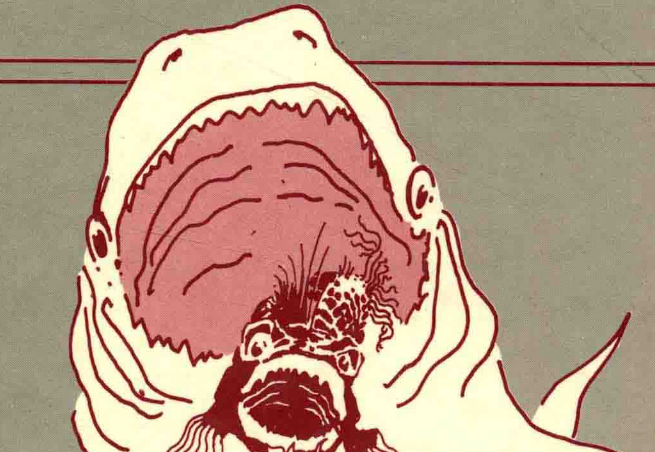
The TAKEOVER GUIDE



an Moore & Kit Stenning

Longman

The Takeover Guide

Brian Moore
and
Kit Stenning

Longman

ISBN 0–85121–363–4

Published by

Longman Professional and Business Communications Division
Longman Group UK Limited
21–27 Lamb's Conduit Street, London WC1N 3NJ

Associated Offices

Australia	Longman Professional Publishing (Pty) Limited 130 Philip Street, Sydney, NSW 2000
Hong Kong	Longman Group (Far East) Limited Cornwall House, 18th Floor, Taikoo Trading Estate, Tong Chong Street, Qarry Bay
Malaysia	Longman Malaysia Sdn Bhd No 3 Jalam Kilang A, Off Jalan Penchala, Petaling Jaya, Selangor, Malaysia
Singapore	Longman Singapore Publishers (Pte) Ltd 25 First Lok Yang Road, Singapore 2262
USA	Longman Group (USA) Inc 500 North Dearborn Street, Chicago, Illinois 60610

A CIP catalogue record for this book is available from the British Library.

Printed in Great Britain by
Biddles, Guildford

The Takeover Guide

Preface

This book has evolved from the business relationship of the authors.

Brian Moore now runs his own management consultancy business supplying executive management services to a wide range of companies especially in the light engineering/electronic sectors, having previously worked for some of the great names in British business.

Kit Stenning is a solicitor with the Prudential where he specialises in corporate finance related matters.

The authors first met each other when Brian was appointed Managing Director of a company in which the Pru had a material interest. Kit was heavily involved in the 'legals' relating to that company.

The authors began writing this book in the spring of 1987. That was a particularly interesting time in the takeover world, as the Guinness affair began to unfold. This preface was written in November 1987, in the aftermath of the stock market crash of October 1987. The two completely different environments give an interesting perspective on the different attitudes in the way in which takeovers are conducted. Now that the stock market crash has, at any rate, temporarily put an end to the more speculative type of takeover, the authors believe that the basic business parameters which they have set out in this book are even more appropriate now than when they were initially formulated.

It is usual in prefaces to books to give acknowledgements to all those friends and colleagues who have either wittingly or unwittingly contributed their thoughts and wisdom to the contents. The authors freely acknowledge that they have, quite ruthlessly, begged and borrowed information and opinions from most of their colleagues and it would be invidious to single out anyone in particular. To one and all, thank you.

The opinions expressed in this book are the authors' and not, necessarily, those of their present or past employers.

Brian Moore
Kit Stenning

London
November 1987

Introduction

Takeovers impact right at the heart of managerial ambition and complex notions of power and personality frequently surface in the takeover arena. It is a fertile area for management to 'do their own thing' because it offers opportunities to achieve growth and changes in direction on timescales not usually possible when developing and growing a business from internally generated or externally raised funds.

A research project indicated that 50% of all acquisitions 'are not considered successes' by those responsible for implementing them. It is difficult to ascertain quite what this means since it contains a number of imponderables and changing circumstances. With this book at your side, you have every chance of being able to demonstrate that your acquisitions come within the successful 50%.

