

T.C
MARMARA ÜNİVERSİTESİ
SOSYAL BİLİMLER ENSTİTÜSÜ
İŞLETME ANABİLİM DALI
YÖNETİM VE ORGANİZASYON BİLİM DALI

MERGERS AND ACQUISITIONS

Yüksek Lisans Tezi

ARKIN BALIKÇIOĞLU

İstanbul, 2006

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Tez Danışmanı: PROF. DR. ŞULE İŞINSU ÖZMEN

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ÖZET

Küreselleşme ve teknolojik gelişmelere bağlı olarak firmaların büyüme amacı ile birleşme ve satın almalar konusunda yatırımlar yaptığı gözlemlenmektedir. Türkiye’de özellikle özelleştirmeler ve dış sermayenin gelişi ile birlikte konunun popülaritesi artmıştır. Ülkemizde birleşme ve satın almalar kurumsal anlamda tarihsel olarak yeni kavramlardır.

Bu çalışmanın amacı birleşme ve satın almaların arkasındaki nedenlerin, başarı ile sonuçlanmaları için yapılması gerekenlerin ve finansal başarı değerlendirme ölçütlerinin tanımlanması ile Türk ve yabancı firmalar arasında bu konularla ilgili karşılaştırmalar yapılmasıdır.

Araştırmada, Earnst & Young firmasının Birleşme ve Satın Almalar 2003- 2004-2005 Raporlarında yayınlanan listeler kullanılmıştır. Listelerde bulunan firmalara yollanan anket cevapları SPSS 13.0 programı aracılığı ile istatistiksel olarak değerlendirilmiştir.

Sonuçlara göre Türk ve yabancı firmalar arasında birleşme ve satın alma nedenlerinde belirgin farklılıklar bulunmasına rağmen başarı için yapılması gerekenler ve finansal başarı değerlendirme ölçütlerinde anlamlı bir fark bulunamamıştır.

Hem Türk hem yabancı firmaların başarı faktörleri konusunda görüş birliğinde olmalarına karşın dünyadaki yüksek başarısızlık oranı düşündürücüdür. Bu sonuç düşüncelerin fiiliyata dönüştürülmediği şüphesini uyandırmaktadır.

ABSTRACT

It has been observed that bound to globalization and technological developments, companies make investments in mergers and acquisitions in order to grow. The subject has become highly popular in Turkey especially with privatizations and incoming foreign investments. In Turkey, mergers and acquisitions are historically new subjects on corporate basis.

The purposes of this study were the identification of the motives behind mergers and acquisitions, necessary actions to succeed and financial success evaluation criteria and second, making comparisons between Turkish and foreign companies about the issues that are aforementioned.

In the research, lists that were published within Earnst& Young's Mergers and Acquisitions 2003-2004-2005 Reports have been used. The responses to the questionnaire that was sent to companies have been statistically examined by means of SPSS 13.0 programme.

According to the results, there were significant differences between Turkish and foreign companies about the motives, yet no significant differences have been found about necessary actions to succeed and evaluation criteria.

Even though there was a consensus among Turkish and foreign companies about the success factors, high failure rates of mergers and acquisitions around the world are thought provoking. This result raises doubts that ideas are not being put in practice.

ACKNOWLEDGEMENTS

There were times when I said to myself “ok that’s it, I’ve finished this thesis”, but I was always wrong and the week after I was saying to myself “ok that’s it, I’ll never be able to finish this thesis”. There were so many ups and downs one after another, and there were so many times when I felt depressed, trapped, hopeless and lost. However, there were always people who stood beside me, did not abandon me and believed in me.

For starters, I would like to thank all my family for always believing in me and helping me get up again when I felt that everything was going down as far as this thesis was concerned. They have always been right beside me and I know that they will always be. I know how lucky I am to have a family like you.

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1. INTRODUCTION

Just like the world itself, the business world of today is changing with an increasing acceleration. With the technological developments and enlarging globalization theme, even the newest things get obsolete in a blink of an eye while over competition is making it much harder for companies to survive than ever.

In order to continue existing in such a high speed medium with harsh conditions, companies not only strive to survive, but also are trying to grow since big fish always eat the smaller ones. The ancient jungle laws still apply no matter how much the world has been technologically and intellectually developed.

Having said that bigger entities stand a much better chance of surviving, mergers and acquisitions are becoming more popular every day as they look very attractive as a means of growth. It is not very surprising that mergers and acquisitions have reached an outstanding volume of 3,5 trio USD in the year, 2000. With the influence of globalization, mergers and acquisitions have gained a cross border feature as well. It is very common to see a deal taking place between companies of which headquarters are thousands of miles away from each other. One should also not forget that these deals do not come very cheap; on the contrary multi-billion-dollar agreements do not surprise the business environment any more.

However, mergers and acquisitions don't have a very good track record after the deals are done and dusted. It is known that almost 70 % of the transactions make the stockowners suffer. This tells us that companies still have not fully learned the key points to a successful integration. However, in a world where resources are limited, synergy that comes out of a merger or an acquisition which creates value out of nothing is priceless. Therefore mergers and acquisitions stay as a very popular theme both for business people and researchers to study on.

This study mainly focuses on the driving forces behind mergers and acquisitions, the determination of the actions to be taken to achieve success and how financial success is assessed by companies.

After this section, the study continues with **Chapter 2- Corporate Growth Strategies**, where internal and external growth strategies are introduced to the readers.

Chapter 3- Uncertainty Effect on FDI, mentions studies about the economical and political uncertainty effects on FDI volumes as well as sociocultural and global economical environments' positive and negative effects on FDI. The chapter also gives brief information about the progress that Turkey has achieved during single party government after 2002 elections.

In **Chapter 4- Definitions of Merger and Acquisition**, general information about the real issue of this study is given. Readers can find definitions and legal explanations regarding mergers and acquisitions which will make them acquainted with the basic material.

Chapter 5- Varieties of Takeovers talks about the kinds of mergers and acquisitions which happen to be horizontal, vertical and conglomerate takeovers.

Chapter 6- Driving Forces Behind Mergers and Acquisitions, - obviously - is about the driving forces behind mergers and acquisitions that make them so attractive for companies.

In **Chapter 7- Mergers and Acquisitions History**, an overview about the past of mergers and acquisitions in the USA, Europe and Turkey is given. The chapter is very interesting as it reveals the correlation between technological& economical changes with the merger and acquisition pace.

Chapter 8- Merger and Acquisition Process enlightens us about the stages that companies go through when a deal is made. This chapter summons the stages in three steps- planning, implementation and assessment.

Chapter 9- Financing Mergers and Acquisitions, gives information of how transactions can be financed. The exchange medium of the deals can be cash, stock or a combination of both. The chapter explains cases by examples and tables.

Chapter 10- Success Measures and Factors describes the elements that companies should think thoroughly when making the very important strategic decision of mergers/acquisitions. Any missing part of these elements can cause the collapse of a giant merger and it is up to the companies' skills to follow the right strategies to avoid any pitfalls. The chapter also gives information about companies' perception of success and which criteria they use during assessment.

The research continues with **Chapter 11- Research Design and Methodology**, in which the model and research methodology regarding the survey are explained.

Chapter 12- Findings presents the statistical findings that are obtained from the survey in tables. The tables are interpreted for clarification.

Finally, the research ends with **Chapter 13- Conclusion** summarizes the findings of the survey and conclusions are drawn about the hypotheses.

2. CORPORATE GROWTH STRATEGIES

Economic growth is an increase in quality and quantity of goods and services produced by a nation.¹ In micro terms, business units replace the term “nation” in the definition. Business units are basically after profits and continuity of the entity. Enterprises are said to be growing if an increase in profits, sales, exports, imports, assets etc. is realized. Achieving these goals necessitates a deeper market penetration and it is provided by meeting customers’ needs and drawing their attention. The most known tactics for this are developing the features of the existing products and services are coming up with new products that customers will prefer over other brands or widening of service network. Aside from these, a company may grow by working more efficiently and use its idle capacity, increasing its capacity, saving costs by efficiency increase, creating a competitive edge and economies of scale and scope. Such broadenings of operations and diversification of products bring along the need for reorganization of enterprises. As these refer to the quantitative aspects of growth criteria, the quality of products and services produced and the human resources of an enterprise refer to the qualitative aspect of growth.²

As enterprises strive to survive in the market (continuity), they also try to grow to maximize their profits. In order to grow in a continuous fashion, they should identify strategies. It could be a growth strategy, a stability strategy or a retrenchment strategy depending upon the current situation of the enterprise; however these all serve to the ultimate purpose of profiting and growing in the end. Growth strategies can be examined in two categories: internal and external.

2.1 Internal Growth Strategies

Enterprises that grow by new investments financed by loans or by its own funds that are created by means of its operations have a strategy of internal growth.

¹ “Economic Growth” http://en.wikipedia.org/wiki/Economic_growth_ (15.10.2005), p.1

² Göksel Ataman, *İşletme Yönetimi Temel Kavramlar&Yeni Yaklaşımlar*, 1st Edition, İstanbul: Türkmen Kitabevi, 2001, p.8

When the enterprise finds the necessary funds, it can widen its operations or start looking for new markets. Internal growth has two dimensions: horizontal and vertical.

2.1.1 Horizontal Growth

Horizontal growth happens as an enterprise broadens its operations within the same production level. Let's take a chocolate company as an example. If the company managers decide to open up a new factory or produce candy as well as chocolate, they mean to grow horizontally.

Enterprises usually go horizontal growth by product differentiation and market extension. What is meant by product differentiation is to change a product, so that it draws attention from customers, meets their needs better or is produced at better quality. For example, a new package with new colors, adding a different spice to a food product, making consuming goods more durable all contribute to differentiation of the product leading customers' preferences in favor of the brand. A market extension would provide the product meet new and more customers which would increase sales as a consequence.

2.1.2 Vertical Growth

Vertical growth strategies on the other hand come true if an enterprise succeeds in attaining production inputs by its own resources (backward) or set its own distribution channels (forward). An automobile company that establishes its own car dealer network, then it has achieved a forward vertical growth. And if a company that sells coats builds up its own warehouse and doesn't pay for storage to its supplier any more, then it has achieved a backward vertical growth.

2.2 External Growth Strategies

External growth is utilized when an enterprise chooses to acquire another firm partially or as a whole, merge with another firm or make strategic alliances. The main motives behind external growth are decreasing cost, integration of production functions, increasing sales, risk spreading, creating economies of scale and scope, entering a new

market and adding value to the enterprise by creating synergy. There are various forms of external growth strategies.

Trusts are organizations where two or more independent organizations lose their legal and economic entities to limit competition by controlling the production and distribution of a product or service, in other words to acquire monopolistic power.³ This type of organizations is under scrutiny by legal authorities such as the Competition Authority in Turkey. There are certain anti-trust laws and regulations, so that market players and consumers don't get hurt by the monopolistic power of trusts. Just like trusts, cartels are organizations formed to maintain monopolistic power in the market. The difference between trusts and cartels is that in cartels, parties don't lose their legal entities whereas in trusts they do.

A joint venture (often abbreviated JV) is a strategic alliance between two or more parties to undertake economic activity together. The parties agree to create a new entity together by both contributing equity, and they then share in the profits, losses, and control of the enterprise. The venture can be for one specific project only, or a continuing business relationship such as the Sony Ericsson joint venture.⁴ Reasons behind joint ventures are spreading costs and risks, improving access to financial resources, economies of scale and advantages of size, access to new technologies, entrance to foreign markets, acquiring raw materials and cheap labor. However, the main idea of a joint venture is to undertake a project with each party utilizing its core competencies hence creating synergy. Firms may have strong financial structures but not high technology. This is a typical motive for a joint venture.

Licensing is a form of strategic alliance which involves the sale of a right to use certain proprietary knowledge (so called intellectual property) in a defined way. This intellectual property may be registered officially, as in trademarks or patents, or just be sustained in a company as know-how.⁵ The licensee pays a fee and a royalty in return of the right to use whatever the agreement is about. Licensing especially comes

³ Princeton University, <http://wordnet.princeton.edu/perl/webwn?s=trust>, (17.10.2005), p.1

⁴ "Joint Venture", http://en.wikipedia.org/wiki/Joint_venture, (17.10.2005), p.1

⁵ "Licensing (Strategic Alliance)", http://en.wikipedia.org/wiki/Licensing_%28strategic_alliance%29, (17.10.2005) p.1

handy when there are trade barriers in a market or risks on foreign direct investments. International license agreements boil down to the idea of an enterprise exporting its intangible assets. It enables a firm to enter a market where foreign investment is forbidden and it also eliminates the necessity of market specialization and provides savings on logistics and customs tariff costs.

Foreign direct investment (FDI) is the movement of capital across national frontiers in a manner that grants the investor control over the acquired asset.⁶ FDI's can take place as mergers and acquisitions or Greenfield investment which is investment in new facilities or expanding existing ones. What a host nation would want the most is a Greenfield investment where capital flows in the host nation, investment creates job openings, contributes to the GNP and new technology and know-how is acquired. Acquiring new customers through new markets, increasing sales and profits, exploiting developing countries' markets, achieving low production costs are the main motives for companies which make FDI's. Interests of foreign industrial giants in Turkey's privatization programme and Turkey's content with their interest are because of the above mentioned motives.

Mergers and Acquisitions is a general term used for the combination of two or more firms. In mergers, two or more companies combine to form a new company whereas in acquisitions one company acquires another one while no new company is formed.⁷ Since next chapters go into the details thoroughly, just a narrow definition is given for now.

⁶ "Foreign Direct Investment", http://en.wikipedia.org/wiki/Foreign_investment, (17.10.2005), p.1

⁷ "Mergers and Acquisitions", <http://www.investopedia.com/terms/m/mergersandacquisitions.asp>, (17.10.2005) p.1

3. UNCERTAINTY EFFECT ON FDI

As globalization became more popular, economies of the world became more integrated which caused significant growth in capital flows to developing countries. Particularly in developing countries like Turkey, capital flow is an essential tool for mitigating economic problems such as capital shortage and current account deficit.

When a multinational firm decides to invest in a host country, there are many issues that must be taken into account. Besides firm-specific factors which are in correlation with size, technological advancement and efficiency of the firm, there are also factors of global environment and those that are pertaining to the host country such as policies, resources, sociocultural environment and uncertainties associated with economy and politics. Host country factors gain special importance when the economic and political indicators are highly volatile. In developing countries, political and institutional factors are main factors that affect the investors' confidence, which is magnified by market failure that result in pricing and foreign currency exchange rate instabilities. In his study, Lucas labeled three factors as political risk in countries where capital inflow is slow. These three factors were capital imperfections, differences in human capital and external benefits of human capital.⁸

3.1 Economical Environment

There are numerous studies that end up in different directions of relationships between economic uncertainty and FDI. The objectives of multinational firms to diversify location of production and to have the option of production flexibility often caused a positive relationship between uncertainty and FDI. This is because multinational firms pay more attention to gain market share and production flexibility than to the risk of uncertainty. The classical view that the higher the risk, the higher the return which supports this positive sign.⁹

⁸ Robert E. Lucas and Edward C. Prescott, "Investment Under Uncertainty", **Econometrica**, Vol:39, No:5, 1971, pp. 659–681.

⁹ Andrew B. Abel, "Optimal Investment Under Uncertainty", **American Economic Review**, Vol:73, No:1, 1983, pp. 228-233.

On the other hand, there are many other studies conducted by various researchers who designed their studies under different risk and production assumptions and found negative relationships with uncertainty and FDI. Itagaki developed such a model under various tax structures and concluded positive relationship.¹⁰ Some other models were developed by Goldberg and Kolstad, under the production flexibility¹¹, Sung and Lapan, for the case of strategic FDI¹² and they all found similar results.

3.2 Sociocultural Environment

The social and cultural influences on business vary from country to country. It is vital for a corporation to be aware of such factors if there is a desire to go and invest in another country. Corporations should be asking themselves if they know about the host country population's attitude towards foreign products, male and female roles in society, gender dominance, income segments, issues that the people are sensitive to, educational levels, religions and groupings etc. Sociocultural differences play a major role when it comes to the integration part of an M&A deal. Many mega mergers have gone through difficult times because of cultural clashes between the employees. In cross border M&A's, it is a well known fact that language may give rise to problems.

Socioculture is a diffused and complex concept which makes it hard to be analyzed. Apart from its complexity, sociocultural change is evolutionary and can not be preplanned whereas other environments such as political environment can be changed through preplanned reforms. A high degree of a nation's receptiveness to different sociocultures and business modes makes it attractive for FDI. This does not imply that the host country adopts foreign values and cultures, but it means it is flexible enough to accept developments and business practices in global marketplace.

¹⁰ Takao Itagaki, "The theory of multinational firm under exchange rate uncertainty" **Canadian Journal of Economics**, Vol: XIV, No: 2, 1981, pp.276-297.

¹¹ Linda S. Goldberg and Charles D. Kolstad, "Foreign Direct Investment, Exchange rate Variability and Demand Uncertainty", **International Economic Review**, Vol: 36, No:4, 1995, pp. 855-873.

¹² Hongmo Sung and Harvey Lapan, "Strategic Foreign Direct Investment and Exchange Rate Uncertainty", **International Economic Review**, Vol: 41, No: 2, 2000, pp. 411-423.

3.3 International Environment

One can not ignore the effect of global changes on FDI. The most striking evidence comes during crises times.

We have seen a recent example of this in Asia when the crisis occurred in the second half of 1997. In short and medium terms, the crisis had interesting influences in terms of inward FDI to the most affected regions, East and South East Asia. First, the dollar costs for foreign investors have decreased because of the decrease in the asset values and devaluation of the domestic currencies. Second, devaluation in these countries made them attractive as sites for export oriented investments. Third, the liberalization of government policies made it easier for foreigners to invest.¹³ On the other hand, there are adverse effects as well. Reduced domestic demand and slower economical growth have led to some canceling or postponing of investments.

Since the world became a global marketplace, every single move in one corner of the world has effects in another corner. Following the Russian debt moratorium, the capital flows from international markets to developing countries were cut in half of its value in 1998. Investors deserted emerging market instruments for safer and more liquid assets.

3.4 Political Environment

In the OECD Global Forum on International Investment, V.N. Balasubramanyam indicated some of the positive determinants of FDI as follows:¹⁴

1. Macro economic stability,
2. Political stability
3. A stable and transparent policy framework towards FDI

¹³ UNCTAD, "Room For Cautious Optimism on Foreign Direct Investment in Asia", **Press Release**, 08.09.1998, <http://www.unctad.org/Templates/webflyer.asp?docid=3172&intItemID=2024&lang=1>, (16.05.2006), p.1

¹⁴ V.N. Balasubramanyam, "Foreign Direct Investment in Developing Countries: Determinants and Impacts", **OECD Global Forum on International Investment**, Mexico City, 26-27 November 2001, p.2.

4. Distortion free economic and business environment

5. Fiscal and monetary incentives in the form of tax concessions (of little importance in the absence of economic stability)

Balasubramanyam indicates three aspects of low inflation rates and stable exchange rates. Firstly, they are good indicators of a stable and strong economy. Secondly, they provide a degree of certainty relating to the future course of economy and make it easier for firms to forecast their future budgets, cash flows and other financial decisions. Thirdly, a stable microeconomic environment implies a stable political environment as well because these two issues are usually dependent on each other.¹⁵

Although there are many studies that examine the relationship between the economical environment and FDI, there has not been as many that focus on political aspect of the FDI determinants. Most of the existing studies with regard to political environment concluded that the perception of this political environment in a host country is one of the most important determinants of FDI.¹⁶ Nigh's 1985 article examined the relationship between manufacturing FDI and political climate across 21 years and 24 countries. In his article, Nigh concludes that both international and intranational conflicts affect the US outbound FDI to developing countries significantly whereas only international conflicts are effective as far as developed countries are concerned.¹⁷

In 1990's most of the studies took a closer look at the influence of policy-related variables on FDI flows. Within these studies, Brunetti and Weder found a negative relationship between institutional uncertainty and private investment.¹⁸ Lee

¹⁵ V.N. Balasubramanyam, p. 4

¹⁶ Hans Schollhammer and Douglas Nigh, "The Effect of Political Events on Foreign Direct Investment by German Multinational Corporations", **Management International Review**, Vol: No: 1, 1984, pp. 18-40.

¹⁷ Douglas Nigh, "The Effect of Political Events on United States Direct Foreign Investment: A Pooled Time-Series Cross-Sectional Analysis", **Journal of International Business Studies**, Vol. 16, No. 1 (Spring 1985), pp. 1-17.

¹⁸ Aymo Brunetti, and Beatrice Weder, "Investment and Institutional Uncertainty: A Comparative Study of Different Uncertainty Measures", **Weltwirtschaftliches Archiv**, Vol. 134, No. 3, 1998, pp. 513-533.

and Mansfield indicated a positive link between FDI and intellectual property.¹⁹ Wei's study resulted in negative effects of corruption on FDI flows.²⁰

One of the most recent studies was conducted by Busse and Hefeker where they focused on the FDI data to 83 developing countries which covered a time span of 20 years. (1984- 2003)²¹ The aim of the study was to explore the role of political risk and institutions of host countries as determinants of FDI. The conclusion of the study was that government stability, law and order and quality of the bureaucracy were exceptionally closely related to incoming FDI.

As we turn to Turkey, what we see different than before is the reign of a single party in government. In 2002 elections, Justice and Development Party (AKP) has gained a sizeable majority in Parliament and constituted the government on its own. Since a single party government has occurred very rarely within the 60 years of multi-party regime, Turkey is experiencing a new model in the highly global world. When we examine the AKP's programme, we can say that the party recognizes the benefits of FDI. The advantage of a single party hides in its power to realize the necessary reforms fast. Coalition governments may have represented a larger share of the population; however certain obstacles hindered their flexibilities. With the advantage of majority of seats, AKP has its chance now and some changes have already been done.

For the last several years, Turkey has been going through a comprehensive economic reform with a series of restructuring reforms. With the strong backing of single party government, economy has gained power especially within the past three years. Starting from the financial sector, significant reforms have been carried out in agricultural, social security, energy and telecommunications sectors by the Government. Privatizations have been accelerated as it has never been before. Many projects that had been planned in the past related to privatization have come to life during the single party

¹⁹ Jeong-Yeon Lee and Edwin Mansfield, "Intellectual Property Protection and US Foreign Direct Investment", **Review of Economics and Statistics**, Vol: 78, No: 2, 1996, pp. 181-186.

²⁰ Shang-Jin Wei, "How Taxing is Corruption on International Investors?", **Review of Economics and Statistics**, Vol. 82, No. 1, 2000, pp. 1-11.

²¹ Matthias Busse and Carsten Hefeker. "Political Risk, Institutions and Foreign Direct Investment", 2005, Hamburg Institute of International Economics, <http://www.hwwa.de/Publikationen/DiscussionPaper/2005/315.pdf>, (10.05.2006) pp. 2-3.

government. In economy, single digit inflation rates that many citizens have never seen in their entire life are achieved. Many objectives of the economic programme are attained and successive high growth rates are obtained (5, 9%- 2003, 9, 9%- 2004 and 7, 6% -2005 are the official rates, but they are debatable considering stocks and debts). Being still high compared to European countries; interest rates have been shrinking down. During the last three years, productivity growth has reached 10% which is a positive sign for the sustainable development and competitiveness of Turkish economy. The membership to EU process has advanced and Turkey has become closer to achieve the Copenhagen and Maastricht criteria during the last three years.

