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Research on Merger and Acquisition Motivation and Methods

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Abstract: *The global economy penetrates into each other, and in order to cope with the competitive pressure from home and abroad and gain a better foothold in the market, large and small enterprises are expanding their market share and enhancing their core competitiveness through various efforts. At present, there are two main ways for enterprises to expand: one is to start from within the enterprise, strengthen enterprise management, improve the utilization rate of resources and equipment, and accelerate enterprise innovation to improve their own competitive advantages; The other is to face the outside of the enterprise, through mergers and acquisitions(M & A) of other enterprises to obtain more resources, to achieve synergistic development, or to carry out diversified operations, open up new markets, in order to enhance the value of the enterprise. The merger and acquisition is the acquisition party's control over the target enterprise through different methods. Mergers and acquisitions may involve multiple parties, usually stronger enterprises acquiring weaker ones. The specific motivations of mergers and acquisitions include four aspects: based on management decision-making, obtaining synergies, reducing transaction costs, and achieving market expansion. There are various ways to classify the types of mergers and acquisitions, and the criteria for division must be determined first, and the classification results of mergers and acquisitions are different depending on the angle selected. By studying different ways of mergers and acquisitions, this paper finds that different ways of mergers and acquisitions will have different effects on enterprises. It is suggested that enterprises should choose different ways of mergers and acquisitions according to different motivations to maximize the benefits of mergers and acquisitions.*

Keywords: *M & A, M & A motivation, M & A method*

1. Introduction

Throughout the world, there have been five large-scale mergers and acquisitions: the first was mainly initiated within the same industry to achieve economies of scale, which occurred in the second half of the 19th century; The second began at the beginning of the 20th century with the aim of achieving the integration of production, supply and marketing, that is, vertical mergers and acquisitions; The third mergers and acquisitions was mainly to diversify into other industries, which occurred in the mid-20th century; The fourth is the mergers and acquisitions characterized by financial leverage that occurred in the 80s of the 20th century; The most recent mergers and acquisitions was accompanied by economic globalization and began in the 90s of the 20th century, and the mergers and acquisitions was mainly a cross-border mergers and acquisitions.

With the continuous introduction of relevant policies, mergers and acquisitions have also become the preferred path for many listed companies to become bigger and stronger. In terms of the choice of mergers and acquisitions, many enterprises choose to achieve their goals through absorption and merger, because this method can better achieve synergies. As for the choice of payment method in the process of mergers and acquisitions, many enterprises tend to use share swaps to achieve mergers. This method is characterized by the exchange of shares between two companies, and no cash or only a small amount of cash is involved in the transaction process, which avoids the future development of the surviving company due to a large amount of cash outflow.

Mergers and acquisitions is usually broadly and narrowly defined according to the scope it covers. In the narrow sense, the scope of mergers and acquisitions is relatively small, and generally only refers to mergers by absorption, that is, the acquirer can obtain the assets, liabilities, owners' equity, etc. of the target enterprise through the transaction, and thereby obtain the control of the target party, and in terms of legal personality, the acquirer continues to retain the legal personality, and the acquired party is

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cancelled. In terms of scope, a broad mergers and acquisitions includes a narrow mergers and acquisitions, and the difference between the two is that after the completion of a mergers and acquisitions in a broad sense, the legal person status of both parties may not be affected.

2. Motivation of enterprise merger and acquisition

2.1 Literature review

According to the research of domestic and foreign scholars on enterprise merger, its motivation can be summarized into four aspects : one is based on management decision-making ; the second is to obtain a synergistic effect ; third, hope to reduce transaction costs ; fourth, achieve market expansion.

