ARTICLE 4: CORPORATE MOTIVES FOR ACQUISITIONS

Prepared by: Oscar Kalu
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MOTIVES FOR ACQUISITIONS OR TAKEOVER

The most biggest takeover in recent time is the takeover of Sky a UK media company by Comcast a US media company which owns the NBC network and the Universal Pictures out bidding Disney whose already owns 39% of Sky and wanted to consolidate the two corporation to become the World single biggest media company.

Comcast out bid Disney and offer to pay $40bn (£30.6bn) in other word, the share price jumped to £17.28 per share. This represent 10.3% [(£17.28 / £15.67) -1] above the offer made by Disney for a share price (The Telegraph).

Motives for a corporate acquisition or a takeover can be split between **economic motives** and **managerial motives.**

Economic Motives

Economic motives has the concept of increasing shareholder value, either because the "target" company can be acquired at less than its true worth; and/or because the value of the two companies combined is greater than the worth of the sum of their individual values, because of the presence of synergies. The takeover of Sky is purely on economic motive as the synergy of the two companies would increase the value of the two companies. This is the case as we have seen the share price of Sky increasing from £15.67 to £17.28.

Economic motives has three types of acquisition:

i. Horizontal acquisition is where the target company is in the same industry and at the same stage of the "production chain" as the predator company. The motive for the acquisition is often either that of gaining market power or production economies. It can also be for cost savings in terms of supply chain, logistics and R&D.

ii. Vertical integration can either be upstream, with the acquisition of a supplier company, or downstream, with the acquisition of a customer company. The two companies involved are in the same industry, but operate at different level either upstream or downstream of the production process. The motive for such an acquisition may be cost economies (savings), but is more likely to be either security of supply, (with an upstream acquisition), or security of a customer-base, (with a downstream acquisition).

iii. Unrelated diversification is where the target company is in a different area of business to that of the predator company, although there may still be some overlapping activities, such as logistics or marketing, which then is often termed "**concentric**" diversification. The motive for such a diversification may be cost economies or may be some managerial (i.e. non-shareholder value focused), motivations.

Managerial Motives

Managerial motives occurs due to the problem of *agency theory* and the fact that corporate ownership is divorced from managerial control. The acquisitions may not be motivated by their impact on shareholder value, but by the benefits that they can bring to management.

Perhaps the most common motive beside all is to exploit the cost savings arising through economies of scale. These economies may occur in terms of the full range of business functions from input supplies, logistics, marketing, distribution, production activities, through to financing activities, (where significant scale economies can exist in terms of raising finance).

Synergy is common motivation for acquisitions. The term "synergy' relates to cost savings that are not specifically related to the issue of scale. Another motive for an acquisition is the need to "plug gaps" in a company's product range.

The issue of "critical mass" can also provide the motivation for an acquisition. This particularly applies in industries where there are very significant economies of scale and so larger companies in such industries can easily undercut the cost base of smaller rivals. In such industries, acquisitions may occur to help provide that critical mass; and for analogous reasons, small companies may allow themselves to be acquired because they lack the critical mass required.

Acquisitions can also be motivated by a management's desire to generate or restore growth, by acquiring companies in high-growth business sectors.

The final economic motivation would be the acquisition or enhancement of "market power" that will allow the company to reduce competitive pressures and so enhance profitability.

Oscar Kalu