

The Effect of Mergers & Acquisitions on the Performances of the Companies

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Abstract: In recent years, the importance of mergers and acquisitions transactions has increased nationally and internationally as a result of globalization and developing technology. As a growth strategy, companies prefer mergers and acquisitions transactions because in this way; they have opportunities to combine their powers mutually and keep on taking place in a competitive area. This study aims to investigate which reasons encourage businesses for mergers and acquisitions, failure and success elements, and the process of mergers and acquisitions. In this study, the method used for the case study is Ratio Analysis which provides to compare the information concerning profitability, efficiency, and the financial structure of the companies before and after mergers and acquisitions. Thus, as a result of the financial status acquired after the merger, it can be revealed which factors can affect the performance of the companies. In this research, the merger activity between the companies AKIS Real Estate Investment Trust and SAF Real Estate Investment Trust which are the pioneer company in their sector analyzed using financial tables with ratio analysis. With this analysis method, liquidity rate analysis, leverage ratio analysis, activity rate analysis, and profitability ratio analysis were determined and the performance of the company after merger deals was indicated. Lack of cultural differences between the companies eased the process of combination and affected the performance of the companies positively.

Keywords: Performance, Mergers and Acquisitions, Success, Failure, Ratio Analysis

JEL Classification: P47

1. Introduction

In recent years, It is so fundamental for the companies in the world economy dominated by globalization as they endeavor to continue and keep on the entities in the national and international competition area. With globalization, the companies are searching for new markets and trying to improve new institutional strategies economically and prefer to expand their existence in the markets so that they can compete with other companies nationally and also internationally. The companies can actualize their growth as organic and inorganic that is, with merger and acquisition transactions with other companies.

2. Mergers & Acquisitions

2.1. The Definition of Mergers & Acquisitions

At first sight, although it seems that there is no diversity between the concept of merger and acquisition, there are some differences between them. A merger is the combination of two similar size company. For instance; the merger of DaimlerChrysler consists of two companies named separately Mercedes-Benz and Chrysler. They put on their assets separately to gain more power with the new occurred management, ownership, and organization in the market. On the other hand, with the acquisition, the big company purchases the small company, that is, the big one takes control of the other company. (Snow, 2018 : 12) Despite the slight difference between them, both combinations aim to keep on their existence with growth and creating synergy and to hold on the market in their sector.

2.2. The Types of Merger and Acquisitions

The types of M&A are classified as Horizontal, Vertical, and Conglomerate. A horizontal merger expresses the merged companies operating in the same business and benefits from being the bigger company and thus they acquire a competitive advantage and also have an opportunity to utilize the advantages of economy of scale. (L. Wheelen & Hunger, 2015: 213) Purchasing Reebok, Adidas succeed to merge the first and second shoe producers so this is a significant example of Horizontal mergers. (B.Barney & S.Hesterly, 2015: 281) On the other hand, Vertical merger occurs in two types in itself such as backward which means providing input to the company, and merger is called forward when the merger is carried out with the company to which bought the products. (Ülgen & Mirze, 2018: 324) Backward Vertical M&A provides cost advantages in the supply of raw materials or services to the company, reduces raw material supply and storage costs. (Sarıkamış ,2003 cited by Yücebaş, 2005: 23) Purchasing Skype of eBay is a good example of a backward vertical merger, and the combination of Disney and Capital Cities/ABC can be stated as a good example for the forward vertical merger. (B. Barney & S.Hesterly, 2015: 280–281) The Conglomerate Merger is not like neither vertical nor horizontal merger. It is the cooperation of two or more companies that facilitates in a different sector. It is not significant to merge with the same or similar sectors. (Bedier, 2018: 78) But this sort of combination does not provide the sides profit. So It is not generally preferred. And the companies are not a competitor with each other and there is no relationship between them. (A. Gaughan, 2007: 13) Which type of combination that the companies would choose changes according to some factors that occurred inside or outside the business. It is normal for preferences to differ by country and business. With the mentioned methods, the companies merge with different companies which operate

in the same or similar area to improve the competition conditions, increase productivity and efficiency.

2.3. The Types of Purchasing Methods

In addition to which type of M&A methods would be chosen, how the merger deals would be financed is so significant for the companies, some different payment methods utilized such as by agreement, by one side desire, and leveraged buy-out are the known methods. By agreement is the most friendly method, as the top management of the parties makes negotiations and they decide the most logical and applicable method mutually according to law. (Ülgen & Mirze, 2018: 330) On the contrary, one side method is hostile as the decision-maker is the only buyer. The buyer decides to take over the target company and make plans to finish merger deals without agreement. (Şahin, 2020: 43) Another purchasing method is Leveraged Buyout (LBO), in LBO, the buyer uses an important amount of debt to finance the M&A to obtain the target company. And the entities, shares of the target company, and acquirer companies are used for the guarantee of the debts. (A.Gaughan, 2007: 17) LBO is usually the ratio of 90% debt to 10% capital. LBO aims to give a chance to companies that wish to buy a large-scale target company without so much capital commitment. In terms of an acquirer, the situation should be analyzed in detail and then make a decision which one would be suitable and applicable for the company and take action accordingly.

