

***Master of Science
in Innovation and Entrepreneurship
2007/2008***

***ENT 4400:
Innovation Strategy and Management***

4th meeting

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Overview

- 1st meeting: strategic choice – content and process
- 2nd meeting: evaluation of strategic alternatives and criteria for choice
- 3rd meeting: growth alternatives and the M&A process
- 4th meeting: rise and fall of businesses via M&A



Agenda for the 4th meeting

- **Drivers in the M&A process**
 - **Bidding contests and the winner's dilemma**
 - **Internal and external drivers**
- **Strategic management in the M&A process**
 - **Management processes**
 - **Pitfalls**
- **Case 4: "Preparations for an M&A-process in Aker Biomarine ASA"**
- **Recommended reading: Johnson & Scholes (2004): ch. 10-11**
Case example: Intel (pp. 599)

Bidding contests



A market for corporate control is regulated by the following factors:

- The total number of potential acquisition candidates
- The total number of acquirers



“The winner’s dilemma”

- When there are several potential acquirers bidding for a target, the winner is too often the one who has over-estimated the value of the target.
- The purpose of bidding is not to win, but to make a profit.

The top of the slide features five decorative circles in a horizontal row. From left to right, the colors and styles are: a solid light purple circle, a white circle with a light purple outline, a solid light purple circle, a white circle with a light purple outline, and a solid light purple circle.

This raises some intriguing questions:
(1) When does information become opinion?

- When everybody thinks so?
- When the CEO has made her decision?
- When the board has agreed?
- When the advisor says so?
- When it is too late to turn around?

(2) What drives transactions?