Our aim here is to provide a very simple straightforward guide to managers who are faced with planning and executing takeovers, probably for the first time. An attempt has been made to cover, to a greater or lesser extent, all types of takeover, ranging from multimillion bids for quoted companies down to small acquisitions of private companies; but the terminology used is more relevant to the acquisition of private companies. These differ from acquisitions involving quoted companies, in which, the professional advisers play a major part from the inception to the conclusion of the deal.

In any takeover management should concentrate on ensuring that the reasons for the acquisition match, or at least do not detract, from any operational implications of the resulting organisation. It should always be remembered that most of the people in merchant banking and the City community have little feel for operational aspects of the business and will rely heavily on management advice, backing personalities in the belief that a good manager will sort out most situations.

Due to the diverse nature of acquisition activity, little reliable research exists to explain why such a high proportion of acquisitions are unsuccessful, providing no significant material gain to either party. It is quite often a case of comparing apples with pears.

However, from the information available, the following factors are consistently present in a successful acquisition policy:

- acquiring companies in a similar industry;
- acquiring companies in growth markets;
- acquiring companies that have a high market share;
- prospective purchasers being prepared to provide senior management to targets, ideally within the first year.

Before embarking on any form of takeover activity it should be appreciated that considerable time and resources will be involved in investigation and negotiation, most of which will be expended whether the takeover succeeds or fails. Particular care should be taken if there is an aspiration that these costs will eventually be paid by the target company and/or from the proceeds of any share issue required to effect the deal.

One of the reasons that there has been considerably more takeover activity in recent times is the increased awareness by line management of the capital mechanisms available. For example companies can be acquired effectively without cash; the deal could be self-funded, or it may be effectively financed out of the target company's assets.

Always remember that the deal is not done until the contract is signed by both parties and even then there may be conditional aspects that could result in subsequent rescission.

Success will ultimately depend on commercial judgement, instinct, a good bit of horse-trading . . . and a little help from this book.

Have fun!

Contents

Part One
The Nature of Takeovers

1 The role of management

This book is mainly intended for company line managers who spend most of their time and effort running their own business but who ought to consider whether a takeover is the right way to develop their business; and, if so, the essentials which must be understood in order to be successful.

Takeovers demand the following of company managers:

- setting objectives;
- organising activities;
- motivating and communicating;
- measuring and controlling;

coupled with the essential need to inspire the people under the manager's control and influence.

Takeover activity requires all these basic skills to be applied, not only to the continuation of the manager's own business, but also to the management of the target business and the management of the takeover process.

As takeovers are a relatively infrequent event in a company's life it is likely that the manager will be exposed to several situations, relationships and advisers outside his previous experience.

It is assumed that experienced managers are able to manage their own business and the enlarged group after the takeover has been completed. Concentration is therefore necessary on the management principles that apply to the takeover process.

The manager responsible for the takeover should establish early on that:

- the reasons for acquisition (after evaluation of alternatives) are sound;

- the target specification is well defined, understood and communicated;
- responsibilities and accountabilities are defined, together with the timetable for the work of own subordinates and professional advisers;
- the negotiation process is properly orchestrated and involves the manager personally at the appropriate stages;
- momentum is maintained once the deal has commenced.

Perhaps the most unfamiliar aspect of takeover activity is dealing with the specialist advisers involved and the other outside bodies that may have an interest in the takeover. It is possible for the manager to be involved with any or all of the following at various levels depending upon the type of acquisition, any one of which could result in a completely disproportionate consumption of time.

Own company and target company's

- shareholders
- directors
- employees
- banks/financiers
- solicitors
- accountants
- merchant bankers
- consultants
- customers (debtors)
- suppliers (creditors)
- PR/advertising agencies

External

- government
- trade unions
- Stock Exchange
- media
- competitors
- pressure groups

Takeovers encourage entrepreneurs and also develop the entrepreneurial skills of functional line managers; remember, the 'risk profile' changes and the apparent comfort given by academic valuation methods and professional investigations should *not* be relied upon entirely.