3. Merger and Acquisitions Historically in the World and Latest Status in Turkey

3.1. Historical Background of M&A

To know the elements which affect the performance of the merged companies is fundamental to inspect the M&A deals in the context of historical perspective. If we examined the history of M&A, the mergers started to gain importance from the second half of the 19th century and they were so substantial for the economic life and at that time the trusts were the major cooperation which were shown as an example for mergers.

The Standard Oil Cooperation was a trust and in 1890 James Buchanan Duke who owned a Tobacco Cooperation and combined with more other four cooperation to be able to form the American Tobacco Company. And later similar trends came into existence in other sectors like cotton and steel. (Bedier, 2018: 44)

According to the reports throughout the history of mergers, it is observed that this phenomenon is revealed in the US commonly which is important for both nationally and internationally. It can be seen that many available resources were restrained concerning to merger. For instance; some limitations concerning specific industries as the mining industry and on transactions with certain values and some other limitations about specific periods. The developments on the merger in the US show us that the mergers arose as waves in periodic times.

It can be clarified that the types of mergers emerged in waves at different times in the world. Mergers operations carried out as waves tend to economic changes, technological improvements and globalization, and the regulations concerning competition. (Mariana, 2012: 390–397)

Although the M&A waves were ended because of economic recessions and economic crises, the starting and ending point of the waves is not certain. The first and the second waves were especially observed in the USA, the other waves were observed in Europe and the other continents of the world. (Goel, A.M. & Thakor, A.V. 2009 cited by Konak & Çıtak, 2018: 194) The M&A waves, which were predicted to begin from 1890, are considered seven waves.

The first Merger Wave which was appeared between the years 1890–1907 after the 1883 depression and most of the mergers consisted of horizontal mergers. (Gönüllü, 2017: 316–317) The structure of the horizontal mergers was close to the monopoly and this causes to occur the big companies which market share increased day by day. About two-thirds of the merger operations consisted of petroleum products, mining, metals, food, and transportation fields in this period. At this period the purpose of the companies is to acquire the market and works as a monopoly to provide synergy and increase the economy of scale. (Scherer and Ross 1990, Gaughan 1994, Shepherd 1990, Kleinert and Klodt 2002, Martin 1994 cited by Sarıca 2008: 53) And then, the second wave started at the time of the First World War and keep on till the collapse of the stock market on the 29th of 1929. (Gönüllü, 2017: 316–324) The companies which monopolized in the previous wave of mergers were regulated and went on to become oligopolies due to the new legal regulations and lack of resources because of the recession. In the third wave, the mergers commonly occurred crosswise which was also known as conglomerate mergers and the companies tended to merge strategies with other unrelated industrial companies to spread their risks. Also, at this period, the companies were subject to strict anti-trust control by the government. (Gönüllü, 2017: 316–324) Between the years

1981–1990, the fourth wave occurred and from the 1980s, the companies began to approach merger strategies positively because of many reasons such as increasing foreign competition, expeditious technological improvements, and increasing Research and Development costs, however, the business offers was made very hostile and unfriendly way and the debt was the most common way in the financing of the mergers. In the fifth wave, M&A transactions were developed not only in America but also in Europe. Through the years 1993–2000, because of the economic welfare in most of the countries in the world and thanks to globalization M&A transactions started to become internationally. The purpose of the companies in this period is to preserve their entities and compete with especially US markets. Whereas; “internet balloon” which started with the new century caused crises on the stock market and the end of the fifth wave began. The sixth wave started with the ‘rebirth’ of the LBO, the widespread use of financial tools and complicated debt transactions, and the World financial crisis cause the sixth wave to end in 2007 and the merger transaction was more complicated. (Bedier,2018: 54) Consequently, the seventh wave starts with the year 2011 and goes on today and in 2011 the negative atmosphere that the 2008 economic crisis caused started to disappear and the positive atmosphere took place of it. The total number of M&A across the world in the first six months in 2014, reached 1.75 trillion USD.