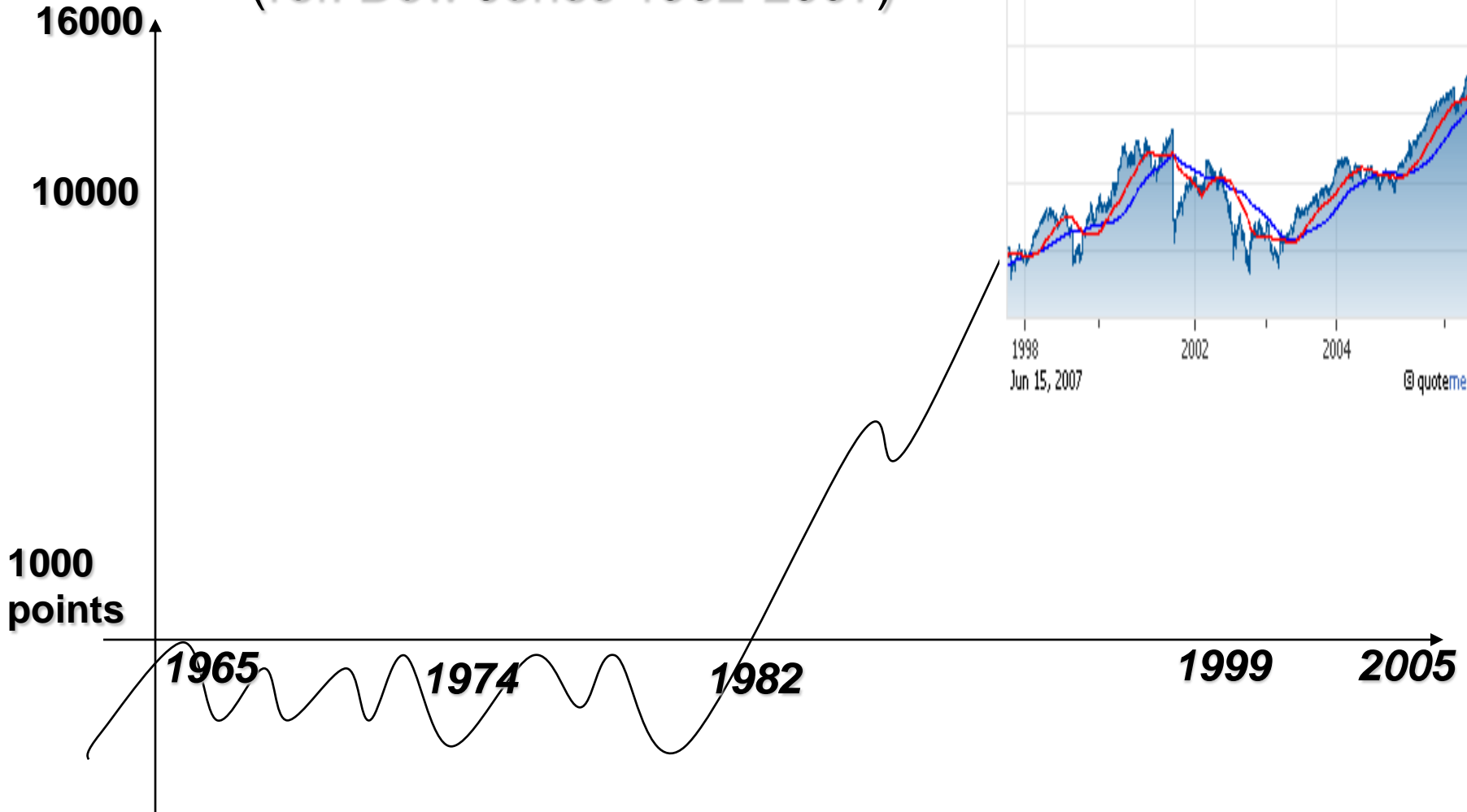


- External factors
 - Economic growth
 - "Bull" market
 - Access to funding
 - Political and financial liberalisation
 - Consolidation in an industry
 - ...and the role played by financial advisors

- Internal factors
 - Total concepts
 - "Control with value chain"
 - "Focus on strategic core"
 - Growth
 - "Time to market"
 - Synergies
 - New technology

(3) When is something expensive?

(ref. Dow Jones 1962-2007)



ENT 4400 4th meeting

Tronn Å. Skjerstad

(4) Who wins – seller or buyer?

Acquisition	Buyer	Seller (target)
Related to strategic core	+5%	+17%
Related, but not to strategic core	0	+24%
Not related	-3%	+26%

Note: buyer typically 5x larger than target

Source: Gretland & Reve (1992)

(4) Post M&A strategic management

- Have objectives been met?
 - typical objectives
 - value creation and synergies
- Turnover and organisational resistance
- Organisation culture



Typical objectives

- Financial results
- Market position and customer satisfaction
- Negotiation power vis á vis suppliers
- Employee satisfaction
- Innovation capability
- Resource and competence development
- Length of cooperation



Profit and synergies

- Since value is based on profit, and since profit is the difference between costs and revenues, the "magic arithmetic" in M&As takes place by:
 - Cost reductions
 - Increased revenues
- But remember
 - Paper synergies \neq actual synergies
 - Synergy is dynamic
 - Synergy as an attitude rather than a financial formula

Watch up for implicit costs

Direct costs are quite easily identified, and are typically called: "*restructuring costs*"

- Compensation packages for laid offs
- Consultancy fees
- Adaptation of IT systems
- Closing of facilities
- Introduction of new brands
- Moving to new locations
- Etc.

Implicit costs (ctd.)



Implicit costs are too often ignored

In the entry phase

- Reduced effort
 - De-motivation
 - Key staff resigns
- Reallocation of effort
 - Queue of internal decisions
 - Lobby activity

In the growth

- Negative economies of scale
 - Longer communication channels
 - Strangled creativity
 - Incentive problems
 - Increased wage costs
- Cost related to complexity
 - Time and attention
 - Sub-optimal compromises
 - Reduced responsibility

Turnover and resistance

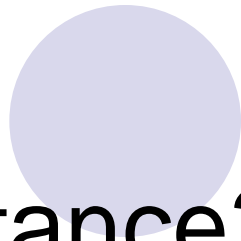
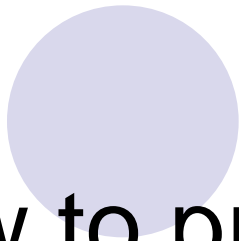


Integration *can* influence management in a negative way:

- Moral, productivity and work satisfaction influenced negatively
- Loss of support from employees in the implementation phase
- Status, own interests and opportunities are threatened
- Frustration of partner's management and leadership style

Management processes

- Who is in charge for M&A in the organisation, what reporting structures are in place, and how are relations to external advisors managed?
- The role of the board of directors
- Action plans and the development of competence and patterns over time



How to prevent turnover and resistance?

