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Billion Dollar Corporate M&A Flops

How to increase shareholder equity?

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Audit / Tax / Advisory

Smart decisions. Lasting value.

How to Ensure Your M&A Increases Shareholder Values

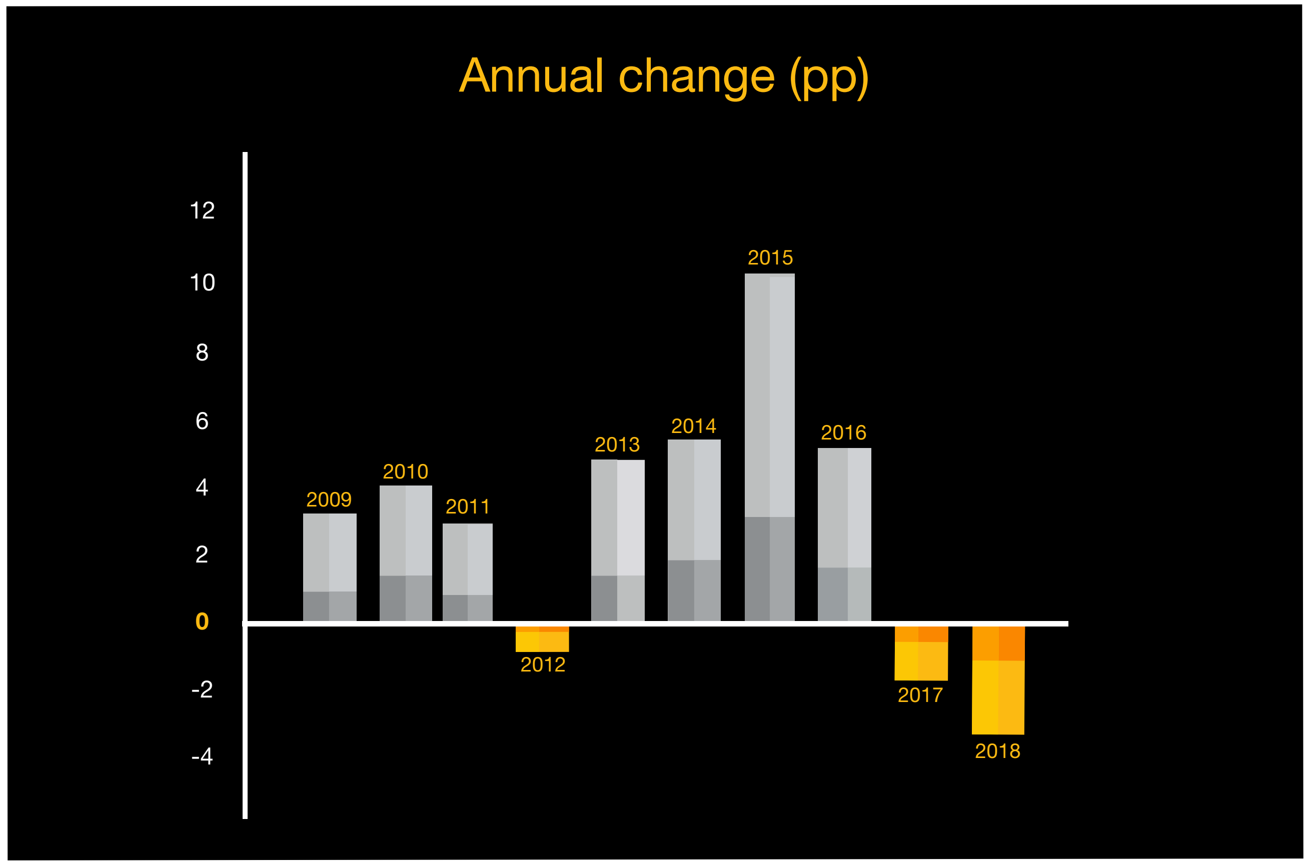
The number and value of mergers and acquisitions (M&As) worldwide have risen year-on-year, and even taking into account increased protectionist policies by governments and weakening economies, deal activities in Asia-Pacific remain robust.

Nonetheless, the increase in M&A volume and deal value has not often resulted in increased shareholder values. And it is not just small unpracticed companies that fail to make deals that meaningfully jolt TSR (total shareholder return).