2.1.1 Management decision-making

Management may drive mergers and acquisitions between companies for two motivations: one is to enhance corporate value through mergers and acquisitions; the other is to increase personal benefits. Devers (2013) [1] and others are confident in the long-term potential for value creation brought by acquisitions, claiming that mergers and acquisitions are expected to bring synergies and increase long-term value. Haleblian (2009)[2] and others point out that due to the existence of agency problems, the main motivation for management's mergers and acquisitions is to increase their personal interests, rather than to increase the equity of corporate shareholders . Harford (2007)[3] and others found through examining CEO compensation and incentive measures before and after company acquisitions that in the years after the merger, poorly performing company management received significantly more options, and their overall wealth became less sensitive to negative stock performance, but rose in sync with positive stock performance. This makes mergers and acquisitions highly attractive to management, who are willing to increase their own interests through mergers. Seo (2015)[4] and others found in further research that compared to those with lower salaries, CEOs are more inclined to use acquisitions as a means of private gain, trying to adjust their compensation levels in this way. Some scholars also believe that management with greater power is more likely to facilitate mergers and acquisitions. Chikh and Filbien (2011)[5] conducted an in-depth study of merger and acquisition events in French companies between 2000 and 2005, finding that these companies' management often act overly confident due to their high administrative status and substantial actual power. At the same time, the CEO's prestige within the company and in the transaction market greatly increased the likelihood of completing mergers.

2.1.2 Give play to the synergistic effect

Many scholars have provided another explanation for the motives of mergers and acquisitions, believing that the main purpose of the company is to achieve synergy through this operation. Anderson (1959)[6] and others pointed out that synergy is not just about synergy in one aspect, but exists at all levels of the enterprise, including: investment synergy, management synergy, operational synergy, and sales synergy. They believe that synergy should not only benefit the acquiring party but should also be conducive to the enhancement of the value of both acquiring companies. Sirower (1997)[7] pointed out that the main driving factor for enterprises to choose mergers and acquisitions is the expectation of achieving synergy through the acquisition behavior. The synergy brought by mergers and acquisitions can improve the level of the enterprise from all aspects, especially enhancing the core competitiveness of start-up enterprises (Nason and Wiklund, 2018)[8]. Erel (2015)[9] and others evaluated 5187 European acquisition samples that occurred between 2001 and 2008, and the empirical analysis results show that synergy and wealth transfer are crucial to the occurrence of mergers and acquisitions.

2.1.3 Reduce transaction costs

Another motive for mergers and acquisitions is to reduce transaction costs. Due to the differences in industries and products, a company entering a new field will face certain barriers, and mergers and acquisitions can allow companies to enter new markets at a lower cost and quickly. Meyer (2009) [10] and others pointed out that the higher the entry barriers of the target market, the more likely companies are to reduce entry costs through mergers and acquisitions. On the other hand, entering a new market necessarily requires the development of new products, and due to the lack of experience and technology, it is too costly for companies to develop new products on their own. If entering a new market through mergers and acquisitions, one can obtain the resource advantages of the acquired company, saving costs for themselves (Karim, 2006)[11]. Therefore, when a company wants to enter a new field, whether it is to overcome barriers or to save costs, mergers and acquisitions are a good choice.

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2.1.4 Achieve market expansion

The development of economic globalization has promoted the rise of cross-border mergers and acquisitions. Many scholars believe that the motivation for cross-border mergers and acquisitions is to occupy new markets. Dunning (1998)[12] argues that there are multiple motives for cross-border mergers and acquisitions, such as resource seeking and market seeking. Borenstein (1990)[13] also agrees that cross-border mergers and acquisitions can achieve market expansion. Shimizu (2004)[14] found through research that cross-border mergers and acquisitions can help enterprises achieve diversification strategies and are conducive to enterprises directly entering foreign markets.

2.2 Theoretical Foundation

2.2.1 Synergy effect theory

The expansion of enterprises includes both internal construction and external mergers and acquisitions. Unlike internal construction, mergers and acquisitions mainly start from the outside of the enterprise, obtaining new resources and markets by controlling other enterprises, which can help enterprises achieve synergistic effects.