3.2. The Latest Status of Mergers and Acquisitions in Turkey

Besides the historical background of M&A, merger and acquisition transactions has still kept on their importance for the companies because of the diversification and complexification of economic activities today, customer satisfaction, the importance of product and service quality, product life shortened course, increase in competition and globalization of competition, the need to join forces with companies and thus increase their share of the market. Additionally, mergers and acquisition deals provide to expand product diversities, increasing the quality and present the products with reasonable prices. On the other hand, M&A can cause to decrease the effective competition by dominant companies in the market. So, M&A deals that have possibilities to increase the prices, decrease the product variety, and weaken innovation are forbidden with the Protection of Competition Law numbered 4054 by 7. article.

To be able to implement the planned inspection indicated in the 4054 numbered law of the 7th article, all M&A transactions have to be informed to Competition Authority to gain legal validity. In this frame, the situations considered as M&A, and the procedures and the principles were arranged with notification numbered 2010/4 Mergers and

Acquisition Transactions which have to be taken Permission from Competition Authority. (Üstündağ Demir & Pişmaf, 2021: 3)

COVID 19 globally pandemic which appeared in China in January 2019 firstly and then has affected the economy negatively in the whole world including Europe and America which was not seen a similar situation throughout history. COVID 19 primarily affected the aviation, tourism, and service sector, but also the rest of the real sector, including production, along with the entire supply chain, and it was observed that economic activity came to a standstill in many countries with mandatory quarantines. So, it was seen that most of the companies preferred to stop their facilities temporarily or slow down their activities to minimize their costs. As a result of this pandemic situation, the global economy has been in recession inevitably. So, the companies did not prefer to realize their growth plans and consequently, the mergers and acquisition transactions have declined significantly and even come to a standstill. (Kaçmaz , 2021)

The merger and acquisition deals slowed down in the first half period of 2020 because of quarantines, forbidden travels, and canceled or postponed huge contracts. Although, the mobilities regarding the contracts have begun to increase in the second half of the year 2020, ambiguities on global economic situations continue. After a stable year, the activities concerning M&A transactions in 2020 have re-gained trust with increasing transaction volume and number. (Deloitte, 2020: 3)

In 2020, a total of 220 M&A deals were inspected by Competition Authority and on the other hand, in 2019, 208 M&A transactions were inspected. (Üstündağ Demir & Pişmaf, 2021: 6) It is clearly understood that in 2020, the volume and number of M&A transactions started to rise by getting rid of the negative effect of Covid-19.

4. Theoretical Approach to Mergers and Acquisitions

4.1. The Reasons for Merger and Acquisitions

The companies tend to corporate with each other nationally and internationally as a strategic method because of so many reasons. There are so many diverse reasons such as social-economic situation and political that cause corporation of companies and the causes differ from company to company. (Aslan, 2018: 6)

The merger and acquisition transactions are not unplanned processes and deciding to enter into M&A transaction is not a spontaneous decision and some incentives motivate companies to drive them to be involved in such a complicated transaction. Those

incentives are identified by many scholars and professions and the incentives list varies promptly. However, the basic factors to drive companies to decide on M&A can be classified as Macro, Sector, and Company level. (Yrkkö, 2002 cited by Aslan,2018: 8)

Benefiting from the economies of large scale, creating operational and financial synergy, tax efficiencies, increasing the competitive power, financial, exchange and psychological reasons, technological alignment and some managerial purposes are the reasons for M&A. But in the merger, it is not significant which factors are more effective, the only aim is for the companies is to rise the efficiency and effectiveness.

4.2. Failure and Success Elements of Mergers and Acquisitions

Notably, while some companies get success from M&A transactions, others can fail. Significantly, some fundamental reasons cause companies to fail and on the other hand, some factors provide them to be successful. It is indicated by most scholarships that the failure of the success of the firm is determined by the share value of the firm. So, while the rising price of share indicates the positive performance, a downturn on the share implies failure. Accounting and financing parameters which consist of profits, return on investments, share price, return on equity, earning per share, losses, and return on assets are the most common indications of failure of the firms. (Bc.Luis E.Marquez Balderas, 2019: 22) Hubris effect, Overpaying, Integration Process, Management Errors, Psychological Factors, and Cultural Differences are the major reasons for failure.

Conversely, some elements affect the success of the companies regarding M&A, such as Speed of Integration, Leadership, Post-merger Integration Team, Communication, Managing Cultural Differences, and Human Resources Management.