Even serial dealmakers and public-listed industry giants have made embarrassing missteps in their acquisition sprees -- the most obvious being Microsoft's US$7 billion purchase of Nokia in 2014, which was quickly written down for US$7.6 billion just one year later.[1]

This type of failure is no abnormality. A 2016 analysis of 2,500 deals by LEK Consulting revealed that more than 60% of M&As actually failed to increase TSR.[2] Other studies paint much more dismal figures of between 70% and 90%.[3]

Willis Towers Watson and Cass Business School analysed deals valued at over US$100 million across a 10-year period and found that 2018 saw dealmakers record their worst annual performance, a 3.0 drop in percentage point (pp)-change of share prices, for a decade.



Source: Willis Towers Watson & Cass Business School (2019)[4]

Changes in share prices were recorded from 6 months prior to deal announcements to the end of the quarter it was completed. The study revealed that Asia-Pacific acquirers recorded the worst annual performance of all regions in 2018, with an underperformance of 17.1pp below the regional MSCI Index. Among deal types, mega deals valued at over US$10 billion underperformed the market by 14.5pp.

> Ensuring that an M&A results in higher TSR requires increased focus on due diligence, value creation planning, and scope over scale.

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The emergence of both VC-backed startups as target acquirees and the sovereign funds as direct players in the acquirer space has resulted in many overvalued assets in the M&A space. Timelines for deals may be more rushed now to take advantage of good timing and valuations may be overly optimistic, but due diligence remains a core part of the M&A process to avoid costly mistakes. In 2011, HP bought data analytics firm Autonomy for a whopping US$11.1 billion, a 79% premium over market prices. Within a year, US$8.8 billion of the deal had been written down for a loss when it was discovered that Autonomy had been inflating performance figures. In 2016, HP divested Autonomy.

Closer to home, Top Glove acquired surgical glove manufacturing company Aspion in April 2018 for RM1.2 billion cash plus new Top Glove shares worth RM137 million. Three months later Top Glove sued Aspion's previous controlling shareholder and its directors, Adventa Capital for RM715 million, alleging it defrauded Top Glove by overstating inventories, plant, and machinery amounting to RM74 million and overstating the acquisition price by RM604 million. In the aftermath of the lawsuit announcement, Top Glove's share price plummeted 30%.[5]

Governments have also ramped up protectionist and anti-competition measures, adding to the importance of regulatory due diligence in addition to existing product and tech due diligence. In 2018, Broadcomm's US$144 billion bid for Qualcomm was blocked by US President Trump on national security grounds in March. China then refused to approve Qualcomm's US$44 billion pursuit of Dutch target NXP Semiconductors.[6] The world's biggest smartphone-chip maker needed Chinese regulatory approval due to its presence in the country.

Strategise value creation

In a 2019 study, a Mergermarket study of 600 global senior corporate executives found that only 61% of buyers believe their last acquisition created value. However, acquirers that prioritise value creation from the onset outperformed industry benchmarks by 14% on average 24 months after completion.

Mergermarket found that of acquisitions that lost significant TSR relative to purchase price, 79% didn't have an integration strategy in place at signing, 70% didn't have a synergy plan in place at signing, and 63% didn't have a technology plan in place at signing.[7]

* Logos shown for reference only.

Google's 2005 acquisition of Android turbocharged the little company to become a market-leading operating system. However, Google's plan to build on this to conquer the mobile devices space via its US$12.2 billion purchase of Motorola in 2011 failed primarily because Google continued releasing its own Nexus-branded phones by partnering with Samsung, Asus, and LG. This lack of strategic focus eroded the value of Motorola so badly that in 2014, it was sold to Lenovo for just US$2.9 billion.

Scope over Scale

More companies are looking at "scope" deals rather than "scale" deals, where acquirers essentially buy-out the competition and aim to benefit from economies of scale. Scale plays resulting in eliminating competitors and higher consumer prices inevitably raise alarms with antitrust regulators. Thus, the focus has shifted to "scope" targets where acquirees are in related businesses that can provide buyers access to new markets, channels or product lines.

Businesses are now strategising new competitive 'edges' to innovate. Micron's 2013 purchase of Japanese firm Elpida aimed to add expertise and manufacturing capacity in mobile memory chips. The deal pushed Micron to a 2-year annualized TSR 129 pp higher than the S&P 500.[8]

Fortune favors the brave, but it is vital to avoid being foolhardy as well. Crowe Malaysia's corporate advisory expertise helps ensure M&A clients leave no stone unturned in getting the most shareholder values out of their deals.

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