Companies on the acquisition trail will be involving themselves in considerable resource commitment through executive time and professional fees. The opportunities and starting assumptions may be continually changing. The good manager should be continually assessing what he really set out to do.

The key characteristics of the target's business need to be evaluated with reference to the integration requirements and should include company direction, management style, available resources and managerial ambition.

Perhaps one of the most important tasks of management is to ensure that the many professional advisers involved are being used in a cost-effective manner. Therefore we have included in this book information about what professional advisers can do for you and how they should be briefed and managed. The manager should view these advisers largely as sub-contractors under his direction and should ensure that they are appropriate for the job, adequately briefed and well controlled. The target's advisers, if slow or not competent, will impact on your costs and time-scales. Wherever possible, therefore, the target's advisers should also be assessed and appropriate representations made if required. This can prove difficult.

Finally, the manager should be constantly aware that when all is said and done and the deal is complete the resultant business has to be managed in a practical, sensible and profitable manner. The ground rules will be established during the takeover process so a 'reality' filter with a dose of healthy cynicism is an ideal recipe for success.

2 Why takeovers?

The main reason companies acquire other companies is to further their corporate development by way of growth and expansion, but there are various refinements on this basic theme, and frequently there may be several reasons for a takeover. The whole process is frequently underwritten by the personal ambitions of the management who are generally pursuing a philosophy of 'the bigger the better'.

Any of the following factors, or combinations of them, may be the prime reason for a takeover being identified as the best method to achieve the objectives set out in the corporate plan.

- **Growth (usually of maintainable profits)** The reasons for growth need to be well defined and decisions made as to how that growth will be achieved. Takeovers most commonly occur when a company acquires businesses similar to itself and as a result of overhead reduction, it achieves higher profitability; ie they are usually buying an increased market share.

- **Enter new markets** It may be easier to buy a developed company in a market you wish to enter to obtain expertise. The economics of this choice need to be evaluated fully against the cost of entering the market by using your own resources.

- **Obtain new products** Products are essential to businesses and, while companies should not rely on buying other companies for new products alone, it often represents a cost-effective way of increasing a product portfolio. At this extreme the acquired business could be completely closed with the resultant overhead, and operating cost savings and the products transferred to the acquiring business, perhaps with just the immediate product support, eg sales and engineering, remaining.

- **Obtain skilled resources** It may be desirable to acquire a company to meet a skill shortage or to obtain some specialised equipment. This is particularly common in 'hi-tech' areas where small companies concentrate on niche parts of technology and are often collected together later by larger companies.

- **Obtain assets** It may be a cheaper way of obtaining capital assets than buying them outright. This is particularly true of distressed companies where assets may be available at a considerable discount and provided the acquiring company has the ability to integrate the assets, ie handle the transfer costs and any resultant closure costs, then this could be very cost-effective.

- **Diversification** This usually applies to conglomerate-type strategies where the financial characteristics of the business are the principal reason for acquiring. It is a relatively high risk strategy and usually requires the acquired company to have its own management skills with the acquirer providing the resources and/or environment for better performance.

- **Market protection** To eliminate and/or control the activities of competitors. A classic example would be where a few major companies are competing in a declining market in which overcapacity exists. The purchase and closure of a competitor could result in improved price/profit stability. This may create competition law problems. Ask your solicitor.

- **Supplies protection** Where a company considers itself vulnerable to a source of supply not under its direct control a takeover may improve stability and reduce the cost of supply.

- **Change of corporate status** Where a company organises a merger or takeover to achieve a change in status. For example, a private company may organise to be taken over by a quoted company as an alternative to 'going to the market'. This is called 'a reverse takeover' and is a difficult manoeuvre requiring professional advice.

- **Expand distribution channels** A target could be purchased for its distribution outlets and customer base. Reorganisation would then typically result in the closure of Head Office, and possibly production, thus producing a lower overhead-to-sales cost and therefore improving profitability.

- **Taxation benefits** In particular to achieve the benefit of tax losses. This area is, however, becoming increasingly more difficult and any perceived benefits from taxation should be thoroughly examined with a tax specialist before proceeding.