In terms of FDI, Turkey's economical and structural uptake and EU progress have made the country more attractive for foreigners. With the privatization programme and huge energy and infrastructural projects, foreign investors started to think of Turkey as one of the most appropriate developing countries to enter. A crucial change has occurred in the "Foreign Investment Law" which dated back to 1954. In June 2003, a new law was enacted and the amendments were directly related to making foreigners' life easier. According to the new law, the old FDI approval and screening system with a notification and registration system, nationalization without fair compensation are replaced in favor of foreign investors. The new law also guarantees national treatment to foreign investors, does not restrict FDI in any sectors, does not impose any performance criteria, eliminates minimum capital requirement, grants transferability of capital and earnings, allows property ownership without restrictions. These changes in the law are good indicators of a solid determination of the government to attract FDI; however the real test will be taken when it comes to changing the mind sets of bureaucrats.²²

Having said these reforms, changes and improvements, these are all done in a 3 year span of a single party government. If Turkey had had a coalition government, then all these decisions would have been subjected to long discussions between partners while some of them would have never been realized. No doubt political stability has caused an economical improvement and stability as well which rendered foreigners'

²² Asım Erkilek, "A Comparative Analysis of Inward and Outward FDI in Turkey", **Transnational Corporations**, Vol: 12, No:3, (December 2003), p.93

trust in Turkey when compared to the past. All these developments and the strictly followed economical and structural reforms are important factors for the incoming all time high 17,5 billion USD from abroad both for M&A's, privatizations and TMSF sales in 2005. Turkey's credibility has been increased by all global financial institutions such as Morgan Stanley, Moody's, Fitch, Credit Suisse etc. This increase in credibility rates of course leads to decreases in both political and economical risk premiums of Turkey. Being risks lowered, foreigners are less afraid to come and invest in Turkey which causes FDI to increase.

4. DEFINITIONS OF MERGER AND ACQUISITION

As an external growth strategy, mergers and acquisitions have been one of the major instruments in business life. Mergers and acquisitions can be named as takeovers. Even though they may end with similar outcomes, they are functionally different themes.²³ After takeovers, companies that are involved get organically bonded. In this chapter, we are going to take a closer look at mergers and acquisitions respectively.

4.1 Definitions of Merger

A merger is generally the combination of two or more companies under the same business entity.²⁴ In the pure sense of the term, a merger takes place when two or more firms agree to continue their commercial lives as a new single company rather than separately owned and operated.²⁵ Accounting Standards Board (ASB) has defined mergers in Financial Reporting Standard (FRS) as:²⁶

“A business combination that results in the creation of a new reporting entity formed from the combining parties, in which the shareholders of the combining parties come together in a partnership for the mutual sharing of the risks and benefits of the combined entity, and in which no party to the combination in substance obtains control over the other, or is otherwise seen to be dominant, whether by virtue of the proportion of its shareholders’ rights in the combined entity, the influence of its directors or otherwise”

According to the Turkish Commercial Code (TCC) 146/I a merger is the formation of a new commercial enterprise by means of combination of two or more firms, or the assigning of one or more firms to another firm. However this definition ignores the factors of mergers. Other factors of mergers are indicated through TCC 146 to 151. Hikmet Sami Turk combines the definitions that are made in law, in court verdicts and in doctrine and defines mergers as the assigning of at least one commercial

²³ Prof. Dr. Cevat Sarıkamış, **Şirket Birleşmeleri**, 1st Edition, İstanbul: Avcıol Basım Yayın, 2003, p.3

²⁴ Prof. Dr. İsmail Mucuk, **Modern İşletmecilik**, 9th Edition, İstanbul: Türkmen Kitabevi, 1998, p.53

²⁵ “The Basics of Mergers and Acquisitions” <http://www.investopedia.com/university/mergers/mergers1.asp>, (18.10.2005), p.1

²⁶ The Accounting Standards Board, 1994, “Financial Accounting Standard 6”, <http://www.asb.org.uk/images/uploaded/documents/FRS%2061.pdf>, (22.10.2005), p.8

partnership to another with its assets and liabilities in compliance with universal succession principle as shareholders of the former receiving shares of the latter in return, resulting in dissolving without liquidation of the assigning company or the formation of a new commercial partnership by means of uniting assets and liabilities of two or more commercial partnerships in compliance with universal succession principle as shareholders of the assigning partnerships receive shares of the newly formed company in return, resulting in dissolving without liquidation of the assigning commercial partnerships.²⁷ The conceptual elements in this definition are the existence of at least two commercial partnerships and the passing on of assets and liabilities of the dissolving partnerships as a whole to another partnership which entitles the shareholders to receive shares of the company in which absorption occurs or of the newly formed company. As a result, at least two companies become one. The universal succession principle means that there is no need to evaluate the assets item by item. Instead they are transferred as a whole. Again it contains the meaning of companies don't have to re-register the fixed assets, delivery of movables and assignment of receivables with other routine procedures are not needed by law. The passing on of assets as a whole without liquidation refers to the continuity of possessions principle. As liabilities are also passed on to the new company, the company is responsible to the creditors for the debts of the assigning companies.²⁸

As it is defined, mergers can happen in two ways. First one is the absorption of one or more companies into another one, which is called an annexation. In cases of annexation, the company that is absorbed by another firm is dissolved yet not liquidated. The absorbing company is neither dissolved nor liquidated. Assigning company receives shares as much as it contributes to the merger. It is calculated by an exchange rate. Second way is the formation of a new company, which is called a consolidation. In consolidations, both firms dissolve without liquidation and pass their assets and liabilities in compliance with the universal succession principal. Companies receive shares accordingly with their contributes to the merger.

²⁷ Hikmet Sami Türk, **Ticaret Ortaklıklarının Birleşmesi**, , Ankara: Banka ve Ticaret Hukuku Araştırma Enstitüsü, 1986, p.38

²⁸ Akar Öcal, "Ticaret Şirketlerinin Birleşmesine Alacaklıların İtirazı Sorunu", **Esader**, V:10, Issue: 2, 1974 pp. 223–233

In order to prevent the creations of monopolies by means of mergers and acquisitions, competition laws have been set all around the world. If there had been no antitrust laws or regulations, free competition would have been self-destructed and monopolies and oligopolies would have prevailed. As a consequence, no small companies could have survived and consumers would have got hurt in this medium. In addition to that, governmental monetary policies would have stumbled since inflation would be triggered by price policies of monopolies and oligopolies. Therefore, the necessity of such laws and regulations is obvious. In Turkey, the Turkish Competition Authority is in charge of exercising the Act on the Protection of Competition. As it is said in the Act;²⁹

“ The purpose of this Act is to prevent agreements, decisions and practices preventing, distorting or restricting competition in markets for goods and services, and the abuse of dominance by the undertakings dominant in the market, and to ensure the protection of competition by performing the necessary regulations and supervisions to this end.”

Business entities that are defined in Article 2 of Communiqué 1997/1 are subject to notification and permission of the Competition Board when the conditions in Article 4 of the same Communiqué are concerned. Article 2 and Article 4 are given below as quoted from the Communiqué.³⁰

“Cases Considered as Merger or Acquisition (Article 2)

a) Merger of two or more previously independent undertakings.

b) Control or acquisition, by any undertaking or person, of the assets of another undertaking, or the whole or a part of its securities, or the means granting it the power to have a right in the management.

²⁹ Rekabet Kurumu, “the Act on the Protection of Competition”, 13.12.1994, Official Gazette <http://www.rekabet.gov.tr/word/ekanun.doc>, (02.11.2005), p.1

³⁰ Rekabet Kurumu, “Communiqué on the Mergers and Acquisitions Calling for the Authorization of the Competition Board”, 12.10.1998, Official Gazette, <http://www.rekabet.gov.tr/word/tebligeng1.doc>, (02.11.2005) pp.1-2

c) Joint ventures which emerge as an autonomous economic entity possessing assets and labour to achieve their objectives, and which do not have any aims or effects restricting the competition among the parties, or between the parties and the joint venture.”

“Mergers or Acquisitions Subject to Permission (Article 4)

Where total market shares of the undertakings that are parties to the merger or acquisition exceed 25 % of the market in the relevant product market within the whole territory of the country or a part of it, or even though they do not exceed this rate, their total turnovers exceed TL ten trillion, it is compulsory for them to take permission of the Competition Board.”

It should be noted that ten trillion TL limit has been increased to twenty-five trillion TL with a change in the Communiqué.

The TCC points out four basic elements in a merger; a written contract between undertakings, universal succession principle, dissolving without liquidation and continuity of share holding. The fourth element- continuity of share holding- is about the regulation that does not allow mergers to be made in exchange for cash. The regulation allows maximum 10% cash payment, but the rest of the payment should be in stocks.³¹ In addition, a merger can take place between companies that are of the same kind as defined in TCC. According to TCC, incorporations and commandite companies with capital in shares are of the same kind while unlimited companies and normal commandite companies are of the same kind as another group.

In summary, a merger should carry these elements:

- At least two companies
- Universal succession
- Dissolving without liquidation

³¹ Doğan Gökbel, Farklı Ülke Şirketleri Arasındaki Birleşmelerin Türk Hukukundaki Vergisel Sonuçlarının Avrupa Birliği Hukuku ile Karşılaştırılması, in: Haluk Sümer and Helmut Pernsteiner (Eds.), **Şirket Birleşmeleri**, 1st Edition, İstanbul: Alfa, 2003, p.30

- A written merger agreement between undertakings
- Stock exchange (cash payment is allowed up to 10%)
- Same kind of companies as defined in TCC

4.2 Definitions of Acquisition

Just like merger, acquisition does not have a specific definition. One definition says that an acquisition happens as one company taking control of another by purchasing a majority or all of the target company's outstanding shares.³² Another definition is the acquiring of the shares of a company or takeover of its assets and liabilities at their current prices.³³ It can also be defined as the buying of all or a part of a company by another company where the buyer maintains its entity as dominant while the other becomes a subordinate or affiliate of it. But we can define an acquisition shortly as the act of obtaining control of another corporation by purchasing all or a majority of its outstanding shares (share deal), or by purchasing its assets (asset deal). The controlling firm is referred as the acquirer and the firm that gets under control is referred as the target firm or the acquiree.

As it is said in the definition, the acquirer may possess all or a majority of shares of the target firm. If it succeeds in buying them all, then it is a full-acquisition and it is a majority acquisition otherwise. If it is a full-acquisition, the acquirer may choose either to absorb the target firm or keep it as a separate enterprise. If it absorbs the target, the target's legal entity ends, otherwise it continues as a subordinate or affiliate of the acquirer.

There are mainly three ways of approaching a target firm; offering to the target firm's managers, offering to the target firm's shareholders and acquiring the shares in second-hand market. Approach choice is closely related to the concepts of hostile and

³² The Global Banking Resource, "Financial Industry Terms", <http://www.tgbr.com/tgbr/terms.html>, (18.10.2005), p.1

³³ Haluk Sümer and E. Handan Sümer Göğüş, Füzyonlar ve Muhasebe Yöntemlerinde Meydana gelen Gelişmeler, in: Sümer and Pernsteiner (Eds.), p.361

friendly acquisitions. Friendly acquisitions take place when target firm's management and shareholders agree to sell the enterprise. Hostile acquisitions take place when the target firm's management and shareholders are against the sale. In cases where the acquirer makes its tender offer to the management and grants consent, the deal proceeds fast and easy. Such offers usually end up in a friendly acquisition. On the other hand, acquiring shares in second-hand market would probably encounter resistance by the target firm's management and shareholders resulting in a slow and expensive acquisition or a failing attempt.

In acquisitions, acquirers can do the payment in cash or in stocks. In friendly acquisitions, generally the payment is made in stocks whereas in hostile acquisitions, in cash. Multibillion USD acquisitions are obviously made in stocks since such large amounts of cash practically cannot be paid.

Even though the terms mergers and acquisitions are usually used as interchangeably, there are certain differences between them. In FRS, ASB has defined four criteria to be met by combination of firms for them to be mergers:³⁴

- Parties that are involved are neither an acquirer nor an acquiree.
- All parties that are involved participate in establishing the management structure for the combined entity.
- The relative sizes of the combining parties are not so disparate that one party dominates the combined entity.
- The shares of the undertakings are replaced by the shares of the merger; therefore it is necessary to hold the shares of the merger in order to claim any rights.

According to FRS, had not these criteria been met, combinations are not defined as mergers but as acquisitions. So the criteria that are mentioned above explain the differences between mergers and acquisitions clearly. One addition could be that in

³⁴ The Accounting Standards Board, 1994, "Financial Accounting Standard 6", <http://www.asb.org.uk/images/uploaded/documents/FRS%2061.pdf>, (22.10.2005), p.11

mergers, assigning undertakings dissolve while in acquisitions an acquiree doesn't necessarily dissolve depending on the acquirer's wish.

5. VARIETIES OF TAKEOVERS

5.1 Horizontal Takeovers

Horizontal takeovers are the mergers and acquisitions of units engaged in the same stage of production.³⁵ These units are rivals in the same sector and market almost all the time. Mergers of BP and Amoco, Exxon and Mobil, Citicorp and Travelers Group are such examples of horizontal takeovers. Most common type of mergers and acquisitions in the first half of the 20th century was horizontal.

The main motives behind horizontal mergers and acquisitions are increasing market power, attaining economies of scale, acquiring technology and know-how, saving money by cost-cutting and utilizing resources more effectively. By horizontal takeovers, companies can serve their customers better and more efficiently in terms of quality, price, availability and speed.

However, horizontal takeovers may cause some legal problems. Since such takeovers lessen the number of competitors, the Competition Authority may object to the transaction. In cases where a monopoly is formed within market, the Authority calls off deals. Anti-trust and anti-competitive legislations are set because such activities may harm other parties such as competitors, potential entrants and society. A monopoly that controls prices and other monetary factors of the market is against the welfare of society and a scarecrow for potential entrants. Therefore, as a government policy, merger deals need to be first approved by the Competition Authority for the avoidance of such outcomes. Globalization of economies, easy flowing of capitals, low entry barriers, fast developing technologies are other factors that stop monopolies. Today, companies usually choose horizontal takeovers in order to take place in national and international markets.

³⁵ Robert M. Allan, Jr. Expansion By Merger, in: William Alberts and Joel E. Segall (Eds.), **The Corporate Merger**, 1st Edition, Chicago and London: The University of Chicago Press, 1966, p.101

5.2 Vertical Takeovers

Vertical takeovers take place between firms that are in different positions within the value-added chain. In other words, these are the activities between firms that are related to each other on a buyer or seller basis for the production or marketing of a good or a service and working in sub-sectors of the same industry. One basic example for this could be between an automobile manufacturer and a rent-a-car service.

We can also divide vertical takeovers into two categories, backward and forward. In backward vertical takeovers, a buyer acquires or merges with a supplier of a good or a service. On the other hand, in forward vertical takeovers, a supplier acquires or merges with a buyer. The main idea is that a firm that is on an earlier stage of the value-added chain does forward vertical deals and vice versa for a backward vertical deal.

In 2000, the merger between Time-Warner and AOL was a vertical merger where Time-Warner started to use AOL's distribution networks for its movies, magazines and music. AOL acquired Time-Warner for \$160 billion in stock and the new company AOL/Time-Warner was worth \$350 billion having been the largest merger in history.³⁶

Possession of critical raw materials, gaining market power, raising entry barriers, cost reductions, better distribution network, increasing efficiency are the main motives behind vertical takeovers. Companies that do forward vertical takeovers can maintain strategically important distribution channels, so that it gets advantages over its competitors and gets closer to its customers and have a better chance of meeting their needs which strengthens its market power. By vertical integration, companies do not pay extra cost to other parties for procurement, storage etc. resulting in cost reductions. With backward vertical integration, manufacturing companies would not worry about raw materials or marketing companies about finished products. Also quality control becomes less effort consuming since the supplier is under control. Again anti-competition legislations should be carefully followed as in any type of mergers. For

³⁶ Guinness World Records, "Largest Company Merger" http://www.guinnessworldrecords.com/content_pages/record.asp?recordid=53969, (22.10.2005), p.1

example, when a company buys a distribution channel so that other competitors cannot distribute its goods, then an indirect monopoly would be formed and authorities would not overlook such a situation.

5.3 Conglomerate Takeovers

The third variety of takeovers is the conglomerate type. Conglomerate takeovers do not maintain the motive of increasing market power. The usual motive is the risk spreading issue. Therefore many applications do not get rejection from relevant authorities. However, authorities inspect the possible outcomes especially when same products, but different geographies are subject to the matter. Conglomerate takeovers can be divided into three categories; pure conglomerate, concentric and geographic market extension.

Pure conglomerate takeovers involve firms that are in unrelated businesses in every way. There is no linkage in terms of technology, production process, markets or sectors. Such takeovers were especially highly popular in 1960's and 1970's, however they started to lose that popularity by 1980's. Enterprises that wish to spread their risks by diversification through markets may choose this option to stabilize their profits and cash flows regardless of seasonal fluctuations. In pure conglomerate takeovers, only managerial learning, which is the managerial know-how and experience, can be transferred. Industry-specific managerial experience and non-managerial learning cannot be transferred since the merging units do not belong to the same industry and sector. Therefore, it is almost impossible to merge them physically. Only a union at top levels of management can be considered. The deal between Gillette and Duracell in 1996 was an example of pure conglomerate merger.

A conglomerate takeover is called as concentric when firms that are in the same industry, but not producing same products are involved. Diversification is the main goal in this type of mergers. Since firms function in the same industry, managerial, industry-specific managerial experience and non-managerial learning can all be transferred in-between firms. Therefore, managers don't encounter serious difficulties if

they want to combine the firms under one entity. A merger between a passenger car manufacturer and a truck manufacturer would be a concentric merger.

Takeovers between firms that are producing same kind of products in different geographies are called geographic market extensions. The ideas behind that are to enter new markets in different locations of the world and to acquire cheap raw materials and working force, which are compatible with the globalization theme. This brings up the cross-border mergers and acquisitions that became highly popular after 90's. Top executives share the top-level management in this type of takeovers. Aside from production and supplier units, managerial functional units are usually gathered in the headquarters of the new entity or the acquiring company. In cases where such reorganization causes problems, firms can be united under a holding and managed separately.³⁷ The merger between Vodafone (UK) and AirTouch (USA) was a geographical market extension where a European and American companies were involved.

³⁷ Sarıkamış, p.44

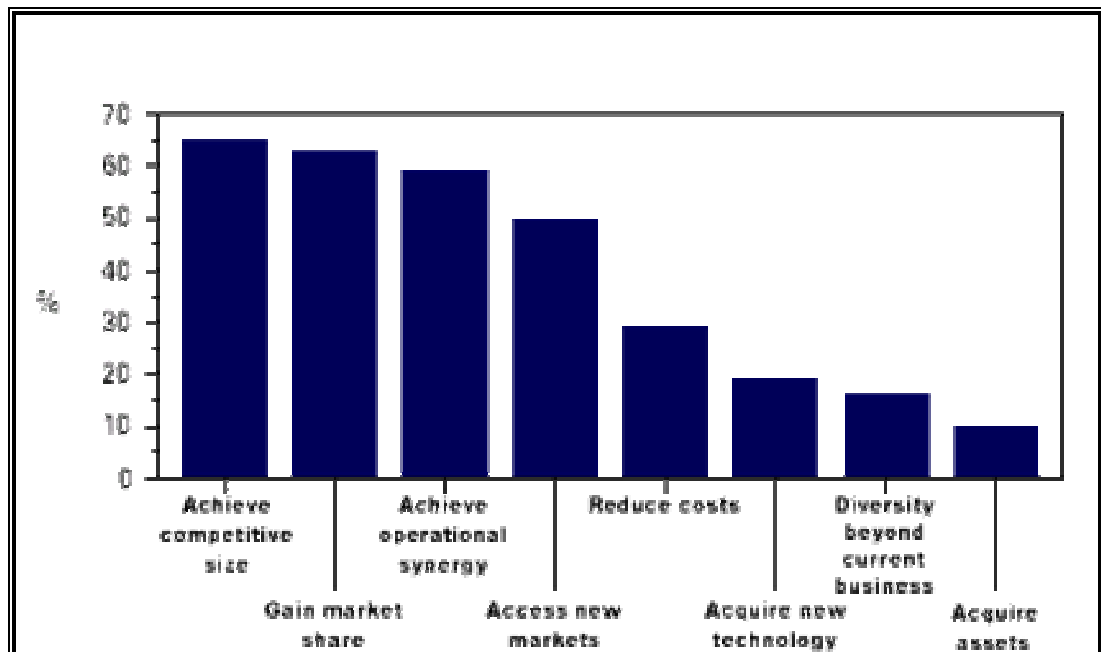
6. DRIVING FORCES BEHIND MERGERS AND ACQUISITIONS

The main reason for companies to realize M&A's is growth. As we have discussed earlier, M&A is a tool of external growth. The question to be asked here should be why companies prefer M&A's rather than other tools of growth. In this chapter, firstly the previous surveys that have been done about the M&A motives will be covered and then the motives in the literature will be examined.

6.1 Previous Surveys About M&A Motives

Below is the graph of motives which is taken from the global survey that was conducted by Watson Wyatt Worldwide in 2000. The survey was held among 120 European companies from various sectors of industry. According to the survey, European companies think that achieving a competitive size, gaining market share and achieving operational synergy are the first three main reasons.