The synergistic effect is a broad concept, which is reflected in three aspects. The first level mainly manifests as the concentration of resources, that is, after the merger, due to the consistency of management, resources can be unifiedly allocated, thus making the operation of the enterprise orderly and optimizing the business processes. For example, after the merger, production and sales can be arranged in the same way, reducing resource waste. The second level mainly manifests as "complementary advantages", and after the merger, the overall improvement can be achieved by absorbing the high-quality resources of both parties and eliminating the poor-quality resources. For example, the complementarity of high-level personnel, high-tech, and advanced production technology between the merging parties. The third level manifests as the reproduction after the absorption of resources, which can enable the enterprise to obtain new competitiveness. For example, after integrating the technologies of both parties, new technologies can be developed for production and manufacturing, thereby improving the competitiveness of the enterprise.

2.2.2 The theory of market power

The theory of market power is closely linked to horizontal mergers and acquisitions. The theory is that in a given market, the larger the size of the firm, the more market share the firm has, and the stronger the overall strength of the firm. On the one hand, mergers and acquisitions can use the resources of the acquirer for its own use, expand the scale of the enterprise, and achieve scale effect, thereby helping the enterprise to obtain more market share; On the other hand, horizontal mergers and acquisitions of enterprises can reduce strong competitors in the same industry, and it is easier for enterprises to monopolize the market and obtain monopoly benefits.

2.2.3 Diversification Theory

Diversification strategies can usually be achieved through two approaches: internal diversification relying on the company's own capabilities and external diversification seeking other resources. Internal diversification is similar to internal new construction, mainly achieved through the development of new products and creation of new processes within the company, that is, the company starts from scratch, relying on its own resources and innovation to enter one or more new fields. External diversification starts from the external market, acquiring the necessary resources such as human, technology, and channels by merging with enterprises within the target industry, thereby becoming a member of the market and realizing diversified operations.

The diversification theory holds that due to the long-term operation and development of enterprises in their original industry, their understanding of the target industry is far less than that of their own industry. If diversification is carried out internally, it is likely to fail due to the mismatch of important resources such as technology and human resources, and the lack of understanding of the external market also makes internal diversification very uncertain and carries potential bankruptcy risks. Conversely, if enterprises choose external mergers and acquisitions, they can directly obtain matching resources, which not only avoids the risks brought by internal diversification but also enables enterprises to integrate into new industries faster and better, smoothly realizing diversification.

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3. Different ways of mergers and acquisitions

3.1 Definition of mergers and acquisitions

There are generally two parties involved in corporate mergers and acquisitions, namely the acquirer and the acquired party. The acquirer realizes the control of the acquired party through different ways, which is called mergers and acquisitions. Mergers and acquisitions may also involve multiple parties, usually strong enterprises to acquire weak enterprises.

3.2 Classification of mergers and acquisitions

According to the industry connection between the two parties, it can be divided into horizontal mergers and acquisitions, vertical mergers and acquisitions and hybrid mergers and acquisitions. Horizontal mergers and acquisitions, generally the two parties are competitors, the product types of the two are similar, and the customer groups faced are basically the same. The advantage of this form of mergers and acquisitions is that through mergers and acquisitions, enterprises can expand their scale, achieve economies of scale, and obtain experience curve benefits. Vertical mergers and acquisitions refers to the fact that the acquirer and the target are in the same industrial chain, that is, the target enterprise to be acquired has a complementary relationship with the acquirer in terms of business, which may be a supplier of raw materials for the acquirer or an agent who helps the acquirer carry out subsequent sales. The advantage of vertical mergers and acquisitions is that if the merger and acquisition is an upstream enterprise, the quality and speed of raw material supply can be guaranteed, and transaction costs can be saved at the same time; If the merger and acquisition is a downstream enterprise, then you can control the sales channel yourself, better achieve sales, and at the same time get closer to the user and understand the specific needs of the user. Hybrid mergers and acquisitions refers to the fact that the acquirer and the target are neither in the same industry nor in the same industrial chain. The main purpose of this type of merger and acquisition is to enter a wider field and diversify its operations.