- Develop an atmosphere of cooperation and change
- Respect contracts and incentive systems
- Adapt management routines
- Deal with conflicts
- Open up for new career paths



Organisation culture

Practical advice for cultural integration

- Focus on causes and not on symptoms
- Create positive attitudes towards the partner
- Give enough time for cultural integration
- If necessary, use external advisors for the integration

Dangers and pitfalls related to post M&A strategic management

- When strategy and motives are not coordinated
- Management develops “gigantomania”
- Analyses of the establishment process comes too late
- Too impatient
- Lack of attitude for change and innovation
- Can not give away “black box”
- Support from owner to board to management
- Employees’ interests are ignored
- Other market development than assumed
- Changes in ownership

Summary



- Merges and acquisitions seldom create value
- Disposal of targets is more profitable than acquisitions
- Few companies and managers develop patterns
- Be conscious about the role of external, financial advisors

Examples: M&A for growth



1. Transaction overview

Transaction overview

- The shareholders of Voyager Group are currently seeking offers for the component parts of the Voyager Group
- Tiger declined to make a bid for the whole of Voyager Group earlier in the year
- Tiger has been invited to submit a bid for the Business/Provider segments in Norway and/or the residential business – Propose to submit bid for Business/Provider
- Voyager Business Norway is the number 2 player in the market (after Telenor) servicing c.27,800 corporate and public customers
- Voyager Provider Norway offers white label services to around 45 customers who in turn sell on these services to in excess of 46,000 end users
- Voyager has unbundled 324 of Telenor's exchanges in 75 cities and installed a total of 445 DSLAMs, providing coverage of c.63% of Norwegian businesses
- Indicative offers are due on Thursday 11 October

Business & Provider summary financials

Dec y/e (NOKm)	Business		Provider	
	2008E	2009E	2008E	2009E
Mobile	969	1,113	159	161
Fixed voice (incl.VOIP)	574	630	103	105
Internet access	192	204	22	22
Datacom	153	160	101	98
Professional services	77	79		
Total revenue	1,964	2,186	384	385
Mobile	212	242	15	15
Fixed voice (incl.VOIP)	152	177	8	8
Internet access	157	169	15	15
Datacom	100	105	64	61
Professional services	50	51		
Gross margin	621	694	102	98

Breakdown of customers

Business	27,736
Public authorities	38
Municipalities	129
Corporates	27,569
SOHOs/low -end SMEs	25,778
High-end SMEs	1,573
Large corporates	218
Provider	45

Source **Voyager Information memorandum & addendum**

2. Timetable to Indicative Bid

Month		September							October													
Date		24	25	26	27	28	29	30	1	2	3	4	5	6	7	8	9	10	11	12	13	14
Week	Responsibility	W/c 24 September							W/c 1 October							W/c 8 October						
Day		Mon	Tue	Wed	Thu	Fri	Sat	Sun	Mon	Tue	Wed	Thu	Fri	Sat	Sun	Mon	Tue	Wed	Thu	Fri	Sat	Sun
Tiger kickoff meeting	Tiger / NMR (dial-in)			■																		
Provide updated Voyager WACC	Tiger			■																		
Provide first view on synergies for model	SAGA				■																	
Provide comments on inputs to model	SAGA / Tiger				■																	
Tiger Treasury to confirm strategy for funding for IO letter	Tiger					■																
First draft of CMT paper circulated	NMR / Tiger					■																
Circulate draft IO letter highlighted where input required	NMR							■														
First draft of valuation, incl. Business Plan DCF, multiples, benchmarking and synergised case	NMR							■														
Conference call to discuss draft valuation	Tiger / NMR / SAGA									■												
Tiger Legal to confirm anti-trust position and strategy	Tiger									■												
Revised draft of Indicative valuation	NMR										■											
Circulate draft CMT paper to Claus (by close)	Tiger										■											
Circulate second draft of IO letter	NMR											■										
Financial secretary review of valuation?	Tiger												■									
Tax review of loss utilisation and other tax assumptions	Tiger												■									
Final CMT paper circulated to committee members	Tiger												■									
Circulate IO letter to legal, tax and financing teams	NMR														■							
Circulate final draft of IO letter	NMR																		■			
CMT meeting	Tiger																		■			
Submit IO letter by 1700 CET to UBS	Tiger / NMR / SAGA																			■		