4.3. Process of Merger and Acquisitions

The process of the merger has a substantial role in respect of the companies due to reaching the planned targets. Taking the right steps in this process is so fundamental. Identifying the right target company is directly related to merger deals. At this stage, the financial evaluation of the target company is an important factor for the decision. To compile a target list and make a right evaluation of the target company would affect the success of the company directly. (Şahin,2020: 46-50) Likewise, well-prepared negotiations, preparing the letter of intent, due diligence, and complete M&A transactions and Legal Integration are also so vital steps in the process of M&A. (Snow, 2018: 104)

5. Analysis Methods Used For Effectiveness of Merged Companies Akış REIT and Saf REIT

5.1. The Types of Analysis Methods

The goal of mergers is to have an effective and efficient structure. Today, It is mandatory to be effective and efficient in a competitive market. The effectiveness measurement is generally done in three types; such as Ratio Analysis which means is to ratio one input to one output and to follow the resulting ratio in time and this measurement is frequently used. (Tarkoçin & Gencer, 2007: 20) However, this method is stable in respect of structure, and data obtained represents the performance of the companies periodically. In the Parametrical method; classification is made according to information that what we know about the community we study. In a parametric method, there is a raw of stable parametric that indicates the probability model. (Taylor, 2020) Non-parametric methods have been developed as an alternative to parametric methods. While analyzing with parametric methods, the production function and some suppositions are needed, the nonparametric methods enable to analyze without any suppositions. Therefore, it is easily and easily applicable. In addition, non-parametric have superiority such as such as using multiple descriptive variables. (Şahin, 2020: 111)

Ratio analysis is the most used method that provides to evaluate the general position of the companies and helps to identify the problematic areas in the company and to take precautions accordingly to improve the facilities.

5.2. Analysis of Effectiveness of Akis REIT and Saf REIT with Ratio Analysis

The two major players of the sector operating in the real estate investment partnership sector, in 2016, resulted in the two enterprises merging and continuing their activities in the Akis REIT, comparing the figures of the pre-and post-merger periods. While evaluating the merger performance, only data between 2013 and 2019, 4 periods before the merger, and 3 periods after the merger data were used. The fact that the number of post-merger periods and the number of pre-merger periods are different is that 2020 is an irrational factor due to the Covid-19 pandemic, and therefore the data obtained for 2020 loses its status as "*ceteris paribus*". The data used in the research is taken from independent audit reports containing the annual consolidated tables that enterprises report to KAP.

While the study was carried out, the merger date of the two enterprises was based on 2016, and the pre-and post-season periods were expanded to a degree that would not break the equality and the relevant data were studied. The main method used in the

study is the rate analysis method and evaluations were made on the relationship of different data of the enterprise with each other. Liquidity rates, operating rates, debt ratios, and profitability rates, which are the basic analyses, between the years 2013–2015 before the merger and 2016–2019 after the merger transaction, increases and decreases are evaluated.

6. Conclusion

The merger process of Akis REIT and Saf REIT, which are the prominent companies in their sector, was evaluated using the financial tables between the years 2013–2015 before the merger and 2016–2019 after the merger with the most used analysis method Ratio Analysis. Through this method, liquidity, operating, debt, and profitability rates were measured. For instance; If the debt ratio is considered, Akis REIT preserves the debt ratio curve horizontally before and after the merger and also the earning coefficient of interest has increased by approximately 10%. This indicates that when balance sheets and income statements are examined, the change in interest income expense balance alters in favor of income. The increase in equity profits experienced in the company after the merger adds a positive value to the business. The above evaluations belong to some ratios in respect of ratio analysis, when inspected all ratios, it can be observed that the merger of Akis REIT and Saf REIT results positively and successfully.

As it is stated within the text that Speed of Integration, Leadership, Post-Merger Integration Team, Communication, Managing Cultural Differences and Human Resources Management are the most important factors to complete the M&A transactions and reach the wanted point and obtain success in the end. It can be concluded from this research that efficient communication and especially lack of cultural differences provide Akis REIT to get success in the process of merger transactions and after the merger as it is understood from the ratio analysis method of the financial tables of the firm. Because of being in the same sector of two sides ease to the communication of the top managements of the companies thus the more likely to ease communication, both sides can express their thoughts and wishes mutually in detail and the more successful it is. Because with the right communication, all ambiguities are minimized. Another fundamental factor in the prosperity of merger deals of Akis and Saf REIT is the lack of cultural differences. As it is indicated before that culture has a big influence on organizational health. Culture harmony and the lack of cultural harmony were frequently used to explain the failure of M&A deals. At the same time, some experts found out evidence that the cultural differences cause *“intercultural work alienation “* and *“cultural anxieties “* and accordingly the failure of the companies in M&A transactions would be

inevitable. Additionally, some scholars also indicated that if the parties are willing to get success, building a common cultural understanding is a necessity. Considering these, it can be revealed that the source of an important large scale of the success of Akis and Saf REIT is related to having the same culture. Otherwise, the failure ratio would be high.

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