Figure 1
M&A Motives



Watson Wyatt Worldwide, Global M&A Survey, <http://www.watsonwyatt.com/canada-english/research/resrender.asp?id=eu09&page=2>, (2000), p.2

In 1998-1999, AT Kearney has conducted a global survey about the importance of M&A motives. 115 transactions were examined and the results showed that cost cutting synergies were in the lead. 76% of the companies were expecting such benefits. Another interesting result that came out of this survey was that around 30% of the companies ignored growth opportunities that may be attained by sharing knowledge or offering a broader product line.³⁸

A very well known study was held by Berkovitch and Narayanan in 1993. 330 tender offers that were made during 1963-1988 period were utilized as the data base. The motives that were taken into consideration were synergy, hubris and managerial (agency) concerns. What made this research distinctive was its feature that target vs. total gains and target vs. acquirer gains were compared in order to distinguish the three motives from one another. The previous studies had examined only average gains which caused inconclusiveness because all three motives may have been present in most of the cases. According to the results of the study, synergy dominated the M&A transactions, agency motive not only caused negative gains, but also played as a value-reducing actor in the deals.³⁹

Based on Berkovitch and Narayanan's research, a similar survey was held by Seth, Song and Pettit in 2000. Same principles applied with the difference that the data base was limited to those companies which made cross-border M&A's, however the results were alike.⁴⁰

In Barney's and Walter's research, 32 individuals that are closely involved in M&A's were surveyed and asked to rank the most important five motives out of 20. This research that was conducted in 1990 was aiming to find out the relationship between the motives and the varieties of M&A's. The conclusion was that even though

³⁸ Max M. Habeck, Fritz Kröger, and Michael R. Tram, **After the Merger**, 1st Edition, Great Britain: Pearson Educated Limited, 2000, p. 55

³⁹ Elazar Berkovitch and M.P Narayanan, "Motives for Takeovers: An Empirical Investigation", **Journal of Finance and Quantitative Analysis**, vol:28 no:3 (September 1993), pp 360-361

⁴⁰ Anju Seth, Kean Song and Richardson Pettit, "Synergy, Managerialism or Hubris? An Empirical Examination of Motives for Foreign Acquisition of US Firms", **Journal of International Business Studies**, vol:31 no:3 (third quarter 2000), pp. 402-403

some motives are common, the importance of motives for each type of M&A was different than each other.⁴¹

A very recent study by Mukherjee, Kıymaz and Baker tried to shed a light on M&A motives, divestitures and target valuation practices. The sample was taken as the largest 100 transactions in each year between 1990 and 2001. The survey results which were conducted with the CFO's of the companies showed that synergy and diversification were the top two ranked motives. The research also concluded that operational synergy was more important for firms than other kinds of synergies.⁴²

In another survey by Hamill and Castledine based on 73 foreign acquisitions by British firms in the period 1985-1992, access to management and marketing skills was important in 61% of the cases and access to technology was important in 47% of the cases.⁴³

In another study which was held in 2001, Bower analyzed all US deals that are above 500 million USD in 1997-1999 period in order to find the relative importance of motives. Overcapacity deals and product-line extension deals were the most common. R&D and industry convergence related motives were at the bottom of the list which is no surprise according to Bower.⁴⁴

A very commonly cited study was held by Ingham, Kran and Lovestam. In their study, a survey was conducted among the CEO's of 146 of the UK's top 500 companies as of 1986-1987 and they were asked to rank the top 10 motives from a pool of 15 choices while ranking the most important as the first. According to the results of the survey, increased profitability was the most important motive. Pursuit of market power and marketing economies of scale were the following two motives. Creation of barriers

⁴¹ Gordon B Walter and Jay B. Barney, "Research Notes and Communications Management Objectives in Mergers and Acquisitions", **Strategic Management Journal**, vol:11, no:1, 1990, p:84

⁴² Tarun K Mukherjee, Halil Kıymaz and Kent Baker, "Merger Motives and Target Valuation: A Survey of Evidence from CFO's", **Journal of Applied Finance**, Vol: 14, No: 2 (fall/winter 2004), pp. 350-353

⁴³ Joseph Hamill and Pam Castledine, "Foreign Acquisitions in the UK: Impact and Policy", **International Business and Europe in Transaction**, vol:9, 1996, pp.240-242

⁴⁴ Joseph L Bower, "Not All M&A's are Alike- and That Matters", **Harvard Business Review**, vol:79 no:3 (March 2001), p.97

to entry, defense mechanism and response to market failure were the three motives at the bottom of the ranking.⁴⁵

Another research that was very similar to Ingham, Kran and Lovestam's was the one that was conducted in 1998 by Brouthers, van Hastenburg and van den Ven. The motives that were used in Ingham, Kran and Lovestam's study were reused with two additions, namely creating shareholder value and enhance managerial prestige. The managers of 47 Dutch firms that have been involved in 121 mergers in 1994 were asked to rank the motives. The motives were classified in three: economic, strategic and personal. Pursuit of market, increasing profitability and marketing economies of scale were the top three motives in order which made the class of economic motives the most important relatively. Economic motives were followed by strategic and lastly by personal motives.⁴⁶

6.2 M&A Motives

M&A motives have always been one of the foci of research topics. Researchers sometimes listed these motives one by one and sometimes they tried to classify them in major motives and then tried to divide them into sub motives. As the following pages will explain, not all these sub motives are mutually exclusive. In fact most of them are interdependent which means that trying to achieve one goal helps achieving another one or many others.

In his article, Trautwein listed M&A motives as net gains through synergies (efficiency theory), net gains through private information (valuation theory), wealth transfers from customers (monopoly theory), wealth transfers from target's shareholders (raider theory), manager's personal benefits (empire-building theory), process outcome (process theory) and macroeconomic factors (disturbance theory).⁴⁷

⁴⁵ Hilary Ingham, Ingild Kran and Andre Lovestam, "Mergers and Profitability: A Managerial Success Story?" **Journal of Management Studies**, vol:29, no: 2, (March 1992), p.203

⁴⁶ Keith D. Brouthers, Paul V. van Hastenburg and J. Van den Ven, "If Most Mergers Fail Why are They so Popular?" **Long Range Planning**, vol: 31 no:3 pp.347-353

⁴⁷ Friedrich Trautwein, "Merger Motives and Merger Prescriptions", **Strategic Management Journal**, vol: 11, 1990, p.284

Mukherjee, Kıymaz and Baker used 7 motives in their survey. These were acquiring a company below its replacement value, benefiting from tax savings due to losses of the target firm, using excess free cash, diversification, realizing gains from break-up value of the acquired firm, achieving a specific organizational form as part of an ongoing reorganization program and synergy. In the survey, synergy is not broken into its subordinates, but rather a list of plain synergy types which are operational synergy, financial synergy, managerial synergy (differential efficiency) and increased market power are given.⁴⁸

Ranft and Lord cited market power, geographical expansion, efficiency gains, resource sharing, diversification and obtaining technology with know-how as M&A motives in their article where they tried exploring technology based acquisitions.⁴⁹

Increased efficiency, operational synergy, diversification, financial synergy, low q-ratio and managerial concerns were considered as motives in Gupta and Gerchak's article.⁵⁰

Ali-Yrkkö divided the motives into three layers as macro, industry and firm levels. He depicted economic booms, technology developments, globalization and regulation& laws as macro level drivers, industry specific shocks as industry level driver and economic, managerial and hubris motives as firm level drivers. Under economic motives, he mentioned cost reductions, market power, acquiring resources, market for corporate control and speculation.⁵¹

Chen and Findlay explained the motives as economies of scale, acquiring technology, market power, financial strength, cost reduction, economies of scope, diversification, growth and access to proprietary assets.⁵²

⁴⁸ Mukherjee, Kıymaz and Baker, pp.34-35

⁴⁹ Annette Ranft and Michael Lord, "Acquiring New Technologies and Capabilities: A Grounded Model of Acquisition Implementation", **Organization Science**, vol:13, no:4, (July-August 2002), p. 420

⁵⁰ Diwakar Gupta and Yigal Gerchak, "Quantifying Operational Synergies in a Merger /Acquisition", **Management Science**, vol:48, no:4 (April 2002), p. 517

⁵¹ Jyrki Ali-Yrkkö, "Mergers and Acquisitions- Reasons and Results", Discussion Paper, no:792, (1992), p.25

⁵² Chunlai Chen and Christopher Findlay, "A Review of Cross-Border Mergers and Acquisitions in Apec", **Asian Pacific Economic Literature**, vol:17, issue:2, (November 2003), pp.24-27

Chakrabarti and Souder analyzed the post-acquisition performance with regard to the motives behind the transactions. In their article, they listed the motives as acquiring new businesses, new markets, new technologies, broadening customer base, corporate technology utilization, increasing profit, raw material supply, financial leverage, obtaining new market strength and assuring asset growth.⁵³

Ingham, Kran and Lovestam chose to broaden the motives a little more than the other researchers. A list of 15 motives included: increasing profitability, pursuit of market power, marketing economies of scale, risk spreading, acquisition of management, increasing turnover, cost reduction, technical economies of scale, acquisition of a competitor, differential valuation of a target, availability of raw materials, managerial challenge, creation of barriers of entry, defense mechanism and response to market failure.⁵⁴

Brouthers, van Hastenburg and van den Ven added creating shareholder value and managerial prestige enhancement to Ingham, Kran and Lovestam's motives.⁵⁵

In his article, Gammelgaard structured a different approach about M&A motives which is also the main backbone of the questionnaire design of this research as well. Gammelgaard identified 6 dimensions as main motives and filled in these main motives with their subordinated motives. He claimed that market (subordinates: growth, access to new products or markets, market power), cost (subordinates: economies of scale and scope, access to low cost resources), diversification (subordinates: risk minimizing and alternative use of resources), financial synergy (subordinates: shareholder value, debt/equity ratio, tax and capital cost), synergy (subordinate: pooling of complimentary resources) and competence (subordinate: access to non-tradable, unique and inimitable resources driving sustained competitive positions in the market) are the main motives behind M&A transactions.⁵⁶

⁵³ Alok K. Chakrabarti and William E. Souder, "Acquisitions: Do They Really Work Out", **Interfaces**, vol:14, no:4, (July-August 1984), p.43

⁵⁴ Ingham, Kran and Lovestam, p.203

⁵⁵ Brouthers, van Hastenburg and van den Ven, pp:347-349

⁵⁶ Jens Gammelgaard, "Access to Competence: An Emerging Acquisition Motive", **European Business Forum**, vol: 17, (Spring 2004), pp.44-47

Having seen what the previous researches have used as M&A motives, now it's time to take a deeper look into the motivations one by one. The following motives will also form the basis of the questionnaire that I will be using for the survey.

Synergy: The word synergy is derived from the Greek word 'synergos' which is "working together".⁵⁷ Synergy can be defined as the whole having a greater value than the sum of its parts. Generally the term is mentioned with the very well known inequality formula $1+1 > 2$. In other words, market value of a merger is greater than the summation of the market values of separate firms.

$$PV (M) > PV (A) + PV (B) + \dots PV (i)$$

The synergy revealed after a merger can be explained by the following reasons:

- Reduction in operating costs and increase in profit margin due to an increase in operational efficiency
- Decrease in capital cost due to the improvement in the financial structure of the firm
- The elimination of managerial inadequacies belonging to one or more companies that have merged
- Increase in market penetration
- Advantages of integration if any integration is aimed

Synergy can be examined in three subtitles; operational, financial and managerial.

Operational synergy is obtained where the takeover results in a merger and the new company reaches or gets close to its optimum volume. There are two ways of attaining operational synergy; either by joining the departments that have been working

⁵⁷Michael A. Hitt, Jeffrey S. Harrison and R. Duane Ireland, **Mergers and Acquisitions: A Guide to Creating Value for Stakeholders**, 1st Edition, New York: Oxford University Press, 2001, p.57

separately such as marketing, research and development⁵⁸ or by integrating the organization capitals of the merging firms.⁵⁹ Organization capital represents a value, which is not shown in the balance sheet of the firm, added by know-how and experience and to what degree it is transferred plays a major role in the synergy created after a merger transaction. Know-how and experience factors are outcomes of organizational learning. Organizational learning can be examined as managerial learning, industry-specific managerial experience and non-managerial learning. Managerial learning is the acquiring of planning, organizing, managing, controlling skills. This has nothing to do with the sector in which the company is operating. Industry-specific managerial experience is comprised of the experience and know-how related to a specific area. Non-managerial experience is the know-how of the worker staff and is directly related to the specific jobs that they are assigned to. These three factors determine the largeness of the organizational capital. Managerial learning can be transferred with the managers; the industry-specific managerial experience can only be transferred to those firms who operate within the same working area whereas non-managerial learning usually cannot be transferred at all.⁶⁰

Financial synergy is the increase in the share value of a firm due to the improvement in financial structure related to the merger. Financial improvement can be attained in various ways. The different aspects can be explained as follows.

When idle funds of a firm are not used efficiently or distributed as dividends to shareholders, the efficiency of the firm goes down which lead to a decrease in share value. On one side shareholders demand dividends whereas on the other hand, management would approach this in doubt since it would lessen their funds and their power to manage business. As an alternative to dividends, management stands closer to an investment option that brings up mergers and acquisitions. A firm with excess idle funds, but not with a growth potential may seem as a target to the former kind of entities.

⁵⁸ Trautwein, p.284

⁵⁹ Sarıkamış, p. 12

⁶⁰ Sarıkamış, p.12

If a firm is characteristically having a seasonal fluctuation in cash flows, merging with another firm of which the cash flow is negatively correlated with the former one might balance the cash flows. Merger of a firm with low liquid assets and another firm with high liquidity would reduce risk for the former one. Therefore a firm with high idle funds, but low growth potential makes a good target firm. In addition to these, a firm that has grown bigger may likely borrow funds from investment institutions easier than a small firm and with lower rates which results in a lowered capital cost. However it is a fact that a solid company will face some disadvantages in terms of the mentioned subjects, and of course a financially weak company that is in net loss will have some advantages since the merger is made with a solid company. Higgins&Schall suggest that such a merger will create no value, nevertheless they admit that the tax savings caused by high interest expenditures and the net loss the weak company is incurring can overcome this.⁶¹

Another financial synergy that is utilized by means of takeovers is that a profiting acquiring firm can save money on taxes if the target firm has a balance sheet showing a loss. When mergers and acquisitions are conducted in compliance with the provisions and laws of the country, they may also bring along some tax allowances to the acquiring or the resulting firm. Less tax would lead to more net profits which in consequence would result in an increase of the share value of the firm. And in some countries like US, acquisitions that are made by stock transactions instead of cash payments can be advantageous. In US, if at least 50% of the target's shares are exchanged for stock, the transaction is non-taxable for the target firm shareholders.⁶² However, although tax issue can be considered as a motive for takeovers, it is hardly on top of the list.

Managerial synergies are realized when the bidder's managers use their superior management skills for the benefit of the poorly managed target.⁶³ In literature, superior management's contribution to the target firm, hence to the whole organization is

⁶¹ Robert C. Higgins and Lawrence C Schall, "Corporate Bankruptcy and Conglomerate Merger", **Journal of Finance**, issue: 30, (March 1975), pp.93-113

⁶² Hitt, Harrison and Ireland, p.194

⁶³ Trautwein, p.284

described by differential efficiency which refers to the marginal benefit that a positive difference in management creates value which is a result of synergy.

Synergy motive is closely related to the neo-classical view which defines the goal of management is to maximize the value of the firm, hence to increase the shareholder value.

Tax: By means of takeovers, a profiting acquiring firm can save money on taxes if the target firm has a balance sheet showing a loss. When mergers and acquisitions are conducted in compliance with the provisions and laws of the country, they may also bring along some tax allowances to the acquiring or the resulting firm. Less tax would lead to more net profits which in consequence would result in an increase of the share value of the firm. And in some countries like US, acquisitions that are made by stock transactions instead of cash payments can be advantageous. In US, if at least 50% of the target's shares are exchanged for stock, the transaction is non-taxable for the target firm shareholders.⁶⁴ However, although tax issue can be considered as a motive for takeovers, it is hardly on top of the list.

Undervalued assets: Before explaining this motive, we should first define the q-ratio (aka Tobin's q-ratio). The q-ratio is calculated as the market value of a firm's assets divided by the replacement value of the firm's assets.⁶⁵ If the q-ratio is lower than 1, then it means that the replacement value is higher than the value of its stock. This feature of a firm makes it a target for other enterprises. Instead of making a new investment in a production unit, a firm would prefer to buy the stocks of a low q-ratio company which would cost cheaper. High inflation and interest rates during the 70's kept the stock prices low, and many mergers and acquisitions had been realized because of this motive.⁶⁶ However, as inflation and interest rates became lower, the popularity of this motive has been diminished in certain regions.

⁶⁴ Hitt, Harrison and Ireland, p.194

⁶⁵ The Free Dictionary, "Q Ratio or Tobin's Q Ratio", <http://financial-dictionary.thefreedictionary.com/Q+ratio+or+Tobin's+Q+ratio>, (19.10.2005), p.1

⁶⁶ Ayşe Gül Yılıgör, Şirket Birleşme, Ele Geçirme ve Satın Alma İşlemlerinin Finansal Çerçevesi, in: Sümer and Pernsteiner (Eds.) p. 386

Market share: Increasing the market share of a firm not only increases its profits, but also carries a strategic role for keeping the profitability in an incremental fashion. A high market share brings along the ability to influence pricing policies within the market, collect more information belonging to customers, be one step beyond its rivals by means of brand awareness and regulate its costs more efficiently. It is obvious that a firm should acquire a high market share in order to survive in a competitive market. Firms can achieve this goal in a shorter period of time and less costly by means of mergers and acquisitions and therefore gain the abilities mentioned above.

Entering new markets: It is not always easy to enter new markets either national or international. In today's competitive world, barriers to entry are built up so rapidly that if you don't take your place in the right time, you'll be out of the market without even getting out of it. Major players may be dominant so that you cannot price your goods as you wish to or not achieve brand awareness or it might take too much time to get into the game properly. Sometimes making an investment for a start up company, doing deals with suppliers and distribution channels, make customers know your brand and many other subjects might be too costly and time consuming. Therefore a company may choose to merge with or acquire a company that already exists in the market. This is especially true for cross-border situations where legislations also may be disadvantageous to foreigners. But mergers have advantages of saving money by not building a new facility, not dealing with the regulations for foreigners. In addition to these, obtaining a present market share, working with people who are experienced in sector and familiar with customers' needs and culture, using the target's sales organization, utilizing the target's good wills are reasons for entering a new market. One other important factor is that when customers go international, companies should follow the same route in order to serve better and for customer retention.⁶⁷ When all these factors are calculated thoroughly, it may be sensible to make a merger or acquisition deal.

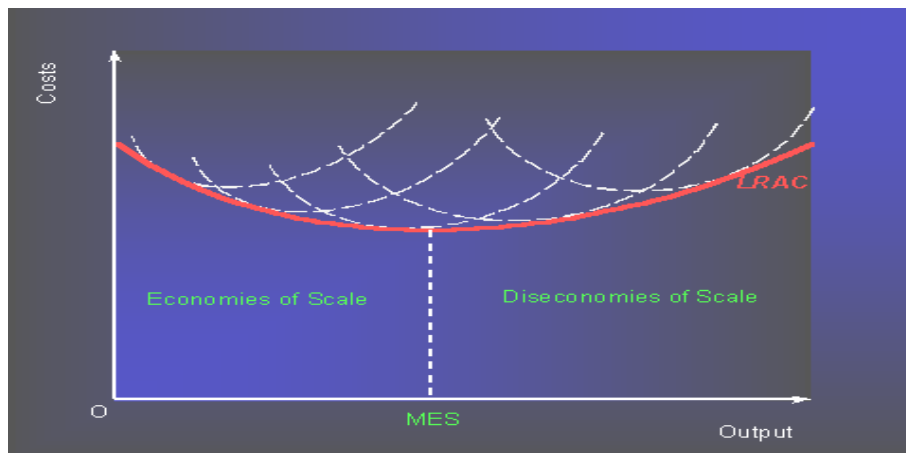
More efficient usage of idle funds: When idle funds of a firm are not used efficiently or distributed as dividends to shareholders, the efficiency of the firm goes

⁶⁷ Gammelgaard, "Competence: A Dynamic Extension of the Existing Typology of Acquisition Motives", pp. 5-6

down which lead to a decrease in share value. On one side shareholders demand dividends whereas on the other hand, management would approach this in doubt since it would lessen their funds and their power to manage business. As an alternative to dividends, management stands closer to an investment option that brings up mergers and acquisitions. A firm with excess idle funds, but not with a growth potential may seem as a target to the former kind of entities.

Economies of scale: As the number of goods being produced increases, the average cost per unit decreases since the fixed costs remain the same. Since mergers and acquisitions are tools for growth, the number of goods being produced increases in consequence. The unit cost decreases not only because fixed costs are now divided into more number of goods but also firm's negotiation and bargaining power for raw material increases since it starts making larger volumes of purchases. In the oil industry, Exxon and Mobil; Chevron and Texaco; Total, Fina and Elf have been good examples of mergers using economies of scale. However when a firm becomes too large and the unit cost begins to increase due to inefficiency, problems in control, coordination and cooperation, then the firm faces diseconomies of scale. The point where economies of scale is over and diseconomies of scale has started, the cost of production is minimized and is called the minimum efficient scale (MES). A long-run average cost (LRAC) diagram showing the case is as follows:

Figure 2
Long-Run Average Cost



Economies of Scale, <http://www.revisionguru.co.uk/economics/scale.htm> , (20.10.2005) p.3

Economies of scope: most firms produce more than one product. The major problems that need to be addressed are what to produce, how to produce them and in what quantities to produce. What makes these questions more complicated than they sound is the interrelationship between goods. If it is less expensive to produce a good together than separately, then economists interpret this situation as the presence of economies of scope.⁶⁸ Especially, vertical and conglomerate M&A's brings the economies of scope advantage on the surface where the acquiring firm gets the chance of producing a different or complimentary product which makes it cheaper and more effective than buying.⁶⁹

Diversification: Management of a firm can decrease the financial and operational risks and increase the profitability via diversification. A firm cannot influence the perceived sector risk, on the contrary the risk influences the market value of the firm. Likewise, fewness of the goods it produces, lack of distribution channels or suppliers all affect the profitability and the market value of the firm negatively. One solution for a firm for overcoming these problems is to merge with or acquire another firm. Another reason for mergers and acquisitions for diversification is to handle the seasonal or conjectural fluctuations. In terms of sales and profits, negatively correlated two firms can come together to solve the fluctuation problem, which lead to an improvement in financial structure. It should be noted that in publicly held companies, shareholders usually prefer the option of buying other sectors' stocks instead of a merger. Management usually chooses to merge because of personal concerns which are in contrast with the concept that management should act accordingly with the shareholders' best interests.

Researches about the correlation between the wealth of share holders and mergers for diversification would also reveal how useful conglomerate mergers are. One such research has been made by Frederick Scherer and David Ravenscraft, comparing such mergers' results with the whole market.⁷⁰ The data that was taken belonged to 60's since conglomerate mergers have been conducted intensely in that

⁶⁸ Stiglitz, p.333

⁶⁹ Chen and Findlay, p. 24

⁷⁰ Patrick A Gaughan, **Mergers, Acquisitions, and Corporate Restructurings**, 3rd Edition, New York: John Wiley and Sons Inc. , 2002, p.121

decade. They assumed an investment of 1000 USD in 13 shares that have made conglomerate mergers and watched their prices between years 1965-1968 and 1968-1983, then compared the results with the S&P 500 index. It turned out that until 1968 the virtual investment increase was 3,6 times the increase in the index. Then between 1968-1983 the increase was 2,7 times the index increase. The year 1968 was known to be the summit of mergers, then after 1968 mergers have entered a downswing. These results were found with the assumption of the investor always chose the right time to make his investments which is almost impossible in real life for sure. So this research showed that the market values of the mergers increased well above the average market prices, however they slowed down as merger transactions stopped. Same research compared the 13 shares' values with the S&P 425 Industries index from 1965 until 1983 and 6 of the shares stayed below the index, 3 almost the same and the rest 4 above the index. The table of prices is as follows:

Table 1
Values of 13 Companies in 1983 after \$1000 Investment has been Made in
1965 and the S&P 425 Industries Index

rank	company name	value in 1983 (in USD)
1	Teledyne	65463
2	Whittaker	24025
3	Gulf& Western	16287
4	US Industries	7152
5	Taxtron	4947
6	Walter Kidde	4813
7	ChromalloyAmerican	4672
0	S&P 425 Industries	41106
8	Beatrice	3992
9	Consolidated Foods	3820
10	ITT	3625
11	LittonIndustries	2691
12	W.R Grace	2587
13	Genesco	408

Gaughan, table 4.3 p.121

This research supported the theory that a shareholder who invests in a company rather diversifies its share portfolio than counting on a conglomerate merger that the company will make.

Technology: As today's world is developing very fast, companies should keep up with the pace in order to survive in such a competitive medium. Companies continuously improve their products and adapt them according to customers' choices and preferences and to do this they keep their technologies updated. Companies which do not have such technologies can merge with or acquire small companies to obtain technological abilities or can do so with companies with unique technologies to develop a competitive edge.

