employees within the new company at the expense of company B.

2.3.5 A drive for increased management effectiveness and efficiency.

A particular company may have a deficit in management expertise in one or more key areas. Such areas may be 'key' because they are central to a new growth area the company is seeking to develop, or because they relate to the achievement of

new strategic objectives that have just been established. Paul (2001) argues that firms may combine their operations through mergers and acquisitions of corporate assets to reduce production costs, increase output, improve product quality, obtain new technologies, or provide entirely new products. The potential efficiency benefits from mergers and acquisitions include both operating and managerial efficiencies.

2.3.6 A drive to acquire a new market or customer base.

A merger or acquisition can often provide a fast-track route to new and established markets. If a large high street bank merges with another bank, each bank acquires the customer base of the other bank. In some cases the acquired customer base may represent a market that was previously unavailable. For example one bank may have previously specialised in business customers and the other bank in domestic customers. The new arrangement provides a more balanced customer base. This is supported by Isaac et al (2013). He mentioned that market motive aims at entering new markets in new areas or countries by acquiring already established firms as the fastest way, or as a way to gain entry without adding additional capacity. Wang et al (2012) states that the companies will utilize M&A to improve their market share and the entry barriers for other companies, and thus they can make profits by fixing prices autonomously. Black et al (2001) also agree the motives for M&A is for entry new markets.

3. Conclusion

Based on the above information, the authors can conclude Merger and Acquisitions (M&A) never can be an ending story in any companies in the world. Since it began in early Years 1990s, the functions of M&A still encourage many companies to enter the activities with the hope that to make some adjustment, improvement or rebalance their business operations.

Companies that enter into M&A not only focusing on making more profit but also with the aim to create synergy. Synergy here means one plus one will not be two but could be more than three. It means that the creation of synergy may enhance the company's profitability, efficiency and be more sustenance in the market. So, this is one the reason that drives companies for M&A.

4. Recommendation

This is a conceptual paper that has been written by the authors with the aim to share the basic knowledge and the motives of companies going for Merger and Acquisitions (M&A). Many areas can be explored in M&A. The authors are expected to expand the future study by focusing on the performance of companies after going merger and acquisitions (M&A).

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