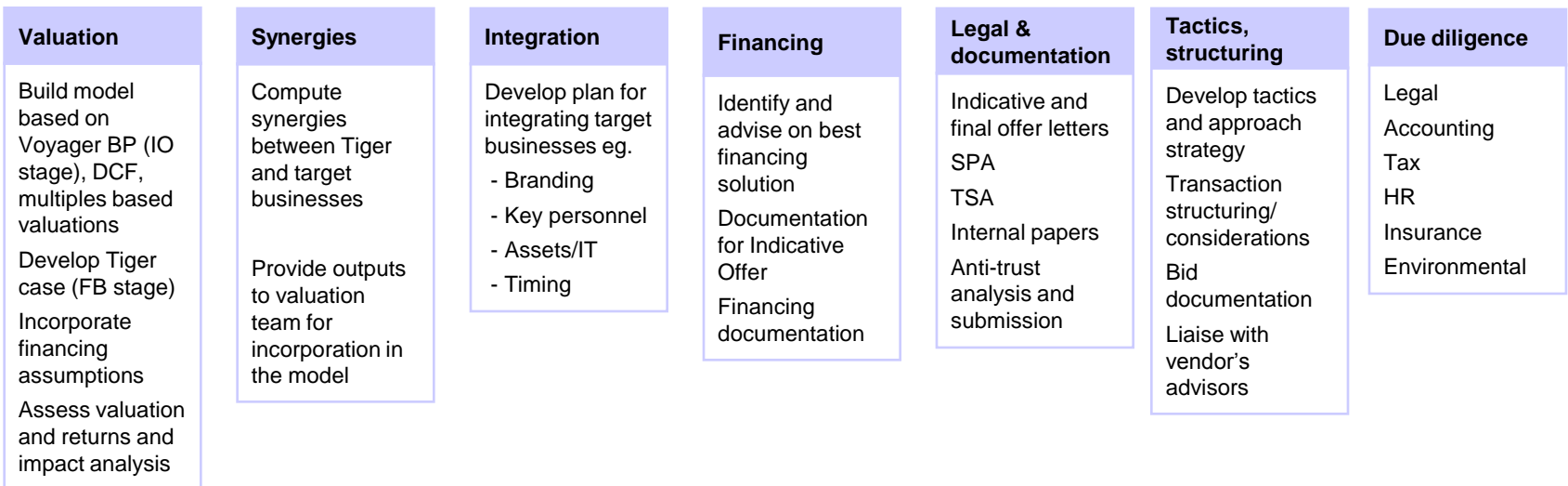
3. Project management

3.1 Key workstreams

Steering group

Key tasks

- Overall direction and ownership of process
- Key strategic decisions
- Final signoff on key documents



3. Project management

3.2 Workstream actions

Area	Responsibility	Deadline
<ul style="list-style-type: none"> ● Valuation <ul style="list-style-type: none"> ▪ Confirm updated WACC analysis ▪ Comments on draft model structure and inputs ▪ Circulate first draft valuation ▪ Conference call to discuss valuation ▪ Circulate revised draft valuation ▪ Conference call to discuss valuation & price for CMT paper 	[Tiger] SAGA, [Tiger] NMR NMR / Tiger / SAGA NMR Tiger / NMR / SAGA	26 Sept 27 Sept 1 Oct 2 Oct 2 Oct 3 Oct
<ul style="list-style-type: none"> ● Synergies <ul style="list-style-type: none"> ▪ Provide synergy data for synergised case 	SAGA	27 Sept
<ul style="list-style-type: none"> ● Financing <ul style="list-style-type: none"> ▪ Confirm funding strategy and documentation for IO letter ▪ Provide documentation for IO letter 	[Tiger] [Tiger]	28 Sept 8 Oct
<ul style="list-style-type: none"> ● Tactics & structure <ul style="list-style-type: none"> ▪ Call UBS for Q2 actuals and 2007 budget ▪ Summary of key target management ▪ Interloper analysis for CMT paper 	NMR SAGA SAGA	26 Sept 28 Sept 28 Sept (am)

3. Project management

3.2 Workstream actions (cont.)

Area	Responsibility	Deadline
● Legal & documentation		
▪ Circulate CMT letter draft1	NMR	28 Sept
▪ Circulate IO letter draft1	NMR	1 Oct
▪ Comments on CMT paper draft1	Tiger / SAGA	2 Oct
▪ Tiger Legal to confirm anti-trust position and strategy	Tiger	2 Oct
▪ Circulate CMT paper draft2 to Claus	Tiger	3 Oct
▪ Comments on IO letter draft1	Tiger / SAGA	3 Oct
▪ Comments back from Claus on CMT draft2	Tiger	4 Oct
▪ Circulate IO letter draft2	NMR	4 Oct
▪ Circulate final CMT paper to Committee	Tiger	5 Oct
▪ Comments back on IO letter draft2	Tiger	5 Oct
▪ Circulate IO letter draft3 to legal, tax, financing	NMR	[8 Oct am]
▪ Legal comments on IO letter draft3	Tiger	[9 Oct]
▪ Tax comments on IO letter draft3	Tiger	[9 Oct]
▪ Circulate IO final draft IO letter draft4	NMR	10 Oct
▪ Submit IO letter to UBS by 1700 CET	Tiger	11 Oct