Management's personal concerns: Although the main reason lying under the idea of mergers and acquisitions is a raise in the wealth of shareholders, sometimes irrational motivations play a crucial role in transaction. One of the most common such motivations is the management's personal concern. The possibility of a management following its own interest is seen often.⁷¹ What we mean by personal interest can be variable. In some cases it's just a matter of money. Usually top management receives a premium when a merger or acquisition deal is done. Especially managers who are near the age of retirement may be inclined to do such deals. Or managers who are obsessed with their egos may want to manage a larger company since it will provide them prestige and a reputation within the market and maybe help him/her make a career movement. In literature this is known as agency cost. Researches about this topic have shown that every merger transaction has lead to an increase in top management's earnings even when the shareholders suffered from losses. Two of these researches are M. Firth's research in England's 254 mergers taken place during 1974-1980 and Conyon and Clegg's research about 170 British mergers during 1985-1990. Nonetheless, readers should not conclude that management always put their own interest in front of the shareholders'. It should also be noted that this is extremely hard to do in companies where public openness is low and the owners have the higher

⁷¹ P. Sudi Sudarsanam, **The Essence of Mergers and Acquisitions**, 1st Edition, London: Prentice Hall PTR, 1995, pp.13-18

percentage of the shares since an approval from the owners would be necessary and that is the common case in Turkey.

Hubris: Roll proposed a new concept where managers commit errors of over-optimism in evaluating M&A opportunities either due to their over prediction or due to their over self-confidence. As a result, bidders end up paying more than they should have been despite the facts presented by objective analyses. Therefore most of the gains of the transaction are transferred to the target's shareholders and the synergy – if there's any- disappears.⁷² The name hubris is adjusted from an ancient Greek word which meant arrogance, pride or over self-confidence which is very convenient for the situation since managers make this kind of mistakes while indulging themselves in these emotions.

Financial improvement: The capacity to borrow funds of a large firm is always easier than smaller companies. Larger companies not only find funds easier but also at lower rates. Therefore larger companies can lower their capital costs and use financial leverage more efficiently than smaller companies. Cash flow fluctuations would be minimized if companies of which cash flows are negatively correlated which would also spread the risk and also support low-rate debts. In addition to these, a good looking merger always attracts investors' attention and the share values of firms go up in the markets which add value to the firm's equity. It should be mentioned that these are all very closely related with the financial synergy created by the merger transaction.

Globalization: Globalization is likely to be the most important key motives of mergers and acquisitions activities in macro scale. The idea of globalization refers to investing, producing, servicing, distributing and selling in all over the world. An enterprise can produce in China, distribute goods via a Korean logistics company, sell its goods in Europe and be managed in the USA. Such an example shows us how the

⁷² Fotios Pasiouras, Sailesh Tana and Constantin Zopounidis, "Application of Quantitative Techniques For The Prediction Of Bank Acquisition Targets", **Computers and Operations Research**, vol:5 (October 2005), pp.19-20

competitive landscape has changed and this is what globalization is all about. In 1987, Peter Drucker wrote in Wall Street Journal that:⁷³

To maintain a leadership position in any one developed country, a business- whether large or small- increasingly has to attain and hold leadership positions in all developed markets worldwide. It has to be able to do research, to design, to develop, to engineer and to manufacture in any part of the developed world, and to export from any developed country to any other. It has to go transnational.

Although today a leadership position requires going beyond developed countries and include emerging markets and less developed countries, what Peter Drucker has said stays as a correct foresight. If firms want to achieve leadership without consuming too much time and without taking some risks like entering the market from zero or making a whole new investment in a new production unit, then mergers and acquisitions might just be what they are looking for. Therefore making especially international deals seems inevitable for firms that are after a leading position in markets, because if they don't, others will.

⁷³ Peter Drucker, "Managing for the Future", **Wall Street Journal**, (March, 1987)

7. MERGERS AND ACQUISITIONS HISTORY

Going over the history of takeovers would help us understand the relationship between takeovers and both economical and technological developments. Takeovers started and became distinctive in the USA around 1890 and have been continuing since then. We'll first take a look at the USA and then Europe and Turkey in order. Global numbers and Turkish M&A numbers are given in more detail in the appendix section of this study.

7.1 Takeovers in the USA

The first attempt was an unsuccessful hostile takeover attempt made by Erie Railways.⁷⁴

7.1.1 1st wave (1897-1904)

The first takeover wave started in 1897, right after the economic stagnation that started in 1883. The wave has reached its peak in 1899 and continued until 1904. Especially mining and manufacturing sectors were the heart of takeovers. Companies involved in mines, food, transportation equipment, petroleum and chemical goods were the key actors in these transactions. The leading purpose of these takeovers was to dominate the market. The merger of JP Morgan's US Steel, Andrew Carnegie's Carnegie Steel and 785 other smaller scaled businesses created the giant US Steel. The triggering factors of the first merger wave were the economic upswing and the developments in the manufacturing technology. It can also be said that a third factor was the absence of regulations that take measures against monopolies.

Extension of railroads all over the USA, usage of electrical power and coals and increase in production changed the economical activities from local to national size. And what made this change possible were mainly takeovers.

In these era, 78,3% of the mergers were horizontal, 12% vertical and 9,7% conglomerate. The first wave greatly increased the market concentration because of

⁷⁴ Gaughan, p.22

horizontal mergers. 15% of all the employees and plants in manufacturing industry were involved where over 3000 firms disappeared.⁷⁵ The first wave ended by the economic stagnation in 1904 and stayed calm until 1916 with the effect of WW1.

7.1.2 2nd wave (1916-1929)

After WW1, the economic recovery continued until the depression in 1929 and this time span has formed the 2nd wave. The economic recovery, land transportation facilities, advertisement on radio all contributed to the acceleration of takeovers. Land transportation replaced the railroad factor of the 1st wave. Radio advertisements and more efficient transportation changed local markets to national markets. Selling goods in bulk volumes to all over the country with low profit margins brought high profits. Reaching economies of scale was attained by takeovers as well as internal growth strategies.

The majority of takeovers took place in food, chemical, petroleum, transportation equipment and mining industries. Most of the mergers were horizontal with an intention diversification, higher market share and more production capacity. The 2nd wave resulted in the disappearance of 12,000 firms, however this did not cause market concentration as in the 1st merger wave. Another feature of the first two waves was that investment banks gave consultation and loans for the transactions.

Nobel prized economist George Stigler claims that the 1st wave mergers yielded monopolies whereas 2nd wave oligopolies.⁷⁶ The lack of regulations caused monopolies in the market, so US governments took action against it. Regulations stopped monopoly resulting takeovers during the 2nd wave, however were not enough to halt oligopolies. Still according to Markham, takeovers intending to form oligopolies in the 2nd wave were just a very small percentage.⁷⁷

⁷⁵ OECD, **Report of the Committee of Experts on Restrictive Business Practices**, Paris 1974, p.7

⁷⁶ Gaughan, p. 23

⁷⁷ J. Fred Weston, **Takeovers, restructuring, and corporate governance**, 3rd Edition, New Jersey: Prentice Hall, 2001, p.108

7.1.3 1940-1947 period

Researchers focusing on takeovers that have taken place in the USA agree that there has not been a significant movement in transactions in this period. Although the economy was getting better after the war, high taxes over income and real estates, owners had to sell their business out. As a consequence, bigger companies bought out the smaller ones. Besides taxes another important reason why takeovers have not realized was because there were not enough technological developments and infrastructural investments. The motivation behind the bigger companies buying smaller ones was either to go vertical integration or diversification.⁷⁸

7.1.4 3rd wave (1963-1969)

Since the regulations were inadequate, monopolies and oligopolies formed during the first two waves. In the beginning of the 60's, authorities carefully set new regulations which prevented such formations. As a result of the antitrust laws, companies began to make conglomerate merger deals. Based on the data by the Federal Trade Commission, 80% of the mergers that have taken place between 1965-1975 were conglomerate.⁷⁹

The feature of this wave was that unlike the former waves, bigger scaled companies had become the targets this time. After Richard Nixon was elected as the President, the antitrust laws that were set in 60's had amendments that made them more liberal. The Supreme Court decided that monopolies did not carry that much of a significance any more since markets were going international.

Highest number of takeovers was seen in this period. In 1963, 1361 transactions took place and in 1969 the number went as high as 6107. After 1970, the number started to decrease due to the economic stagnation. During this period, 25000 companies were disappeared as a result of 6000 takeovers. However this did not result in a concentration in the market since most of the takeovers were conglomerate type. Another feature of this period was that investment banks did not undertake the agency

⁷⁸ Sarıkamış, p.85

⁷⁹ Sarıkamış, p.85

role in transactions and did not give loans to the acquirer firms.⁸⁰ High economic growth caused increases in both the share values and loan rates. Therefore companies issued new stocks instead of taking loans for financing takeovers. Stagnation period around 1968 and recession in 1974-1975, share values decreased again and issuing stocks became no option for financing. Although the number of takeovers got in a decreasing trend until 1980's, the volume started to move upwards in 1975, or in 1977 if we consider the inflation deflator. Seeing the number going down and volume going up, we can say that larger volume transactions occurred in the second half of the 70's.⁸¹ An interesting concept called "corporate raiders" has originated in this decade. Some investors – raiders- started to collect the stocks of a firm that has become a target and of which shares were being collected by acquirers. Later on, raiders sold their issues to acquirers with a high premium or made an agreement with the acquirers that they would not involve in the decision making process and get a premium in return (green mail).⁸² The cycle that has started in 1963 got completed by the year 1980 when the number of takeovers reached the same number as in 1963.

7.1.5 4th wave (1981-1989)

Despite fluctuations from 1981, the number of takeovers had generally an increasing trend. After a drastic fall in 1986-1987, the rise started again until 1989. Although the number of takeovers stayed almost the same, the volumes went high meaning higher volume deals were made. The distinctive features of the 4th wave were 1) corporate raiders started to become more effective over the markets. 2) many takeovers had hostile characteristics. 3) investment banks and law firms were heavily involved in deals or providing services against hostile takeovers. 4) conflicts between state and federal authorities have aroused. State authorities set out strict antitrust laws where federal authorities such as Security Exchange Commission argued that these laws were inhibiting interstate trade. 5) because of globalization and undervalued USD, many cross-border takeovers have taken place. Especially some Japanese and European companies took over US companies. 6) new strategies such as leveraged buy-out,

⁸⁰ Sarıkamış, p.87

⁸¹ Sarıkamış, p.88

⁸² Sarıkamış, p.89

management buy-out and junk bonds have emerged in this decade.⁸³ Junk bonds had a role in bankruptcies of savings and loans associations, insurance firms and investment fund firms.⁸⁴

7.1.6 after 1990's

Convergence in takeovers, which started towards the end of 80's, livened up in 1992 as the recession gradually lost its effects. Increase in number of takeovers continued until 2000, except 1998. After 2000, stagnation in the US economy caused takeovers negatively. The failures of leveraged buy-outs and bankruptcies of many investment banks in 80's led companies to finance deals with their equity capital.⁸⁵ Takeovers in the mid 90's were intensely among commercial and investment banking, wholesales and retail and health industries. Today, takeovers have become mega deals as they go international in large amounts.

7.2 Takeovers in Europe

Takeovers in Europe became important in the second half of the 20th century. The major reasons behind takeovers were adaptation to the changing economic conjecture, strengthen competitiveness and decreasing costs of production. Besides these motives, entrance of non-European countries as competitors and the regulations that made takeovers relatively easy could also be mentioned.

It is known that there were some takeover events in the UK as early as the beginning of the 20th century, but this trend was not as big as it was in the USA. Nevertheless "merger for monopoly" motive -with the predominate type of merger being between 5 or more independent firms- was not any different than the USA. What differed from the USA was this motive persisted too much longer since no antitrust legislations were made. With the fact that not enough statistics were collected from the end of WWII until 1954, the first drastic increase in merger activity came to real in 1959 and reached a peak in 1965, when there were 1000 recorded transactions and £517

⁸³ Sarıkamış, p.92-93

⁸⁴ Weston, p. 337

⁸⁵ Sarıkamış, p.93

million of assets acquired. In this period, horizontal merger was dominant being 67% as of number of transactions and 71% as of value of assets. After the 1965 Act, which gave power to control certain mergers, this trend has turned into diversified mergers both in numbers and value of assets acquired. The share of manufacturing net output held by the largest 100 firms had risen from 26% in 1953 to 50% in 1970 which showed that market concentration happened in this period.⁸⁶ Studies showed that mergers have been responsible for about 40% of the increase in market concentration.⁸⁷ In 1987, economic crisis has forced companies to mergers as share values have fallen down drastically due to crisis.⁸⁸ Besides mergers, divestitures have also taken place in 1987 with MBO's and LBO's as reorganization issues.

When mergers meet certain criteria in Germany, they have to be notified to the Federal Cartel Office, so statistics are known for sure. It is seen that a rising trend exists since 1958 with exceptional growth rates in 1969 and 1970.⁸⁹ In this period, conglomerate mergers have dominated the market just like it did in the USA and the UK.

Economy was the major motive behind mergers in France just like other countries, but more interestingly government's tendency to merge the small and medium sized firms into larger scale firms in industry.

7.3 Takeovers in Turkey

As in Europe, takeovers have started in the second half of the 20th century. This can't be directly related to the economic conjecture since capital markets were not developed as it should have been and corporation number was not as many as other developed countries. The very few takeovers in 50's were the takeovers of banks that were at the edge of bankruptcy. Mergers of Türkiye Eski Muharipler Bank and Tumsu

⁸⁶ OECD, p.8

⁸⁷ OECD, p.9

⁸⁸ Sudarsanam, p.2

⁸⁹ OECD, p.9

Bank becoming Türkiye Birleşik Tasarruf ve Kredi Bank in 1959 and Türkiye Turizm Bank and TC Turizm Bank in 1960 were the noteworthy activities at the time.⁹⁰

Liberalization in the Turkish economy in the 80's caused takeovers speed up. Economy policies that are followed in order to liberalize the economy and diminish the inflation at first caused liveliness in financial sector and led to the establishments of many banks. However, as the demand fell down, companies started to work under capacity and investments nearly stopped. As a consequence, many companies as well as banks had very hard years. This conjecture made it impossible for many companies to survive on their own and forced them to merge.

The motives behind the high number of takeovers in 80's were helping banks, creating an economy by uniting companies that are in the same group, dissolution of companies for them to focus on their core competitive jobs, trying to increase efficiency by means of foreign partners, dissolution of companies in losses in order to get rid of the burden and also takeover of such firms to exploit tax advantages. Koç Holding, Sabancı Holding, İş Bankası, Eczacıbaşı Holding, Zorlu Group and Anadolu Group set examples for this kind of takeovers.⁹¹

Though not many, there had been few takeovers in 80's where the companies with deteriorated operations became targets for solid companies. The acquisitions of Olmuk Mukavva Sanayi ve Ticaret AŞ by Sabancı Holding, Bank Ekspres by Garanti Bankası and Hurriyet by Doğan Holding were the examples that come to mind at first.⁹²

One example of merger of two companies that are in the same holding because of tax concerns happened in Profilo Holding.

According to Cumhur Kuscuoğlu, corporate finance senior manager in Ernst&Young says that the bubble of new economy concept which was the basis for the deals that belong to before 2001 has caused a lot of suffering for the Turkish economy as well as the rest of the world. Kuscuoğlu underlines the fact that companies' were evaluated

⁹⁰ Sarıkamış, p.96

⁹¹ Sarıkamış, p.96

⁹² Sarıkamış, p.97

by the possible revenues that they would make in the future instead of real business models that they should have put forward or the values that they should have created. He was proven right when only a few of the 75+ internet service providers survived through the years.⁹³

Global competitions, high working capital costs, lack of equity and economic crises have given rise to many acquisitions and mergers in the financial services sector in Turkey. The necessity to be more competitive caused Osmanlı Bankası and Garanti Bankası to merge and many public banks to gather under one name.

Also, many banks were confiscated by TMSF as they were bankrupt after the crises in 1994, 1999 and 2001. Later on, these banks were acquired by foreign and domestic banks. Demirbank was sold to HSBC in 1994 which was a controversial issue for authorities. The fear of what had happened in the past forced banks to seek for strong partners or acquirers.

After 2001 crisis, Turkey became one of the most popular emerging markets with its high potential and en route economy. Within the last couple of years, we have seen high volume transactions in financial sector. GE Capital's partial acquisition of Garanti Bankası, Kocbank's acquisition of Yapı Kredi Bankası, BNP's acquisition of TEB, Fortis' acquisition of Dısbank and National Bank of Greece's acquisition of Finansbank have proved the foreign interest in Turkish banking sector. In addition to these acquisitions, nobody believes it is over yet. The expectations are in the way that there are at least 3-4 banks in line for a deal. It is no surprise that the survey results of Earnst and Young pointed at banking as the most promising sector in M&A's in 2006. According to the survey, the highest movements are expected in the following sectors in order: banking, energy, real estate, services, tourism, logistics and retail.⁹⁴

We have seen liveliness in food and drink industry and financial services industry in terms of transaction number in 2002 and 2003. In 2004, mining, tourism and

⁹³ Cumhuriyet Kuşçuoğlu, "Birleşmeler Nasıl Gidiyor?", 19.02.2004, <http://www.insankaynaklari.com/CN/ContentBody.asp?BodyID=2404>, (16.05.2006)

⁹⁴ Earnst&Young, **Birleşme ve Satın Alma İşlemleri 2005 Raporu**, İstanbul, 2006, p.15

energy industries were drawing attention as well. In 2005, financial services were at the focus point again. However, high volume transactions of Telekom privatization and TMSF's sell off of Telsim were the two top deals in terms of volume. These two deals added up to a volume of 11 billion USD and both of them were acquired by foreigners, namely Saudi Oger and Vodafone. It would be unfair to skip the media sector. The reason for the acquisitions in media sector could sound skeptical, but the power of media over politics and economy should not be overlooked. Today, many holdings own either a television channel or a newspaper if not both. Dogus Group owns Garanti Bank, NTV and CNBC-e, Dogan Holding owns Kanal D, Star TV, Hurriyet and Milliyet, Cukurova Holding owns Aksam Media Group. The list can be extended when we consider the television channels that were confiscated after crises.

One distinctive feature of M&A deals in Turkey is that acquisitions have outnumbered merger deals. During 1997-2001 period there had been 11 merger deals against 80 acquisitions. According to Earnst& Young M&A Reports for 2003-2005, there have been only 8 mergers. In addition to that, we see that most of the acquisitions have taken place in a majority acquisition or full acquisition fashion. This structure and the relatively small number of mergers indicate that companies do not wish to operate with the target company, but rather have the control and power alone.⁹⁵

Aside from the last couple of years, Turkey's M&A history has never been very lively. Economical and political volatility, lack of technology, high inflation, crises and other factors always hindered the volumes and numbers as far as M&A's were concerned. Only after the 2001 crisis, privatizations, foreign capital, economical and political stability had positive effects which caused an upswing in M&A's. Volumes and transactions have reached all time highs. In 2005, foreign companies have become more active than domestic firms for the first time in Turkish history. More detailed information in tables and graphs regarding the last 3 years of Turkey can be found in the appendixes section.

⁹⁵ Sarıkamış, p.99

8. MERGER AND ACQUISITION PROCESS

Mergers and acquisitions are difficult, expensive and risky transactions. In order to minimize any potential losses, one should carefully plan this painstaking decision. Unless a path is not drawn beforehand, firms will most likely incur losses that can even lead to bankruptcies. A merger and acquisition process includes many stages such as screening potential targets, focusing on one target, due diligence, intend letter, announcement of the deal, signing the contract, fulfilling the conditions and actualization of the deal. Attaining the goals of the deal entails strategic planning approach where every stage should be scrutinized and reviewed. Mainly there are three stages of a merger and acquisition process.

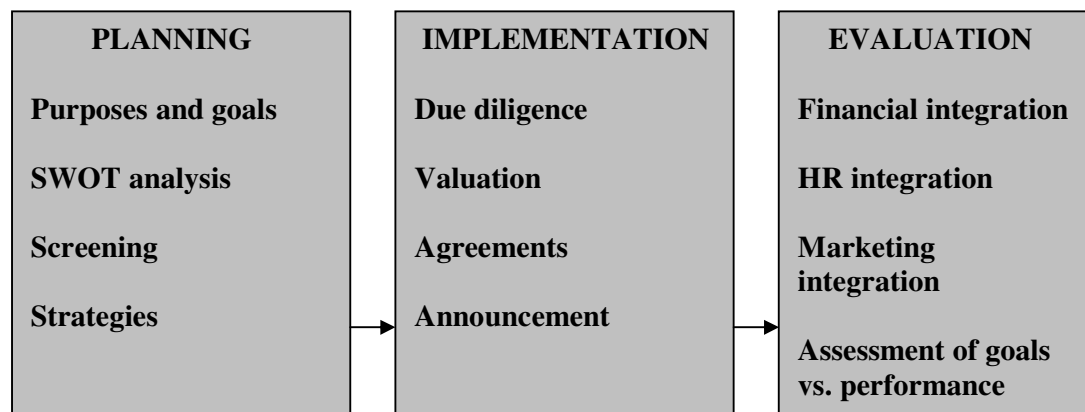
First stage is the planning stage. In this stage, the purposes of the merger and acquisition decision are determined. These are one or more motives that we have discussed in earlier chapters. The planning stage is in fact about screening the potential target companies. Firstly, a SWOT analysis of the company is conducted. Then according to the analysis, the motives for the deal are underlined. Then, potential targets are screened in the way that it is in compliance with the SWOT analysis. A target company should improve a bidder's weaknesses and reinforces its strengths while it has the ability to decrease the risks of threats and increase the ability to exploit the opportunities. Finally a strategy is chosen in which the answers of questions like how the financing is going to be made, whether a merger or an acquisition is going to be followed, how the goals are going to be attained are agreed on.

Second stage is the implementation part of the process. The implementation stage is mainly composed of due diligence and actualization of the deal if the outcomes of due diligence are positive. Due diligence is the process by which confidential legal and financial information are exchanged, reviewed and appraised by the parties of a merger or an acquisition deal. The essence of the due diligence process is to make everyone aware of the facts about the other company, so that a proper pricing can be made and parties do not encounter any bad surprises in the future. Attorneys and consultants usually serve in due diligences on behalf of the company. Financial valuation and negotiations take place in this stage. After the negotiations, should a

positive result is obtained and parties agree on everything then the deal is actualized after the announcement to the shareholders and a series of legal procedures. This part of the stage should be covered as quickly as possible because if it is prolonged, shareholders will be disturbed by the ambiguity, employees and management may become distracted and their morale gets low. All these affect the market as share prices go down. During the implementation stage, goals, assets, human resources and cultures should be brought together. Especially, human resources aspect of the post-merger integration may become problematic. Integration should start with the due diligence, not as a following part. How to overcome integration problems will be explained in the next chapters.

Third stage is the assessment and evaluation stage. In this stage, the goals and strategies planned in the first stage of the merger and acquisition process are compared with the outcomes and feedbacks are provided in order to improve the insufficient properties of the deal. These can be in terms of financial numbers, operating features or human resources aspects of the company. The importance of the planning stage shows itself in this last stage in the way that an accurate evaluation can be made only if objective and clear goals are set before hand, so that comparison between before and after situations can be attained properly. How measurements can be done in order to evaluate the post-M&A success is explained in the tenth chapter of this study.

Figure 3
M&A Process



9. FINANCING MERGERS AND ACQUISITIONS

Financial impacts of a merger and acquisition deal are not one of the first things that should be thought of at the beginning of the process. First of all, strategic decision-making should be covered. Later on, a potential target should be found, then due diligence is handled. After that, it's time to think about the financials.

There are no predetermined templates for financing a merger and acquisition deal. Current market conjecture and target firm's condition should be carefully examined. The elements that will determine how to finance the deal are:⁹⁶

- Price
- Costs of the financial instruments used
- Tax concerns
- Level of debt and used equity
- Profitability
- Available collaterals

There are two ways of financing a deal in terms of resources; using your own resources (auto finance) or taking credits. However more importantly, the medium of exchange is the basic question here. It can be cash, all stock or a combination of cash and stock. The effect of the choice of medium of exchange on share prices has been the subject of many studies. Among these three alternatives, cash is by far the preferred medium of exchange. The percentage of deals with cash grew steadily from 20% in the late 60's to 50% in 1978.⁹⁷ In the 90's, cash has been predominant over the other two alternatives. In a research conducted by Mara Faccio and Ronald W. Masulis, out of 3,864 merger and acquisition transactions in Europe between 1997-2000, 3,123 of them

⁹⁶ Martin Schadle and Helmut Persteiner, *Finansal Açidan İşletme Birleşmeleri*, translated by: Oğün Erdoğan, in: Sümer and Pernsteiner (Eds.) pp. 286-287

⁹⁷ Willard T Carlton and others, "An Empirical Analysis Of The Role Of The Medium Of Exchange In Mergers", *Journal of Finance*, vol: 38, 1983, pp. 813-826

were cash deals, 317 were all stock deals and 424 were a combination. The largest multibillion-dollar deals are mostly financed with stock, but it should be noted that such deals do not count for a very large percentage. In large deals (over 100 million dollars) cash is much popular, counting for 50% of the total.

9.1 Cash Transactions

Especially in countries including Turkey where enterprises see banks as finance resources and are usually family businesses, in small and medium sizes and the capital markets are shallow, stocks are not usually preferred over cash.⁹⁸ Transactions with cash payments end swiftly and there are no ambiguities on the target side about how much they are going to be paid. This eases the procedures of the deal. Having paid in cash, acquirer gets all the benefits that will be created by synergy, however they take all the risk as well. Acquirer becomes susceptible to the volatility of the share price. Although there is no certain proven fact, in many empirical studies, it has been shown that using cash as the medium of exchange receives better reaction in the stock market than the use of stocks. On the other hand, cash has its own disadvantages. First of all, using liquid assets for the merger and acquisition deal will have opportunity costs for sure. Having not enough resources of their own, companies may apply to creditors for loans which will have a negative effect on the financial structure of the acquirer.

A company may use the excessive cash it has for financing the deal. It can also acquire the necessary cash by giving up dividends. Such behavior would prevent the adverse effects of a high debt level and the burden of interests. A company can create the cash by selling off its assets or even by divestitures as well.

When internal resources are not enough to raise the money or the managers prefer not to use these resources, creditors enter the picture. Credits can be obtained from banks, investment banks, and social security funds etc. Assets of the acquirer or the target firm to be acquired or securities can be used as collaterals. Especially in the 80's high yield junk bonds were used widely as instruments, which caused many bankruptcies in the financial sector. Creditors give loans for projects that they think will

⁹⁸ Schadle and Persteiner, in: Sümer and Persteiner (Eds.), p. 287

create the cash flow for the back payment. Leveraged buyouts, management buyouts and employee buyouts are the subtopics of this issue. The biggest risk in loans appears when liquidity falls down and the enterprise starts having problems in payments.

Leveraged Buy-out (LBO) is a strategic method in corporate finance under which a target company is acquired by a group of investors who use borrowed money to finance the deal.

It is basically an acquisition, but it has three distinctive features that separate it from a traditional acquisition. First, the acquirer is not a company, but it is a group of investors. Secondly, the purpose of it is to sell it after a few years when the investors believe that they can make a good profit of it. Last but not the least is that investors use borrowed money to finance their acquisition, which is maybe the most distinctive feature of this method.

Investors borrow up to 80% of the purchase price and put very little capital from their own resources. This makes it possible to making an investment with small capital and investors exploit the benefits of leverage. The acquired company has to operate highly efficient, have a good market penetration, and work full capacity in order to exploit the leverage. If these are all met, the investors can make good profits by selling the business after three to five years.⁹⁹

An investment bank, a commercial bank or a leveraged buy-out specialist trust could be used as creditors in these actions. Leveraged buy-out specialists give consultancy to investors as well as they can provide funds. They don't interfere with the daily management of the target firm, but they leave to professionals.

After a bull market due to the economic upswing in the second half of the 1970's, share values of companies have increased and many shareholders of average companies preferred to go public in this optimistic atmosphere and sold their shares in the second hand market to make profits. After 1982, high inflation influenced the capital markets in a bad way and started to pull down the market values. As a result of that

⁹⁹ Weston, p.316

many firms had q-ratios less than 1 which made them attractive as targets.¹⁰⁰ With the existence of many potential target firms and low-rated interests in an inflationary conjecture, investor groups decided to borrow money in order to acquire companies.

In the USA, acquirers provided approximately 20% of the needed capital from their own resources and borrowing the 80% from creditors. This 80% was comprised of 50-60% from banks and the rest from social security funds, insurance companies and venture capital firms.¹⁰¹ The collateral for the borrowed money was the assets and mortgage of the acquired enterprise. The current assets were collaterals for short-term credits and fixed assets with mortgage were for long-term assets, so that maturity dates were met. However, the real tool for the back payment was the positive cash flow generated by the operations.

What the creditors are concerned in an LBO is of course the risk that it carries. The lack of cash flow and a rise in loan rates are the potential risks for back payment. Loan rates affect the systematic interest risk of a credit. If the loan has a maturity date, then an increase in rates is advantageous for the enterprise and vice versa. However if the credit has no maturity date, which is very rare, the risk is directly proportional with the interest rates.

Apart from the interest risk, firm's capability to generate cash, the economic conjecture of a country and the market, efficiencies of the firm's distribution channels and operations, cost efficiencies are also the determinants of the credit risk. In order to minimize these risks, investor groups and the creditors work together on feasibility plans in order to foresee the future. They help each other on acquisition deals, forecasts, sector analysis and other unknown parameters so that both the creditors don't waste their money and the acquirers don't get involved in a dead project.

LBO's started in 1980 with four deals and a total amount of \$1,7 billion and reached its peak in 1988 when there were 410 LBO's and a total amount of \$188 billion

¹⁰⁰ Weston, p.319

¹⁰¹ Weston, p.322

in aggregate. As of 2005, the largest leveraged buy-out to date was the \$25 billion acquisition of RJR Nabisco in 1989 by Kholberg, Kravis, and Roberts (KKR)¹⁰²

Management buy-out (MBO) is another strategic corporate finance method and can be seen as a subtopic of LBO. The key difference between an LBO and an MBO is that in MBO, the acquirers are the managers of the target firm. Another difference is that the managers' first goal is to takeover the firm and to direct it better than its current situation. This is compatible with the idea that managers' priority should be protecting shareholders' best interests since they become the shareholders. Principles about financing the acquisition are no different than LBO concept. Same creditors as in LBO take part in MBO.

The owners of the company may prefer to sell the company to the management for several reasons. Keeping in mind that a buy-out can be the acquisition of all or some part or a division or a subordinate of a firm; first of all, an MBO can be much faster than an auction. The owners might not want its competitors to acquire and get more powerful or have access to confidential information about the company. The owners of the company may continue doing business with the management staff since they have established a relationship before. And of course the offer could be the best they can get. When outside investors acquire a company and place their own managers as incumbents, it is called a **management buy-in (MBI)**. This usually happens when creditors not only give loans, but also starts depositing capital as equity. Gradually, they can take the control of the company and be entitled to place their own managers.

An employee stock ownership plan encourages employees to buy the stocks of the company as stocks are offered at a discounted price to the employees. If employees acquire the company by using this plan or involving directly in a LBO, then it is called an **employee buy-out (EBO)**.

Another way of creating cash is a capital increase. This happens by the purchase of more shares by existing shareholders or by the introduction of new shareholders. Many companies that are listed in the stock market usually issue new

¹⁰² "Leveraged Buy-Out-Company Acquisition Method", 18.09.2005 http://www.valuebasedmanagement.net/methods_leveraged_buy-out.html, 20.11.2005, p.1

stocks for the market actors. Also venture capital firms are taken as partners in order to create cash.

In incorporations, capital increase is utilized in a wide range of areas. In addition to that, it is tax deductible. On the other hand, in some countries there are regulations that restrict the existing shareholders to buy the newly issued stocks. Even if they can buy them, the dividends are subjected to taxing which makes it less attractive. Studies have shown that companies who have decided to create cash by capital increase have incurred falls in stock prices. The main reason for that is market actors usually think the newly issued stocks are overvalued. Some surveys also show that shareholders think the increased capital will not be used efficiently and resources will be wasted. This is more the case when conglomerate mergers are concerned. However, if the managers of the company have a clean history about using the excess cash, this will soften the reactions.

9.2 Stock Transactions

Not all companies can grow externally by mergers and acquisitions. Many good projects have not been realized because required resources are absent. This is usually the case for very small-scaled companies, which have high potentials to grow. On the other hand, big-scaled companies sometimes cannot implement their growth plans since they require vast financing in spite of the resources and credit lines they own.

In such cases, the intended transactions are done by stock swaps. Instead of paying in cash, the acquirer offers its stocks as a payment instrument. The most known example of using stocks in a merger is the deal between German Daimler-Benz and American Chrysler firms. High value of stocks in the market brings advantages to firms and it is almost a must in big deals. Erickson and Wang have shown in their studies that acquirers have designated their collections more than actual in order to attain a stock price increase before several months before a merger deal.¹⁰³ If the stock is a very well

¹⁰³ Merle Erickson and Shiing-Wu Wang, "Earnings Management By Acquiring Firms in Stock For Stock Mergers", **Journal of Accounting and Economics**, issue:27, 1999, p.149

and reputable brand, then it will hardly by the side effects – fall in stock prices- of the deal made by stock- swapping.

In mergers and acquisitions financed by stocks, liquidity is maintained and interest payments are avoided. Credibility of the acquired firm may increase the debt structure of the acquirer. Also, the synergy that will be created and tax issues are all advantages of the acquiring firm. On the contrary, shareholders of the target firm cannot assess the value of the share that has been offered by the acquiring firm. This is called an information asymmetry, which means that target firm shareholders cannot predict how much they are going to get from the deal while the bidder doesn't know the exact price of the target firm. In cash payments, shareholders of the target firm are not interested in the stock prices of the firm since they will not be holding shares any more. However, in stock transactions they share the risk with the bidder as they enjoy the increase or suffer from decreases in share prices. Aside from giving stocks of the acquiring company, the bidder may also pay in stocks of another company. The stocks of the German insurance company, Allianz were used as the exchange currency during the merger of two banks, Bayerischen Vereinsbank and Bayerischen Hypotheken und Wexhsel Bank. In addition to these two ways of stock usage in deals, issuing debenture stocks is another way of payment. Sometimes debenture stocks have an option of exchanging them with the stocks of the merger. So the target firm shareholders can decide if they want to convert the stocks into cash or acquire the stocks of the merger by examining how the merger is doing.

10. SUCCESS MEASURES AND FACTORS

Mergers and acquisitions became extremely popular during the 80's and 90's with the highly globalized world economy. The transaction volume became \$3,3 trillion by the end of 2000. However, according to previous researches, still 70% of takeovers end up in failure. According to a research conducted by Mercer Management Consulting and published in the Economist in 1998, 50% of a sample group of 300 companies involved in merger and acquisition transactions have provided less income than the sector average.¹⁰⁴ Michael Jensen, a prominent financial economist showed that shareholders of the acquired firms often earn above average returns but that of acquiring firms earn average close to zero.¹⁰⁵ Some studies showed that a high percentage (35-40%) of acquisitions have been sold at prices that produced a loss on the investment. According to a survey conducted by KPMG in 1999, only 17% of the respondents attained to create an added value to the combined company in terms of shareholder value whereas in 83% were unsuccessful in producing any positive effects.¹⁰⁶

In order to define a successful takeover, we first need to define what success means. Is it a positive achievement from bidder's or target's point of view? Success is not only about making a profitable deal, but it is mainly about attaining strategic goals. Success can be expressed in terms of every driving force of takeovers. A firm can lessen its profits due to decrease in efficiency while increasing its market share. Therefore, we cannot measure success by only one variable. A study by Watson Wyatt on 1,000 companies has shown that two-thirds of these companies failed to achieve their profit goals following a merger and only 46% met their cost-cutting goals. AT Kearney supported these findings by another research with a conclusion that 58% of mergers failed to attain their overall goals.

¹⁰⁴ Mercer Management Consulting, "A Year of Mergers in Europe?", **Economist**, (10.01.1998) taken from: "Birleşmelerde Başarı" *Şirket Birleşmeleri*, http://www.businessstomorrow.net/m&a_tr_basari.htm, (01.12.2005), p. 2

¹⁰⁵ Michael C. Jensen, "Takeovers: Their Causes and Consequences", **Journal of Economic Perspectives**, Vol:2, no:1, Winter 1998, pp. 21-48

¹⁰⁶ KPMG, "Mergers and Acquisitions: Global Research Report", 1999, p. 2

10.1 Success Measures

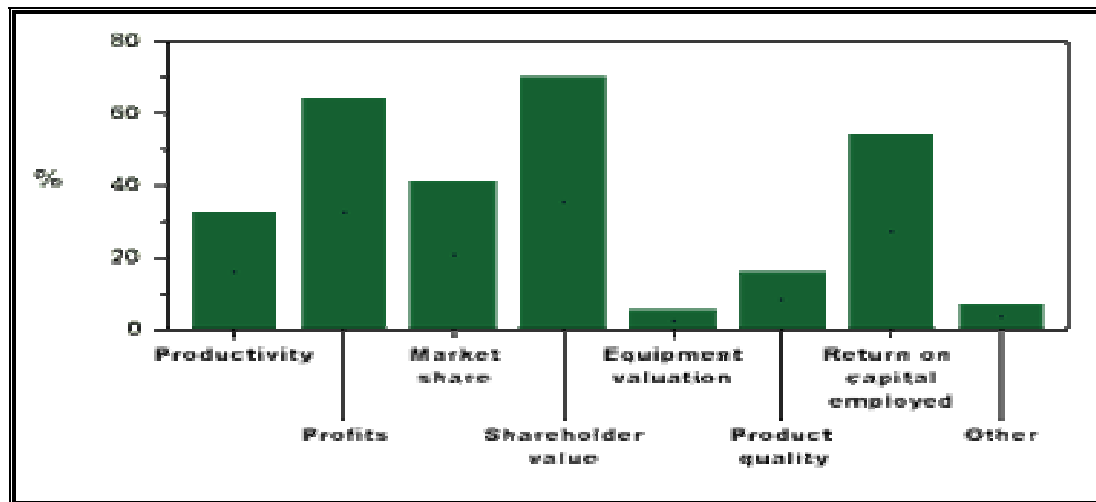
It is widely agreed that success may be defined as the synergy created by the combining firms, but synergy can be measured in different terms, operational, managerial, financial etc. The standard criteria should be set before the deal is closed and later these goals must be compared to the realized achievements. These standardized criteria may be strategic, operational and financial should be laid out as performance requirements. The criteria regarding operations finance and strategy are closely related to the objective of the deal. For example if the deal is done in order to achieve economies of scale, then the criteria should be focused on average and marginal costs per unit.

Various studies have shown that success criteria are composed of hard and soft elements. Hard components are generally pre-deal synergy, integration project planning and due diligence whereas the soft issues are related to the selection of top management, a new structure and communication. Although it has been known that soft issues are extremely important in the success of M&A's, the necessary attention has not been paid during the evaluation stages. The main reason for this deficiency is that such issues can not be easily assessed as easily as financial measures where executives can see the numbers and compare them with the previously set goals very easily. Another perspective is raised parallel to the "modern finance theory". In this neoclassical view of a firm, shareholder value maximization is posited as the ultimate rational criterion for investments and financing decisions made by managers. Professor Pankaj Ghemawat of Harvard Business School claims that stock price performance, accounting measures of profitability and other measures such as market share, achieving a strategic implantation and implementing strategy are the key criteria to measure success of mergers.¹⁰⁷ In 2000, KPMG's survey among Swiss companies indicates that 64% of the companies have defined success criteria before hand whereas 32% have not had any previously planned criteria. The same survey showed that 67% of the companies rely on

¹⁰⁷ Prof. Pankaj Ghemawat, "Mergers: A Prescriptive Perspective", <http://www.ftc.gov/be/rt/presentationpanel2.pdf>, (09.12.2002), p.2

profitability changes as success indicator.¹⁰⁸ Boston Consulting Group has considered the shareholder value as the measurement measure of a fruitful acquisition.¹⁰⁹ According to the survey held by Watson Wyatt Worldwide, European and North American companies cite shareholder value, profits and return on capital as the top three success measures although North America reverses the top two to put profits first. The same survey shows that The Asia Pacific respondents listed their top three as return on capital, market share and shareholder value, in that order.¹¹⁰ The following figure shows how the European respondents cite each success measure in percentages.

Figure 4
Most Effective Success Measures in Europe



Success Measures of M&A <http://www.watsonwyatt.com/canada-english/research/resrender.asp?id=eu09&page=3>, (2000), p.3

10.2 Success Factors

As this chapter is generally about the success of M&A's, we should also scrutinize the factors that lead a deal to success. Although there is an M&A boom since the 80's where transaction volumes are pronounced in trillions of USD, firms still fail

¹⁰⁸ KPMG, "Mergers and Acquisitions", http://www.kpmg.ch/library/pdf/2002_KPMG_Mergers_Acquisitions_in_Switzerland.pdf, (2002), p. 28

¹⁰⁹ BCG, "Succeed in Uncertain Times", http://www.bcg.com/publications/files/Value_Creators_2002_Rpt_Dec02.pdf, (2002), p. 24

¹¹⁰ "European Results of the Watson Wyatt Global M&A Survey" <http://www.watsonwyatt.com/canada-english/research/resrender.asp?id=eu09&page=3>, (2000), p.3

by a very high percent. There are several issues that acquirers should be careful of to avoid the pitfalls of a merger and acquisition deal because there are no ideal target firms in the market. If there had been an ideal company to acquire, then it would have not been sold at a price that the acquirer would have benefits over it. It must not be forgotten that there is no ideal company, yet there are companies with deficiencies; deficiencies that can uplift the acquirer or take it to failure.

10.2.1 Vision

Vision is maybe the most long-term issue in a merger and acquisition transaction. The undertakings of a deal usually have inadequate ideas about the benefits that the deal will contribute them. It is typical to hear about the cost-cutting and synergic advantages of a deal. Since analysts are glad to hear about these issues, the short-term effects of such comments would cause a rise in share prices, however if there is a lack of vision and a long-term strategy regarding these advantages, the companies will likely suffer from the negative synergic effect of a takeover. It is extremely important for firms to form a vision and strategy to create the synergy before the deal.

In order to have and follow a vision, first thing that companies must do is to define what the two companies can do in the future. A thoroughly made due diligence which is not only financial-orientated is the main tool for companies to define their capabilities. Then the companies should start thinking about where they want to be in the future. In other words, goals should be clarified and well defined. This would also provide the chance of a healthy evaluation process. This covers many aspects just like due diligence. It is not only about how much the companies will be earning, but also about their market share, product quality, markets they want to enter or exit etc. Then the management should clarify this vision with a clear and realistic statement that employees would follow by heart.¹¹¹

However vision is not only a statement that is written on a piece of paper or a bulletin that is hung on the wall. It is the way of thinking of the future, setting goals and

¹¹¹ Max M. Habeck, Fritz Kröger, and Michael R. Tram, **After the Merger**, 1st Edition, Great Britain: Pearson Educated Limited, 2000, p. 17-30

defining ways to achieve them. Therefore having and following a vision is intertwined with the planning of an M&A deal. This can be divided into three categories. If we go in order of the M&A process stages, firstly a company should find a strategically fit target. But what makes a target firm fit or unfit? It is more or less the issue that is written in the first paragraph of this vision section. It is what the other entity can give to this partnership and its potential for creating synergy. This corresponds to the part where bidders screen the potential targets in the planning stage. In short, a vision clearly helps the acquirers eliminate the unfit organizations and choose among the right ones. Secondly, a vision clarifies ways to achieve goals which corresponds to the implementation stage. The actions that should be taken in order to achieve these goals happen during the implantation stage where the optimum medium for success is prepared. It is obvious that a company that has a vision and pre-planning has a much better chance of preparing this medium more successfully and faster than a company that does not have a vision. Finally, as it is told before, clearly set goals make it much easier for a company to evaluate the success of an M&A which corresponds to the last part of an M&A process, evaluation and assessment stage.

10.2.2 Due Diligence

Due diligence involves a comprehensive analysis of all important target firm characteristics as financial condition, management capabilities, operational efficiency, core competencies, physical and intangible assets etc. After a thorough due diligence process, a bidder can price the target in a healthy way without paying an extra premium or offer a very low price. Due diligence can bring out the fact that a target may not be the firm that the bidder is seeking after all.

Due diligence takes place during the implantation stage of M&A deals. It is time-consuming, pressurizing and exhausting. However it has priceless benefits to the acquirer. Normally, due diligence happens in friendly transactions which is another reason why such deals have a higher rate of success than hostile deals. It should be underscored that the basis of integration success starts here and a comprehensive due diligence is tremendously important for achieving short-term and long-term goals.

What must be done during a due diligence can be outlined as; gathering and analyzing information so that the target is fit and there are no surprises that can stop the deal in future stages, understanding both companies cultures, examining legal and regulatory issues, and laying basis for further analysis to support program integration after closing the deal. According to the European results of Watson Wyatt Worldwide survey, the top three issues that companies assign priority are finance, strategic business development and operations. In addition that, soft issues like communication and HRM are comparatively low.¹¹²

10.2.3 Financing

Financing a merger and acquisition plays a crucial role in the after effects of the deal. Today, more than half of the deals are made through cash and the trend is looking up. It is a fact that cash transactions are rewarded in the markets by more favorable stock price evaluations. On the other hand, stock exchanging deals help companies to avoid high debt levels and debt levels are strong determinants of success in or failure in mergers and acquisitions. Therefore a company should carefully decide which instrument it is going to use in payment, cash, stocks or both. More details in financing choice related advantages and disadvantages were given in the previous chapter.

10.2.4 Friendliness or Hostility

Friendliness or Hostility is a key aspect in acquisitions. In hostile acquisitions, value to be created is usually destroyed as acquirers pay extra premium to targets, target firms reduce information transfer during due diligence process and many key executives leave the company. Friendly mergers and acquisitions also provide a means of overcoming cultural clashes since people are intended to work together in such cases since they believe that the deal will be in their interest as well. As it was mentioned in the due diligence, friendly deals also create an opportunity for the examination of the target firm thoroughly which enhances the probability of success.

¹¹² Watson Wyatt Worldwide, "European Results of the Watson Wyatt Global M&A Survey", <http://www.watsonwyatt.com/canada-english/research/resrender.asp?id=eu09&page=4>, (2000), p.4

10.2.5 Leadership

Companies are usually slow in handing over the leadership. Mostly, the leadership chaos is overlooked which becomes a threat to their existence. However, integration demands a strong leadership which allows acceptance and follow-up by employees. According to a Global PMI a survey held in 1998/99, 39% of companies fail to establish leadership fast and experience major problems consequently.¹¹³ The problems that are arising from lack of leadership can be in different ways. First of all, such a situation may create uncertainty in the workforce and panic which would be followed by departures of employees. Not only employees, but also customers or suppliers may be annoyed by this ambiguity and start orienting towards other companies. And maybe as the most important aspect of leadership is its role in employees' acceptance of change. A strong and soft skilled leader always become a champion for the workforce and gain their trust while leading them to a new environment that they are not familiar which creates the ambiguity in the first place. Another aspect of this issue is the power struggle. Just like a power struggle within a company can cause serious problems, struggles in a merger and acquisition can lead to the demise of the deal. Such power struggles have adverse effects as management's distraction from the focusing on business issues, decision-making for the management's own interest instead of the shareholders' at the expense of the rest of the organization.

Aside from these, leadership must be assigned before it is too late. Speed of the action is just as important as the action itself. Not leaving the shareholders in doubt, not leaving any space for speculation, looking decisive are all positive signals for the markets and it will definitely help generating a buy-in for the M&A.¹¹⁴ Moreover, the Watson Wyatt global M&A survey pointed out those companies in all three regions, Europe, North America and Asia Pacific, see leadership is the number one factor for success.¹¹⁵

¹¹³ Max M. Habeck, Fritz Kröger, and Michael R. Tram, p. 40

¹¹⁴ Max M. Habeck, Fritz Kröger, and Michael R. Tram, p. 48

¹¹⁵ Watson Wyatt Worldwide, p.3

10.2.6 Risks

Risks are the inseparable parts of a merger or an acquisition. They cannot be eliminated yet they can only be minimized. The way to minimize it is to have a good risk management team, because what is worse than risks being realized is their realization under the circumstances where they are not managed well which will cause a magnifying effect. However, if risks are managed well, they can be strengths of a company.

What needs to be done first is the assessment of the situation and the obstacles that are encountered. Aspects (i.e. financial, legal, technological etc.) can be assessed in criticality and complexity dimensions which will help prioritizing the issues. After this stage, companies should be analyzing the key variables and making assumptions that will be clarifying the risks and their outcomes. The important thing here is that people should keep their objectivity and build the scenarios in a broad view. Then just like prioritizing the issues, risks must be assessed in terms of urgency. Then all risks should be categorized. One way of doing this can be dividing the risks as very urgent, moderately urgent, and less urgent. Lastly, the risks must be addressed in order of their urgencies. By addressing a risk, a company can either try to resolve the risk or to lower the dependence of the project on the related risk. However companies should not forget that addressing a risk either by trying to minimize its impact or resolve the risk changes the internal and external circumstances which may give raise to other risks or enhance the already present risks. Therefore, assessment should be continuing without stopping.¹¹⁶

10.2.7 Human Resources

Human resources are maybe the most important issues in post-merger integration. They have more than one aspect to be carefully examined and each one is indispensable for success.

¹¹⁶ Max M. Habeck, Fritz Kröger, and Michael R. Tram, p.123-131

In a survey based on 413 HR directors in companies with 2,000 or more employees, 70% of the respondents agreed on that **communication** is one of the most important issues which needs to be addressed. Lack of communication between all levels is a significant reason why mergers fail. Not only lack of communication, but also holding back of information under the cover of discreteness is another way of communication and therefore merger and acquisition failure. Middle management and lower level employees feel left out, confusion, uncertainty, loss of trust and loyalty are the other emotions that people feel during lack of communication.

Loss of key employees who are the greatest of all assets is maybe the highest price of corporate mergers and acquisitions. According to American Management Association, one out of four top performers leaves the company within 3 months upon the announcement of a major change in organization and 47% of the senior managers within the first year. However, gaining a skilled workforce, know-how, knowledge and expertise are basic motives for mergers and acquisitions. Therefore the expected synergy can never be achieved if such losses occur. In many cases, employees leave not by their free will as companies reduce the employee numbers and downsize for cost savings. It should not be forgotten that key employees have the ability to take away their customer to a competitor. Not only the leaving employees tackle the success of mergers and acquisitions, but also de-motivated employees play a crucial role in this. Good communications pay and reward strategies, not going to downsizing, distinguishing between talented and ordinary employees are ways of retaining key employees in the business.

Even though undertakings may seem to be right for each other and all negotiations go well, the deal may result in a disaster if **cultural clashes** are taken care of. Every corporate has its own way of making business, an organizational structure that its employees are used to or even a dress code. Cultural differences that cannot be resolved affect communications, decision-making, productivity and no doubt the merger and acquisition success. At the end of the day, you cannot expect a company to function well if people cannot function together well. To avoid cultural clashes, a company should know the differences beforehand and then take strategic actions to reconcile the

differences. A survey within the companies can point out the main differences between the merging companies' employees. Later on, communication processes should bring the parties together in social and professional activities. To avoid the mindset of being conquered or conquerors, the most important thing is to make as many people as possible get to know each other as soon as possible. Steven J. Wall, "Making Mergers Work", *Merger Integration*, March/April 2001. In addition to that, since cross-border mergers and acquisitions have increased by a large volume, companies should inform their employees about another country's culture or even maybe start a language course for necessary departments for things to work out smoothly.

According to Watson Wyatt's global M&A survey, retention of key talent, communication and cultural integration have been ranked as the top three critical success factors. Communication, retention of key talent and cultural integration received rankings of 4.82, 4.67 and 4.32 respectively out of a scale of 5 in terms of criticality.¹¹⁷

¹¹⁷ Watson Wyatt Worldwide, p.6

11. RESEARCH DESIGN AND METHODOLOGY

11.1 Objectives of the Study

Throughout the literature review of this study, information about mergers and acquisitions were given considering various aspects of the issue. Within the study, driving forces behind mergers and acquisitions, factors that affect the degree of success that is achieved after the transaction, criteria that compose the index of success are examined.

The objectives of this survey are to compare Turkish and foreign companies' points of views to the driving forces behind M&A's when they make a transaction with each other in Turkey, actions to be taken to achieve success in an M&A transaction and the criteria that are measured for financial success determination of the transaction.

11.2 Data Collection and Sampling

Data was collected by means of a questionnaire via e-mail which means that primary data is used in the study. Primary data is used especially when the researcher wants to measure perceptions about a specific project at hand. Survey via e-mail was determined because of the wide dispersion of the respondents, the easiness that they could fill the survey in their own time, flexibility of being able to wait for the survey results before taking actions and minimization of cost of conducting the research. Respondents were informed that their answers would be used only for this research and not be revealed for any reason without their permission. Beyond an appeal to help the research, respondents were not offered any other incentive to complete the survey.

This study was conducted among Turkish and foreign companies which have realized M&A deals with each other in Turkey. The target population also met the following criteria:

- Deals that have taken place during the single party government (years '03- '04- '05)
- Not privatization deals or TMSF sales

- Deals that are not between mother company and affiliates or sister companies

The sampling frame that is used was obtained from Earnst & Young's M&A Transactions Report 2003-2004-2005. According to the reports, there had been 108 companies in accordance with the target population criteria. I could get hold of 102 companies, but only 56 respondents returned the questionnaire. However, 3 of those were not usable, so 53 questionnaires were used for the statistical inference. Out of 53 respondents, 26 were representing Turkish and 27 were representing foreign sides.

Table 2

Distribution of the Respondents

origin of the company	
Turkish	26
Foreign	27
total	53

11.3 Limitations of the Study

Just like many other studies, this study has its own restrictions. Since a merger or an acquisition is definitely a strategic decision, the highest authority in making the decision is the CEO of a company. However, since it is very difficult to reach the CEO of a huge national or multinational company and expect them to participate and spare their limited time in a voluntary issue like this, the respondents of this survey are partly CEO's and other high kevel managers whereas most of them are mid-level managers. However this does not mean that the respondents are under qualified for the survey since their positions are related with the issue. Still, every respondent being CEO's would have been better for a research like this.

Another limitation of this study is that only one respondent represented his/her company. Since it was already hard to convince people take part in the study, it was almost impossible to reach more than one person per company. It would have been

much more accurate if I could receive multiple responses from each company and take the average of scores. However because of managers' limited time and it was a very busy time of the year, I could get only one response to represent a company.

11.4 Measurement Instrument

The questionnaire is prepared by the researcher while considering the previously conducted studies. The questions about the driving forces are taken from Gammelback's study.¹¹⁸ The part that is related to the success factors is taken from the survey from Habeck, Kröger and Tram's collaborative study.¹¹⁹ The part about the financial performance criteria is taken from the Wataon Wyatt Survey.¹²⁰ The questionnaire is consisted of 28 questions including the ones about general information of the company and the respondent. Respondents are asked to indicate their answers in a 5-point Likert scale, ranging between "not important at all" to "very important". A pilot study involving 10 foreign and 10 domestic firms was conducted and fortunately there was no need to make any changes in the questionnaire.

A copy of the questionnaire used to gather the research data can be found in the appendix section of this study.

Given the information in literature review, the driving forces are handled in market-related strategic factors, economical factors, financial factors and technological factors. The success factors are taken into account in three dimensions, namely strategic, financial and HR. Measures of success can be divided into three factors which are financial, structural and HR. However in this study, only the financial factor is considered. One reason for this decision is that the ultimate two goals of a commercial entity are first to make its presence everlasting and second to make profit which is a financial issue. Another reason is that since financial measures are more concrete than the other dimensions since they are represented by solid numbers which can be assessed

¹¹⁸ Gammelgaard, "Access to Competence: An Emerging Acquisition Motive", pp. 44-46

¹¹⁹ Habeck, Kröger, and Tram, pp. 13

¹²⁰ European Results of the Watson Wyatt Global M&A Survey, p. 3

clearer than more abstract issues such as employee satisfaction. The elements that are considered in this study are given with the related question numbers in the questionnaire that is utilized as follows:

Grouping determinant:

1- Origin of the company: Section I - Q 2

Elements to be compared between groups:

1- Driving Forces (Section II)

1: market-related strategic dimension Q 1 and 6

2: cross-border market extension dimension Q 2

3: economical dimension Q 3, 4 and 5

4: financial dimension Q 7

5: technological dimension Q 8 and 9

2- Success Factors (Section III)

1: strategic factor Q 1, 2 and 5

2: human resources factor Q 7, 8 and 9

3: financial factor Q 3, 4 and 6

3- Financial Performance Evaluation Criteria (Section IV)

1: financial criteria Q 1, 2, 3, 4 and 5

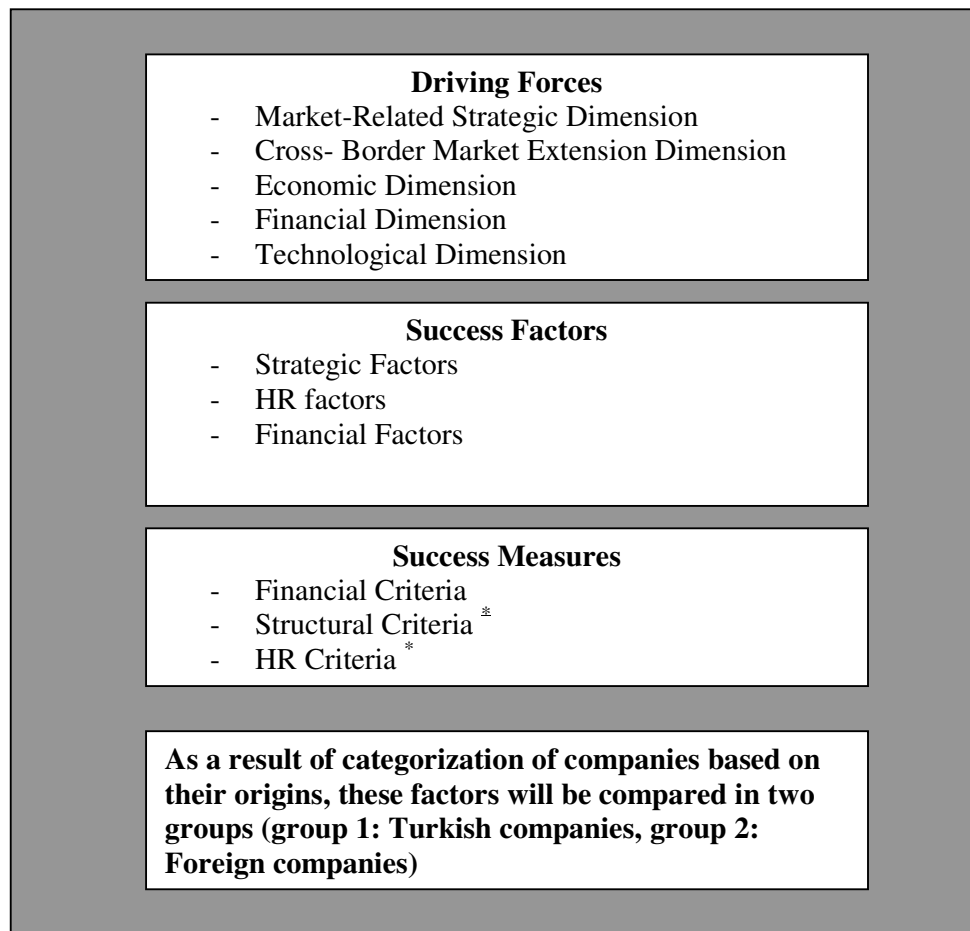
11.5 Conceptual Model

The elements that are to be compared between Turkish and foreign companies are depicted in Figure 5 of this section. The model designed for this study consists of one determinant which groups the total sample in two categories and three subjects

which are the motives behind M&A's, the success factors that lead to success and the financial performance evaluation criteria.

Figure 5

Conceptual Model of Comparing Turkish and Foreign Companies in terms of Driving Forces, Success Factors and Success Evaluation Criteria regarding M&A's



11.6 Hypotheses

H1- Turkish and foreign companies have different motives for making M&A deals with each other in Turkey.

H2- Turkish and foreign companies think differently about the importance degree of success factors in M&A's.

H3- Turkish and foreign companies have different priorities of financial measurement criteria when they evaluate M&A success.

12. FINDINGS

In this chapter, reliability analysis, Mann-Whitney test and Friedman test results are presented. The analyses were conducted by using SPSS 13.0. For the reliability tests, data set is assessed as a whole whereas for Mann-Whitney tests, data set is handled as two groups determined by the grouping factor, origin of the company. As for Friedman tests, both groups are analyzed separately and also as a whole. As confidence level in Mann-Whitney test, the critical value is taken as 0, 95 which makes the significance value as 0, 05.

12.1 Reliability Analysis

Although there are five factors in terms of driving forces that lead to M&A, two of them, cross-border market extension factor and financial factor are omitted in the reliability analysis because in the questionnaire, they were represented in one item each. As can be seen in the following table that is in the next page, the Cronbach's Alpha values are reasonably high.

Table 3
Internal Consistency Values

Factor to be measured	Cronbach's Alpha
<i>Driving Forces</i>	
<i>i) Market-Related Strategic Dimension</i>	0,87
Increase in market share	
Product/service diversification	
<i>ii) Economic Dimension</i>	0,80
Economies of scale	
Economies of scope	
Decrease in product/service costs	
<i>iii) Technological Dimension</i>	0,86
Improvement in an already acquired technology	
Acquiring a new technology	
<i>Success Factors</i>	
<i>i) Strategic Factor</i>	0,68
Having and following a vision	
Assigning leadership	
Providing a friendly deal	
<i>ii) HR factor</i>	0,79
Good communication within the company	
Retaining key employees	
Stopping cultural clashes	
<i>iii) Financial Factor</i>	0,80
A carefully made due diligence	
Making the right choice about financing the deal	
Thoroughly made risk analysis	
<i>Financial Success Evaluation Criteria</i>	
<i>i) Financial Success Evaluation Criteria</i>	0,70
Efficiency	
Profitability	
Market Share	
Share Value	
Return on Capital	

12.2 Mann-Whitney Tests

The following Mann-Whitney test results are presented in order to point out the differences in the way that Turkish and foreign companies think about the motives behind M&A's, the factors that lead to success and the financial performance evaluation criteria. Averages of the scores of the items related to the relevant factors are taken into account while conducting the analyses. The full test results can be found in the appendixes.

Table 4
Mann-Whitney Test Results

Dimensions to be measured	Significance
<i>Driving Forces</i>	
i) Market-Related Strategic Dimension	0,000
ii) Economic Dimension	0,418
iii) Technological Dimension	0,031
iv) Cross-Border Market Extension Dimension	0,000
v) Financial Dimension	0,000
<i>Success Factors</i>	
i) Strategic Factor	0,120
ii) HR factor	0,665
iii) Financial Factor	0,440
<i>Financial Success Evaluation Criteria</i>	
i) Financial Success Evaluation Criteria	0,171

As can be seen from the table, there are significant differences in market-related strategic factor, technological factor, cross-border market extension factor and financial factor. However, we see no difference in success factors and financial success evaluation criteria. When we look at the descriptive results, it becomes obvious that Turkish companies consider technological factors, market related strategic factors, financial factor as the aspects that they can benefit from foreigners whereas the foreigners think about extending their market reach by entering new markets.

12.3 Friedman Tests

Below are the results of Friedman tests which are conducted in order to find if there is any significance in orders of importance both when the data set is taken as a whole and separated in terms of the grouping variable, origin of the company. All the significance levels have come out to be less than 0,05 which meant that there is a significant difference in orders as a whole and also in separate groups.

Table 5
Friedman Test Results of Driving Forces for Turkish and Foreign Companies

Item	Mean Rank (Turkish)	Item	Mean Rank (foreign)
Increase in market share	7,63	Entering new markets	8,63
Product/service diversification	6,52	Decrease in product/service costs	6,67
Improvement in financial structure	5,75	Product/service diversification	5,17
Acquiring a new technology	4,85	Increase in market share	5,11
Entering new markets	4,42	Economies of scale	5,02
Improvement in an already acquired technology	4,21	Economies of scope	4,89
Economies of scope	4,13	Improvement in an already acquired technology	3,67
Economies of scale	4,12	Improvement in financial structure	3,00
Decrease in product/service costs	3,37	Acquiring a new technology	2,85

The table in the previous page shows us that Turkish companies are sensitive about increasing their market shares, diversifying their products and services, improving their financial structures whereas they do not expect much in terms of decreasing their product costs and obtaining economies of scale and scope. On the other hand, foreign companies care about entering new markets, decreasing their product/service costs and diversifying their products. Acquiring new technology, improvement in financial structure and technology are least important objectives for the foreigners.

Table 6
Friedman Test Results of Driving Forces for the Whole Data Set

Item	Mean Rank (total)
Entering new markets	6,57
Increase in market share	6,35
Product/service diversification	5,83
Decrease in product/service costs	5,05
Economies of scale	4,58
Economies of scope	4,52
Improvement in financial structure	4,35
Improvement in an already acquired technology	3,93
Acquiring a new technology	3,83

If we look at the companies as a whole without paying attention to their origins, entering new markets, increasing their market shares which are about realizing potentials in markets are the top two items in ranking. Acquiring new technologies and improving the already acquired technology are seated at the bottom of the list.

Table 7
Friedman Test Results of Success Factors for Turkish and Foreign Companies

Item	Mean Rank (Turkish)	Item	Mean Rank (foreign)
Having and following a vision	6,31	Having and following a vision	6,11
A carefully made due diligence	6,19	A carefully made due diligence	6,00
Retaining key employees	5,67	Assigning leadership	5,74
Thoroughly made risk analysis	5,27	Stopping cultural clashes	5,41
Assigning leadership	4,77	Thoroughly made risk analysis	4,91
Stopping cultural clashes	4,69	Retaining key employees	4,83
Making the right choice about financing the deal	4,33	Providing a friendly deal	4,78
Good communication within the company	4,06	Good communication within the company	3,76
Providing a friendly deal	3,71	Making the right choice about financing the deal	3,46

Table 7 shows us the mean ranking orders of success factors according to Turkish and foreign companies separately. Both Turkish and foreign companies think that having and following a vision with careful due diligence procedures are the most important factors to be followed in order to achieve success after an M&A deal. Yet again, both groups think that making the right choice about financing the deal, communication within the company and providing friendly deals are the least important factors.

Table 8
Friedman Test Results of Success Factors for the Whole Data Set

Item	Mean Rank (total)
Having and following a vision	6,21
A carefully made due diligence	6,09
Assigning leadership	5,26
Retaining key employees	5,25
Thoroughly made risk analysis	5,08
Stopping cultural clashes	5,06
Providing a friendly deal	4,25
Good communication within the company	3,91
Making the right choice about financing the deal	3,89

As a summation of the results of the previous table, table 8 also shows us that vision and due diligence are the leading factors as assigning leadership and retaining key employees are the following important factors. Providing a friendly deal, good communication within the company and making the right choice about financing come out to be the least important factors which is no surprise because these factors were at the bottom three places for each group.

Table 9
Friedman Test Results of Financial Performance Evaluation Criteria for Turkish and Foreign Companies

Item	Mean Rank (Turkish)	Item	Mean Rank (foreign)
Return on Capital	3,27	Profitability	3,50
Efficiency	3,17	Return on Capital	3,07
Profitability	3,17	Efficiency	2,91
Share Value	3,08	Share Value	2,81
Market Share	2,31	Market Share	2,70

Table 9 tells us the ranking orders of financial performance evaluation criteria from both parties' points of views. It is shown that return on capital, efficiency and profitability are the first three criteria that every company cares about, yet in different orders. Share value and market share are the last two criteria that companies inspect when evaluating financial criteria.

Table 10
Friedman Test Results of Financial Performance Evaluation Criteria for the Whole Data Set

Item	Mean Rank (total)
Profitability	3,34
Return on Capital	3,17
Efficiency	3,04
Share Value	2,94
Market Share	2,51

When looked as a whole, the most important three criteria stay at the top while profitability gets the leading position. Return on capital and efficiency are the following criteria while share value and market share criteria are the ones that companies lastly.

12.4 Discussion

According to the results of the study, regarding to driving forces clearly there are differences in market-related strategic factors. We can see that Turkish companies definitely expect market-related benefits more than the foreigners do. When we look at the descriptive statistics item by item, we can see that both increasing market shares and product diversification got higher scores from the point of Turkish companies. On the other hand, foreign companies seem to wish to extend their geographic reach in order to enter new markets which results in a significant difference in the cross-border market extension reason. Turkish companies apparently are not eager to enter new markets by using M&A's. This is also in accordance with the nature of M&A's in Turkey because most transactions happen to be acquisitions made by foreigners in Turkey. We can not really see huge mergers which limits the possibility of new market entrance for Turkish companies. With a population of 70 million and being most of it as youngsters, the foreign goal makes sense. On the other hand, Turkish side has an intention of gaining market shares with the synergy that will be created by the benefits of a foreign partner, such as a globally known famous brand name. In terms of economical factors, there is no significant difference; however the difference in mean scores of decrease in product costs could be worth some attention. It is known that Turkey has a competitive advantage in labor costs, location and raw materials which may explain the roots of cost reduction abilities. Results indicate that Turkish companies expect financial improvement by making a deal with foreign companies. This is in no contradiction with the fact that after the economic crises in Turkey, domestic firms have gone through problems related to lack of equity. One of the striking examples came from the financial sector in Turkey where banks were confiscated. As of technological factors, Turkish companies are more eager to improve or acquire technologies which are parallel to the fact that Turkey is not a technologically developed country.

When success factors are examined, we see that none of the three dimensions, namely, strategic, human resources and financial, imply any differences between the two groups. Therefore we may say that both parties think the same way in the necessary actions that are to be taken to achieve success. However, when we think about the high failure rate of M&A's, serious doubts rise about the implementation of actions. Both parties think of having and following a vision with a deep due diligence process are the top-of-the-list factors hence there are no significant differences. It should also be noted that the means for assignment of leadership, friendliness of the deal, stopping cultural clashes are higher for the foreign side, though not significantly. We can say the same thing about the Turkish side for right choice about financing.

Lastly, it is clearly put forward in the study that there are no differences in the way the financial success of M&A's are evaluated. When we look at the means, it can be said that Turkish side thinks the return on capital is the most important criteria and the foreign companies think the profitability is the most important criteria. Return on capital, efficiency and profitability are the top three criteria that companies examine when they want to assess the financial performance. Nevertheless there is no significant difference between the two groups.

13. CONCLUSION

This study has examined the differences between Turkish and foreign companies about the driving forces behind realizing merger and acquisitions with each other in Turkey, the factors that lead an M&A deal to success and the criteria they use to evaluate the success of the deal. The study does not imply what companies should do to achieve success; instead it tries to grab an insight of the points of views of the two groups.

Since mergers and acquisitions are very new subjects in Turkey, there has been no research that investigates the differences between the points of views of Turkish and foreign companies. However there are myriad studies about the driving forces and success factors and enough number of studies about the financial performance criteria.

The literature study reveals that market related motives, cost cutting synergy effects, diversification and as a result increasing shareholder value are the main driving forces behind M&A deals. The survey of this study also shows similar results to the literature survey. Entering new markets, increasing market share, diversification, decreasing costs and economies of scale came out to be the most important driving forces in order. It is understandable that foreign companies want to enter new markets in Turkey. With its large population, decreasing inflation and steadily increasing GNP, Turkey became one of the fastest growing developing countries which make it very feasible to invest and do business. In addition to that, the new regulations which are related to foreign direct investment enabled foreigners to feel safer when investing in Turkey. With its rich raw materials, cheap labor and geographic advantages, Turkey also has a big advantage of decreasing foreign companies' costs. Turkish companies on the other hand obviously want to increase their market shares. By being partners with foreign companies, they can promote their products with labels that are world wide known which build trust among consumers and brand knowledge would automatically increase. Especially after the 2001 economic crisis in Turkey, many businesses went down due to insufficient capitals and the survey results clearly shows that Turkish companies expect financial support from partnerships. Also the high technology that developed companies possess seems attractive to Turkish companies because they can

use their capacities more effectively and also create a competitive edge against their rivals in their industries. So, just like the literature survey tells us, the companies are after synergy and the market related gains which are consequences of this synergy. Although the motives are parallel to the literature survey, it should be emphasized that the importance of the motives for the two parties differs when compared with each other except for economic reasons. The results show that except for cost cutting synergies, these two parties expect different benefits from each other which in consequence brings out the synergic gains.

Only for the last one or two decades, companies and researchers started focusing on measuring the soft issues on success. However, it is still true that companies put the financial success on top of their priority list. This matches with the neoclassical view of economy. One reason for this is that shareholders' value maximization is the ultimate goal for managers and another reason is that it is much easier to measure success financially since facts and figures are easy to interpret. On the contrary, soft issues like human resources and structural success are harder to measure. In the literature survey, share value, profits, productivity, market share and return on capital are found out to be the mostly used criteria when evaluating financial success. In this study, the survey results are in the way that both Turkish and foreign companies think that profitability, return on capital and efficiency are the most important criteria that companies pay attention to. Therefore, it is impossible to say that there are any differences between the two sides about the way they evaluate financial success.

As for the success factors, just like the success evaluation criteria, there are no differences between the two sides. The factors are parallel to the literature survey, so there is no doubt that every company executive in the world think of the same factors in order to achieve success. However it is also known that failure rates are around 60-70 % and even in some studies this rate is around 80-86%. So clearly there is something wrong with the implementation of putting these factors into practice. Another possibility is that companies underrate some factors and overrate others. As a result, they don't concentrate on the necessary issues and their weaknesses bring their ends. For example, in the survey, both companies thought that communication is not as

important as the other factors. Although communication is a major success factor in the human resources dimension, the literature also shows us that other success factors are at better places in survey results. No matter how much the researchers underline that good communication goes a long way in M&A's, the companies seem to be ignoring this fact. Although most firms put communication on top places of surveys, the failure rates tell us another story. What companies should do about this is that firstly they should spot their weak points accurately and honestly, spend more time on cultural issues more, implement these essential success factors sharply and most importantly act coherently with the survey results because actions speak louder than words.

I, as the researcher of this study, hope this work will be useful to other researchers and companies, which are especially in Turkey where mergers and acquisitions are becoming extremely important day by day.

APPENDIXES

Appendix 1- Research Questions

- What are the driving forces for companies to make an M&A deal in Turkey?
- What are the success factors that lead an M&A deal to success?
- How do companies measure the financial success after an M&A deal?

Appendix 2- Questionnaire (in English)

As a part of an MBA thesis that is held in Marmara University, Turkey, a survey is being conducted about merger and acquisition activities. Thank you for your participation and time. (PS: The information you provide will not be disclosed to third parties and results will be assessed as a whole.)

Thesis student: Arkin Balıkçioğlu arkinbalikcioglu@yahoo.com	Instructor: Assistant Prof. Aslı Küçükaslan
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PART I

1. Company name:						
2. Company's	Ownership Structure	Origin (Turkish/Foreign)				
	Turkish %	Foreign %				
3. Department and position:						
4. Does your company have any experience in mergers or acquisitions (M&A's) such as a realized deal, negotiations with other companies, delegation of power to a financial institution, establishment of a department related to M&A activity etc.?		<table border="1"> <tr> <td>Yes</td> <td>No</td> </tr> <tr> <td></td> <td></td> </tr> </table>	Yes	No		
Yes	No					

PART II

How important have the following motives been for you in M&A? (1 stands for "not important at all".... 5 for "very important") (If you are a foreign company, think of the opposite party as a Turkish company and vice versa)

	1	2	3	4	5
Increase in market share					
Access to new markets					
Decrease in production/service costs					
Economies of scale					
Economies of scope					
Product/service diversification					
Improvement in financial structure					
Improvement in an already acquired technology					
Acquiring a new technology					

PART III

How important are the following factors for a successful M&A? (1 stands for "not important at all".... 5 for "very important")

	1	2	3	4	5
Having and following a vision					
Assigning leadership					
A carefully made due diligence					
Making the right choice about financing the transaction					
Providing a friendly deal					
A thoroughly made risk analysis					
Good communication within the company					
Retaining key employees					
Stopping cultural clashes					

PART IV

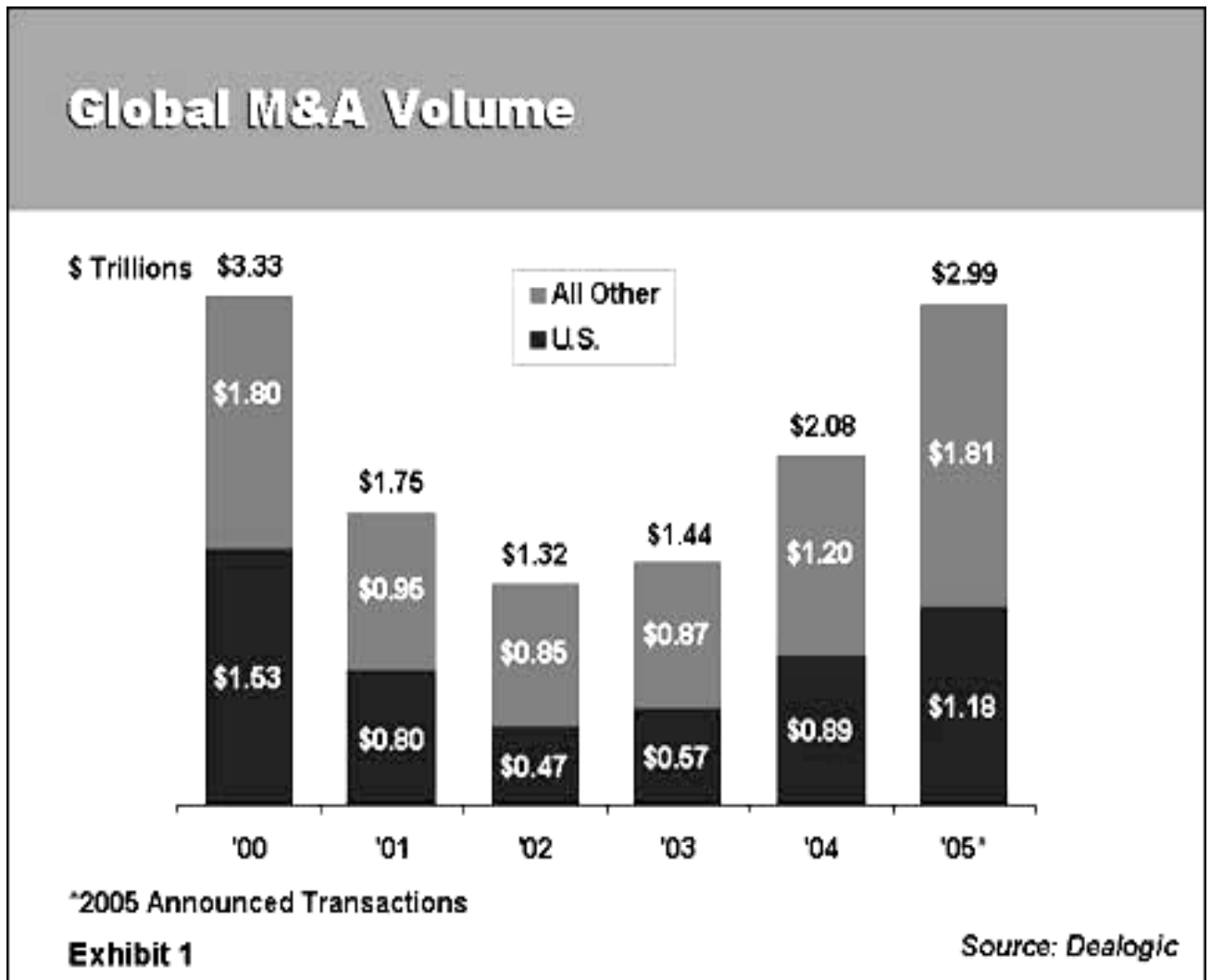
How important are the following criteria when you evaluate the financial success of an M&A? (1 stands for "not important at all".... 5 for "very important")

	1	2	3	4	5
Efficiency					
Profitability					
Market share					
Share value					
Return on Capital					

Appendix 3- Questionnaire (in Turkish)

Marmara Üniversitesi/ Sosyal Bilimler Enstitüsü İngilizce Yönetim ve Organizasyon MBA programı dahilinde yürütülen Şirket Birleşmeleri ve Satın Almaları konulu yüksek lisans tezi ile ilgili olarak bir anket çalışması düzenlenmiştir. Katkınız ve ayırdığınız zamanınız için teşekkür ederiz. (Vereceğiniz bilgiler 3. şahıslarla paylaşılmayacak olup sonuçlar toplu olarak değerlendirilecektir.)									
Tez Öğrencisi: Arkin Balıkcıoğlu arkinbalikcioglu@yahoo.com			Tez Danışmanı: Doç. Dr. Aslı Küçükaslan						
BÖLÜM I									
1. Firma adı:									
2. Firmanızın		Ortaklık yapısı		Orijini (yerli/yabancı)					
		Yerli %	Yabancı %						
3. Çalıştığınız departman ve pozisyonunuz:									
4. Firmanızın şirket birleşmeleri veya satın almaları ile ilgili daha önce gerçekleşen bir işlem, konu hakkında başka firmalarla görüşmeler, finansal bir kuruluşa yetki verme, konu ile ilgili kurulmuş bir birim vb. bir tecrübesi var mı?					<table border="1"> <tr> <td>Evet</td> <td>Hayır</td> </tr> <tr> <td></td> <td></td> </tr> </table>	Evet	Hayır		
Evet	Hayır								
BÖLÜM II									
Eğer yerli bir firmaysanız yabancı bir firma ile, eğer yabancı bir firmaysanız yerli bir firma ile birleşme veya satın alma işlemi yaptığınızda aşağıdaki nedenler sizin için ne kadar önemliydi? (1 hiç önemli değil 5 çok önemli anlamındadır)									
	1	2	3	4	5				
Pazar payını arttırmak									
Yeni pazarlara girmek									
Üretim/hizmet maliyetini düşürmek									
Ölçek ekonomisini yakalamak									
Kapsam ekonomisini yakalamak									
Ürün çeşitlendirilmesini sağlamak									
Finansal yapıyı güçlendirmek									
Mevcut bir teknolojiyi geliştirmek									
Olmayan bir teknolojiyi elde etmek									
BÖLÜM III									
Başarılı bir birleşme veya satın alma işlemi için aşağıdaki faktörler sizce ne kadar önemlidir? (1 hiç önemli değil 5 çok önemli anlamındadır)									
	1	2	3	4	5				
Bir vizyon dahilinde hareket etmek									
Lider takımın görevlendirilmesi									
İyi bir araştırma- inceleme safhası (due diligence)									
İşlemin finansmanı hakkında doğru seçimleri yapmak									
Dostça devir almayı sağlamak									
İyi risk analizi									
Şirket içi iletişim									
Anahtar çalışanları kaybetmemek									
Kültür çatışmalarını engellemek									
BÖLÜM IV									
Birleşme veya satın alma işleminin finansal başarısını ölçerken sizce aşağıdaki ölçütler ne kadar önemlidir? (1 hiç önemli değil 5 çok önemli anlamındadır)									
	1	2	3	4	5				
Verimlilik									
Karlılık									
Pazar payı									
Hisse değeri									
Sermaye getirisi									

Appendix 4- Global M&A Volume



<http://www.bofabusinesscapital.com/resources/capeyes/a01-06-321.html>

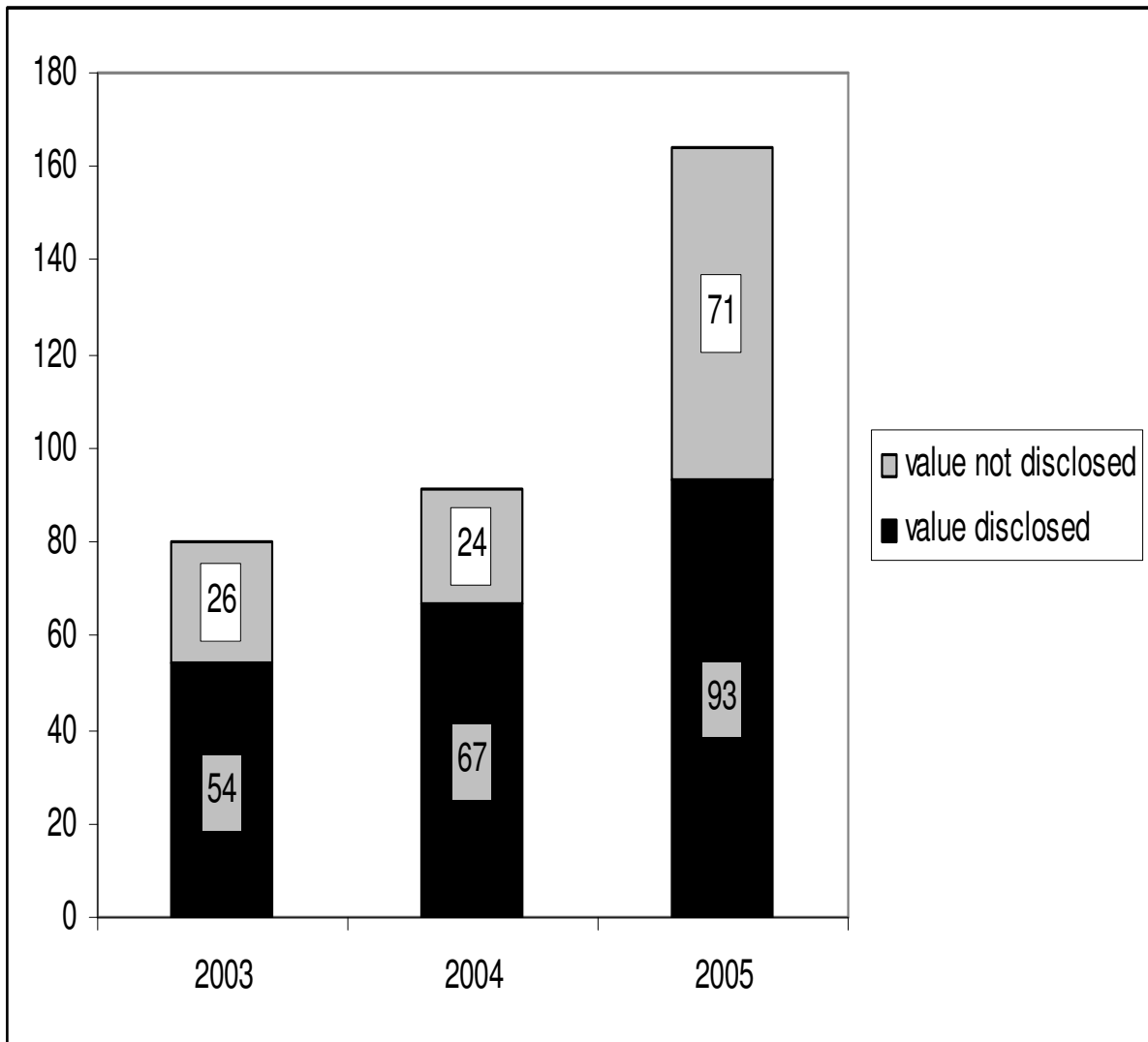
Appendix 5- 2005 Global M&A Deal Value by Range

'05 Global M&A Deal Value by Range		
Deal Range	'05 Completed Deal Value	'04 Percentage Increase
\$1 billion to \$10 billion	\$956.41 B	41.8%
\$100 million to \$500 million	\$478.12 B	14.9
\$10 billion and more	\$471.76 B	18.9
\$500 million to \$1 billion	\$260.07 B	11.2
\$100 million and less	\$227.79 B	11.3

Exhibit 4 *Source: Dealogic*

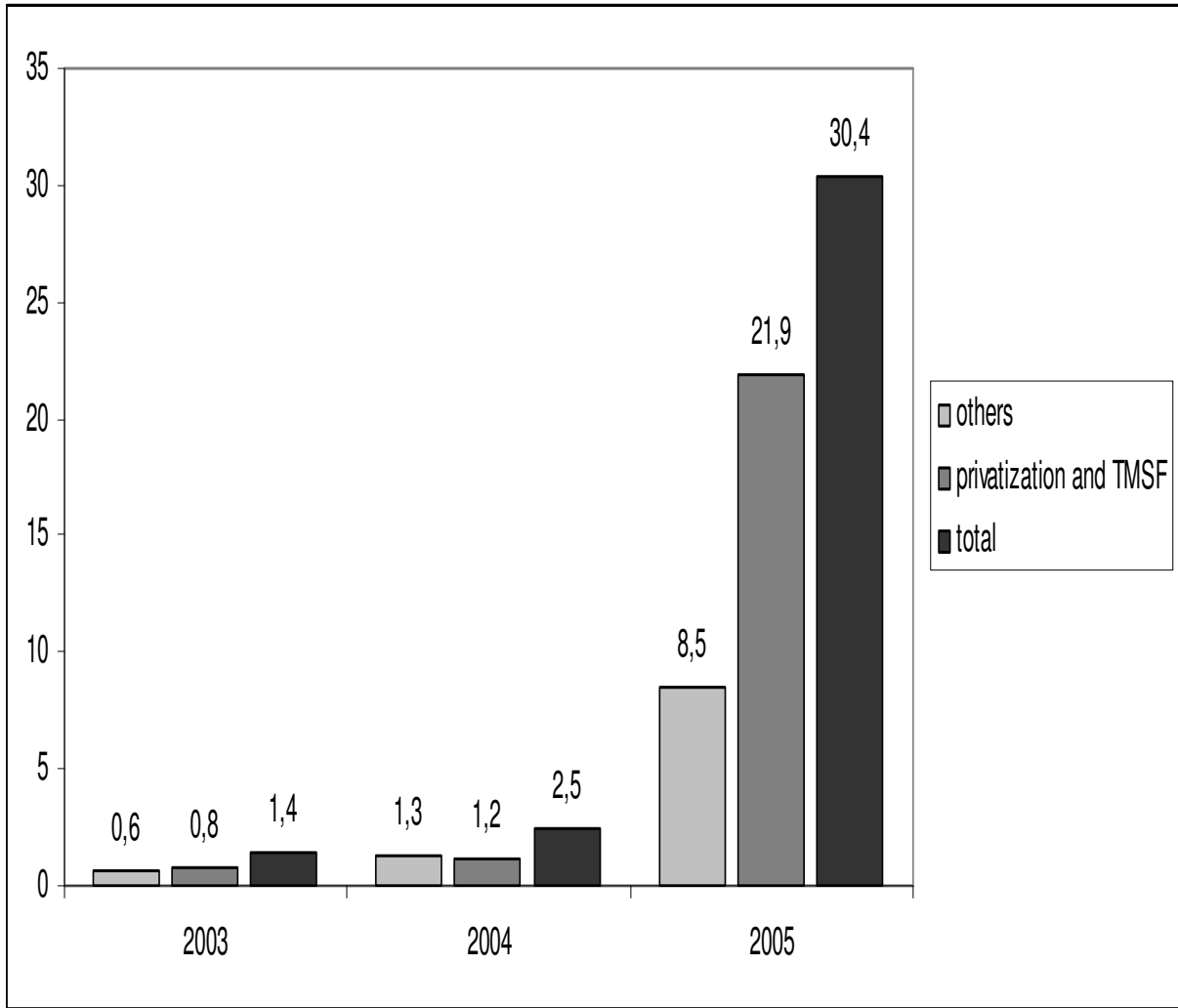
<http://www.bofabusinesscapital.com/resources/capeyes/a01-06-321.html>

Appendix 6- Number of M&A Deals in Turkey



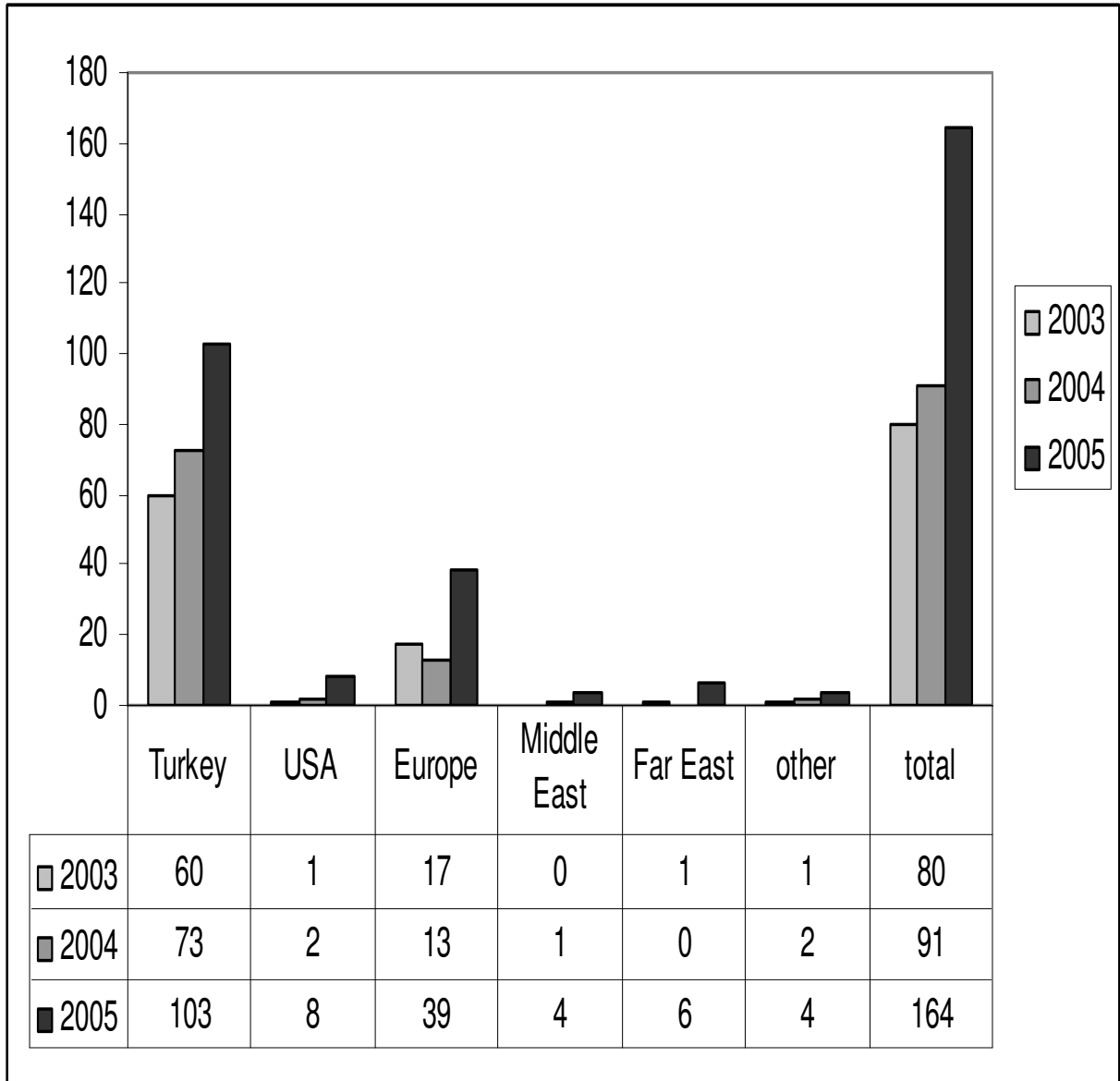
Earnst&Young Birleşme ve Satın Almalar Raporu (2003- 2004- 2005)

Appendix 7- Deal Volumes in Turkey (billions USD)



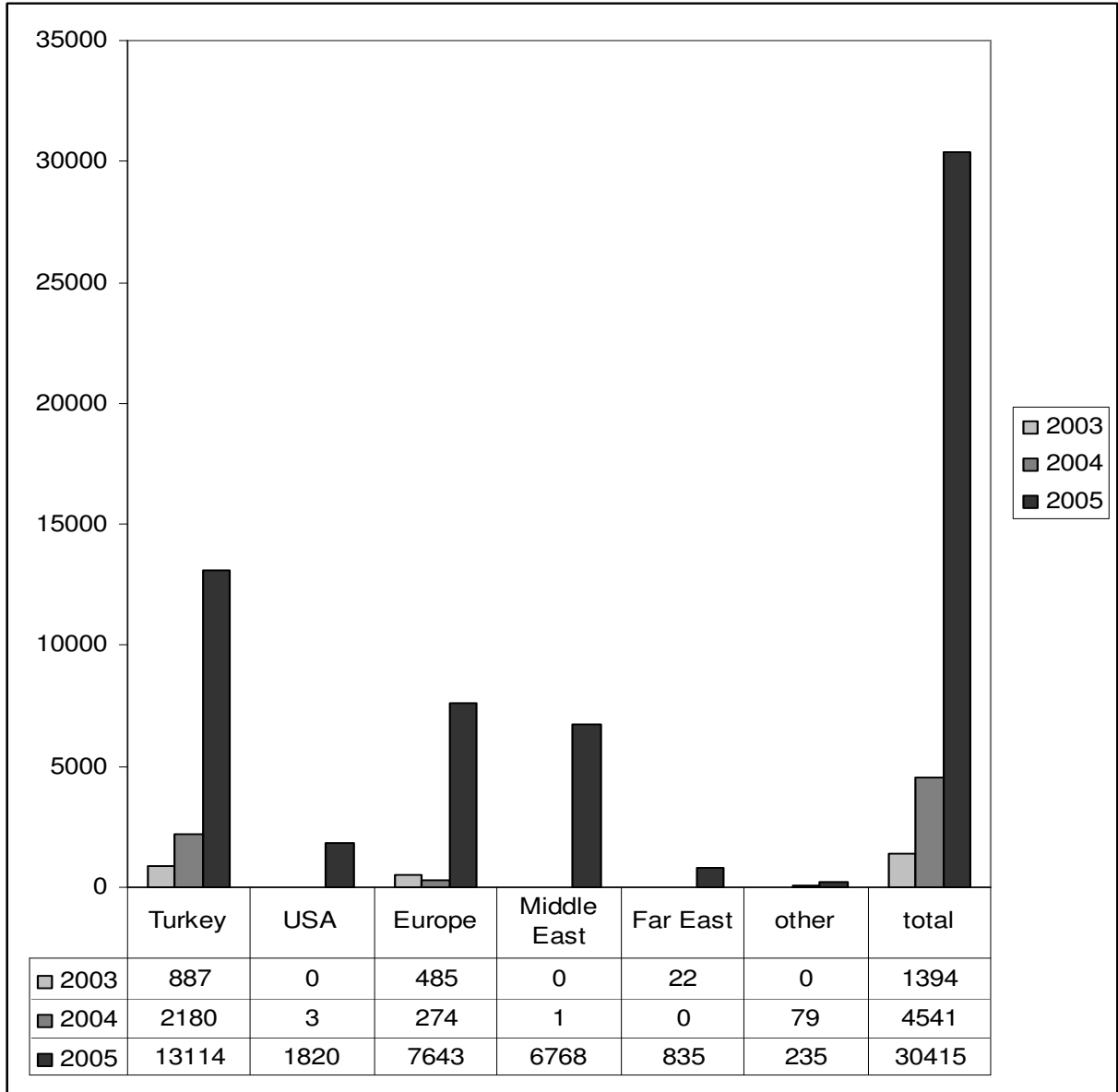
Earnst&Young Birleşme ve Satın Almalar Raporu (2003- 2004- 2005)

Appendix 8- Number of Deals in Turkey (sorted by origin)



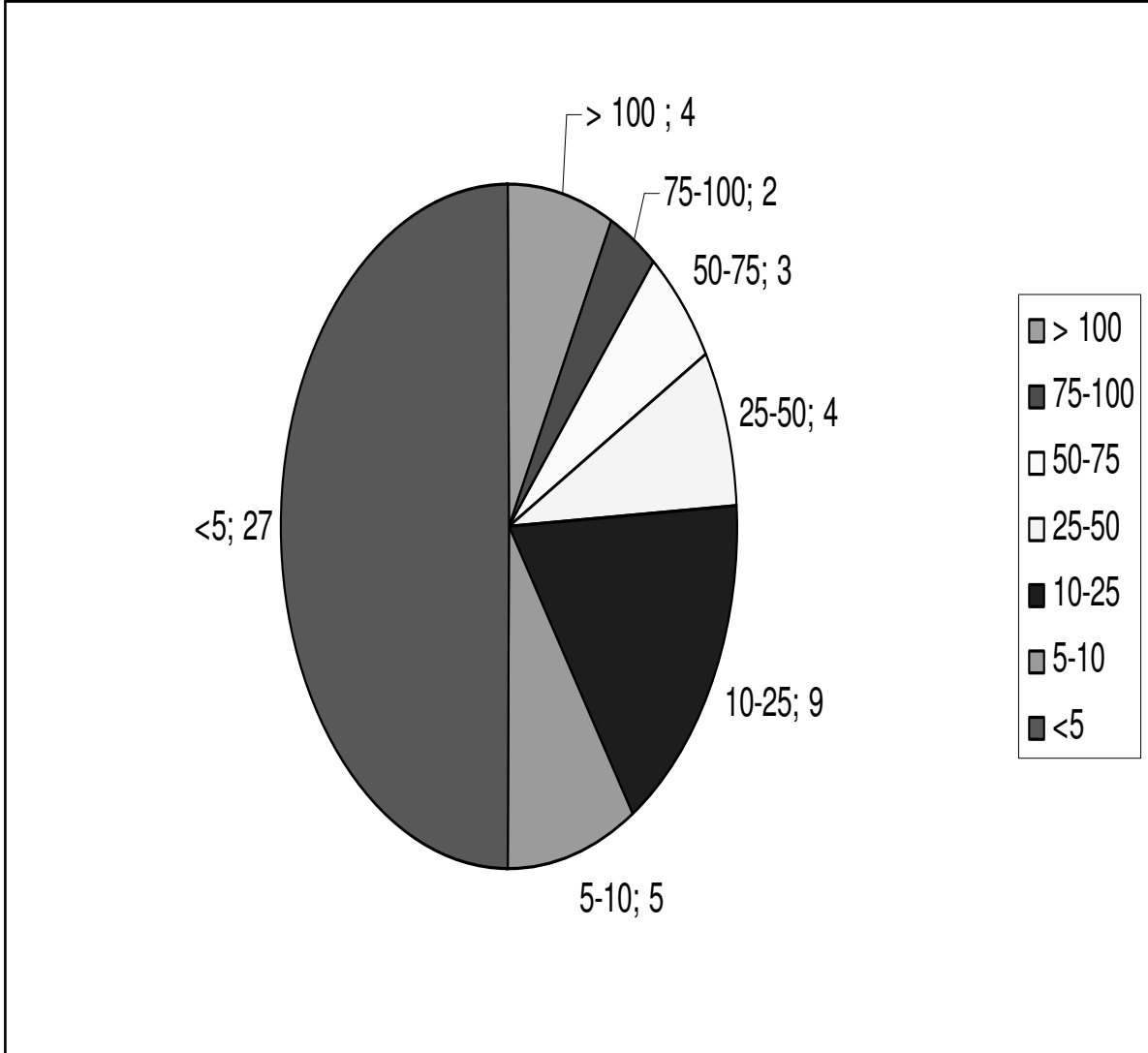
Earnst&Young Birleşme ve Satın Almalar Raporu (2003- 2004- 2005)

Appendix 9- Volume of Deals in Turkey (sorted by origin, millions USD)



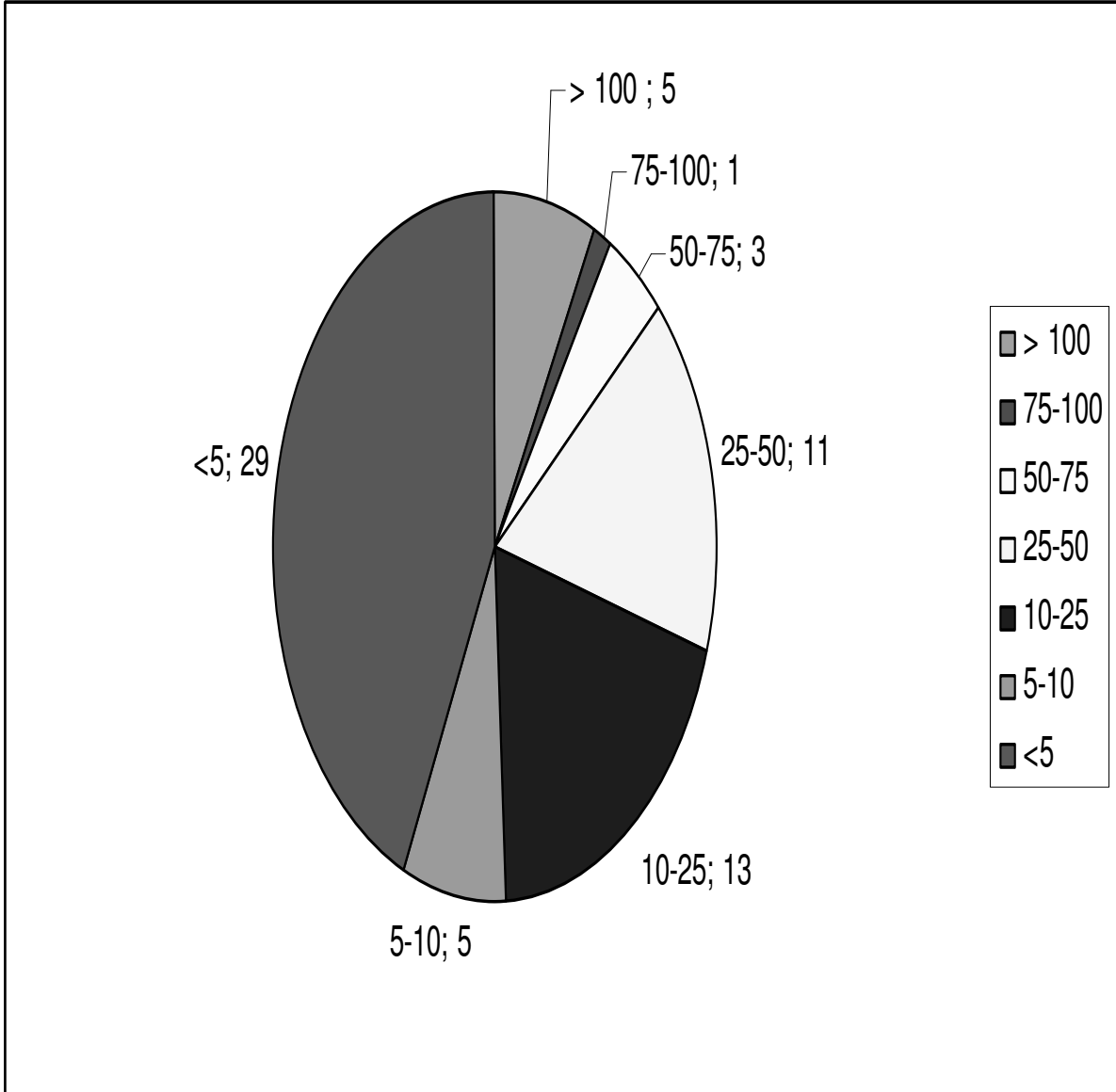
Earnst&Young Birleşme ve Satın Almalar Raporu (2003- 2004- 2005)

Appendix 10- Deal Value by Range, 2003 Turkey (deals with disclosed values, millions USD)



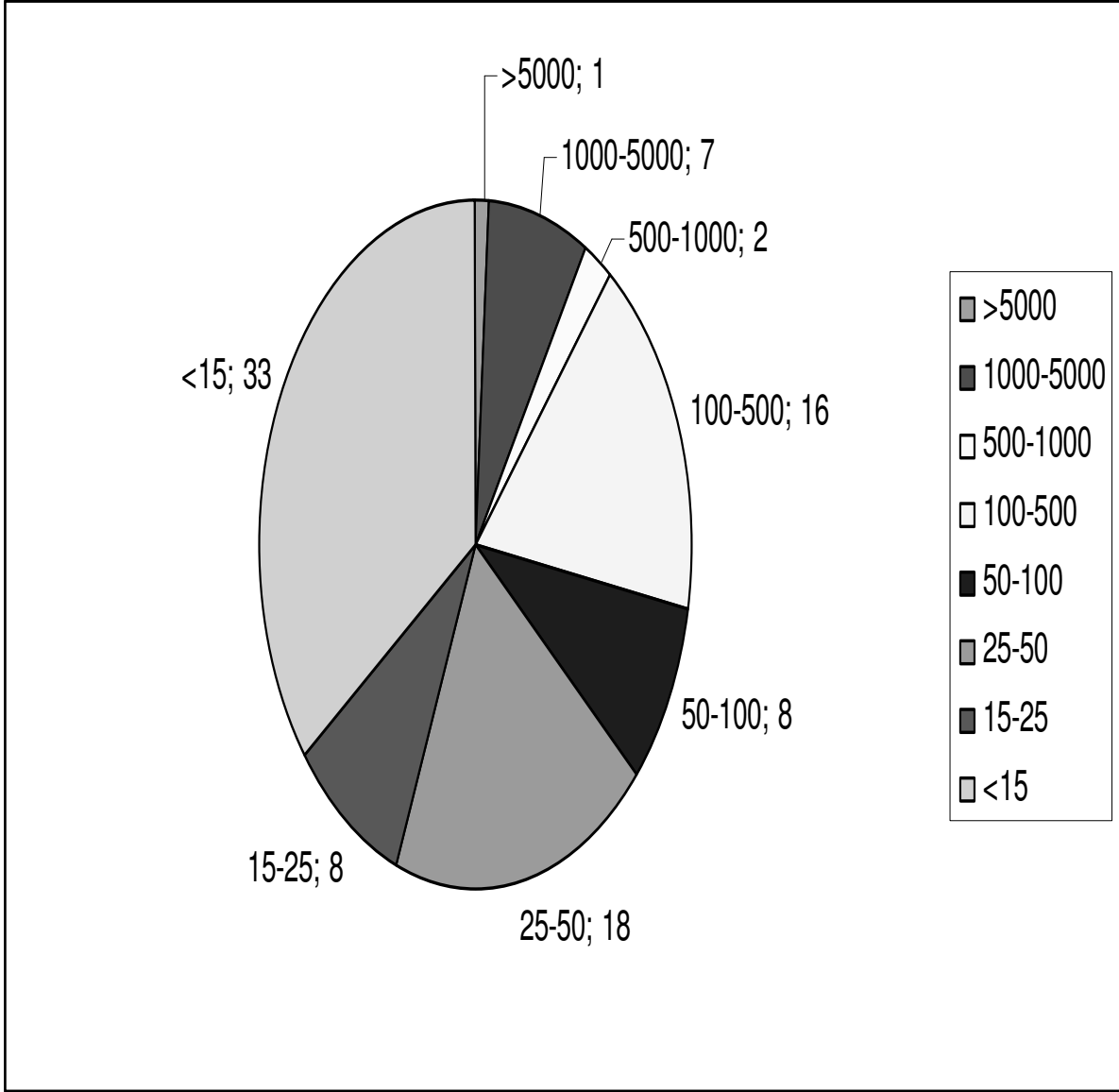
Earnst&Young Birleşme ve Satın Almalar Raporu (2003- 2004- 2005)

Appendix 11- Deal Value by Range, 2004 Turkey (deals with disclosed values, millions USD)



Earnst&Young Birleşme ve Satın Almalar Raporu (2003- 2004- 2005)

Appendix 12- Deal Value by Range, 2005 Turkey (deals with disclosed values, millions USD)



Earnst&Young Birleşme ve Satın Almalar Raporu (2003- 2004- 2005)

Appendix 13- Top Ten Transactions in Volume

ACQUIRER	COUNTRY	TARGET	SECTOR	SHARES ACQUIRED	VALUE (mil.USD)
2003					
Aycell	Turkey	Aria	Telecommunication	--	not disclosed
Nurol-Limak-Ozaltin-Tutsab	Turkey	Tekel Alkollu Icecekler	Food and Drink	100,00%	292,0
Tesco	England	Kipa	Retail	majority	124,0
Calik Enerji	Turkey	Bursagaz	Energy	100,00%	120,0
Yıldız Enerji	Turkey	İgsaş	Chemicals	100,00%	100,5
Deutsche Bank	Germany	BSh Profilo	Durable Goods	13,86%	88,3
Yilyak Yakıt	Turkey	Gemlik Gubre	Chemicals	100,00%	83,1
Danone Groupe	France	DanoneSA	Food and Beverage	50,00%	72,0
BSH Bosch	Germany	BSH Profilo	Durable Goods	11,11%	70,8
Pharmaco	Iceland	Fako İlac	Pharmaceuticals	90,00%	63,0
2004					
Akfen-Dogus-Tüvsüd JV	Turkey	Araç Muayene İstasyonları	Services	100,00%	613,5
Enka	Turkey	İzmir, Adapazarı, Gebze Doğal Gaz Cevrim Santralleri	Energy	60,00%	358,6
OYAK	Turkey	İskenderun Enerji üretim	Energy	49,00%	300,0
BNP Pariba	France	TEB Mali Yatırımlar	Financial Services	50,00%	217,0
Denizciler Atakoy JV	Turkey	Atakoy Grubu Sirketleri	Tourism	65,00%	120,3
Ereğli Demir Çelik	Turkey	Yarımca Porselen Sanayi	Ceramics	100,00%	82,0
Astay Grubu	Turkey	Sultanahmet AŞ	Tourism	100,00%	60,0
Yıldırım Dış Ticaret	Turkey	Eti Krom	Mining	100,00%	58,0
Erkan İnşaat Madencilik	Turkey	Samsun Gubre Sanayi	Chemicals	100,00%	54,1
Inmet Mining	Canada	Çayeli Bakır İşletmeleri	Mining	45,00%	49,3

Earnst&Young Birleşme ve Satın Almalar Raporu (2003- 2004- 2005)

Appendix 13- Continued

ACQUIRER	COUNTRY	TARGET	SECTOR	SHARES ACQUIRED	VALUE (mil.USD)
<u>2005</u>					
Saudi Oger	Saudi Arabia	Turk Telekom	Telecommunication	55,00%	6550,0
Vodafone	England	Telsim	Telecommunication	--	4550,0
Koc-Shell JV	Turkey	Tupras	Energy	51,00%	4140,0
Oyak-Arcelor	Turkey	Erdemir	Steel	49,30%	2960,0
GE Capital	USA	Garanti Bankası	Financial Services	25,50%	1805,0
Alfa Group	Russia	Turkcell	Telecommunication	13,20%	1590,0
Kocbank	Turkey	Yapı ve Kredi Bankası	Financial Services	57,40%	1508,0
Fortis	Belgium	Dısbank	Financial Services	89,30%	1160,0
PSA-Akfen JV	Singapore	TCDD Mersin Limanı	Port Services	--	755,0
Dogan Sirketler Grubu	Turkey	POAŞ	Energy	44,10%	616,0

Earnst&Young Birleşme ve Satın Almalar Raporu (2003- 2004- 2005)

Appendix 14- Mann-Whitney Test Results

NPar Tests

Mann-Whitney Test

Ranks

	sirketin mensei	N	Mean Rank	Sum of Ranks
technofac	Turkish	26	31,62	822,00
	foreign	27	22,56	609,00
	Total	53		
ecofac	Turkish	26	25,27	657,00
	foreign	27	28,67	774,00
	Total	53		
marketrelatedfac	Turkish	26	38,46	1000,00
	foreign	27	15,96	431,00
	Total	53		
financialfact	Turkish	26	35,54	924,00
	foreign	27	18,78	507,00
	Total	53		
crossbordermarextfac	Turkish	26	15,25	396,50
	foreign	27	38,31	1034,50
	Total	53		
HRfac	Turkish	26	26,08	678,00
	foreign	27	27,89	753,00
	Total	53		
strategicfac	Turkish	26	23,73	617,00
	foreign	27	30,15	814,00
	Total	53		
financialfac	Turkish	26	28,63	744,50
	foreign	27	25,43	686,50
	Total	53		
finperfevacriteria	Turkish	26	29,79	774,50
	foreign	27	24,31	656,50
	Total	53		

Test Statistics^a

	technofac	ecofac	marketrel atedfac	financialfact	crossborde rmarextfac	HRfac	strategicfac	financialfac	finperfeva criteria
Mann-Whitney U	231,000	306,000	53,000	129,000	45,500	327,000	266,000	308,500	278,500
Wilcoxon W	609,000	657,000	431,000	507,000	396,500	678,000	617,000	686,500	656,500
Z	-2,160	-,810	-5,407	-4,069	-5,879	-,433	-1,554	-,773	-1,368
Asymp. Sig. (2-tailed)	,031	,418	,000	,000	,000	,665	,120	,440	,171

a. Grouping Variable: sirketin mensei

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