According to the attitude of the target party, it can be divided into friendly mergers and acquisitions and hostile mergers and acquisitions. Friendly mergers and acquisitions is generally carried out after negotiation, listening to the opinions of the target party, and obtaining the consent of the target party. Usually, the acquirer determines the target through research and analysis, and then discusses with the shareholders and management of the target party before signing the merger agreement, but occasionally the merged party may take the initiative. Different from friendly mergers and acquisitions, hostile mergers and acquisitions has two specific manifestations: one is that the acquirer directly purchases the shares of the target enterprise from the market without the consent of the target party, and the shareholders of the target party have a negative attitude towards this, in this case, the target party is likely to refuse to protect its own interests, so as to take a series of resistance measures against the merger; The other is that the acquirer proposes to acquire the target enterprise but is opposed, but the acquirer acquires the target enterprise despite the wishes of the target enterprise.

According to the identity of the acquirer, it can be divided into industrial capital mergers and acquisitions and financial capital mergers and acquisitions. In the former, a financial enterprise generally buys the shares of the merged party or makes direct investments to gain control of the merged party. The mergers and acquisitions of industrial capital has a strong pertinence and has clear demands on the target company, so the negotiation conditions are relatively harsh. The acquirers of the latter are generally financial institutions, such as venture capital funds, investment banks, etc. Its mergers and acquisitions mainly control the target party by purchasing ownership directly from the target company or acquiring the target company from the secondary market. Compared with industrial capital mergers and acquisitions, financial capital mergers and acquisitions are very speculative, and this kind of mergers and acquisitions are not for the purpose of obtaining business profits, but for the purpose of obtaining profits through the purchase and sale of equity, which requires great risks.

According to the different sources of cash paid for mergers and acquisitions, they can be divided into leveraged buyouts and non-leveraged buyouts. The former has less of its own funds, and the funds used mainly come from outside the enterprise, such as banks or financial institutions. The main feature of a leveraged buyout is that the acquirer does not need to invest a lot of capital to achieve the merger. Generally, self-owned funds account for 10%-15%, loans account for 50%-70%, and bond financing accounts for 20%-40%. Non-leveraged buyouts mainly rely on their own funds to complete the mergers and acquisitions, and their risks are less than those of leveraged buyouts. Similarly, in both a leveraged

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buyout and a non-leveraged buyout, the acquirer pays a certain amount of money to acquire the equity of the target buyer.

According to the payment methods used in mergers and acquisitions, they can be divided into debt-bearing type, cash purchase type and share transaction type. Debt-bearing is a way to gain control over the target company by helping it repay its debts. The disadvantage of this type of merger and acquisition is that the merger and acquisition will consume a large amount of funds of the enterprise, and if the enterprise is not sufficient, it will have an adverse impact on the later operation and make the company enter the business predicament. Share-based mergers and acquisitions mainly achieves control over the target party through the issuance of shares to purchase assets or exchange shares. Contrary to cash purchase, share transaction mergers and acquisitions can save a lot of cash for enterprises and provide a good guarantee for the development of enterprises after mergers and acquisitions.

According to the legal form, it can be divided into absorption merger, new merger and holding merger. After the merger is completed, except for the acquirer, all other parties will be cancelled, and the acquirer will own the assets, liabilities, owners' equity, business personnel, etc. of the target enterprise. A new merger is different from an absorption merger in that after the completion of the merger, both parties to the merger and acquisition will be deregistered, while the newly established enterprise will inherit the various resources of the deregistered enterprise and enjoy independent legal personality. A controlling merger refers to the control of the acquired party by the acquirer through direct investment or the purchase of shares of the acquired party in the secondary market, and both parties continue to enjoy legal personality after the merger.

4. Research conclusion

There are many ways of mergers and acquisitions, and different ways of mergers and acquisitions will have different effects on mergers and acquisitions. Horizontal mergers and acquisitions can achieve economies of scale and gain experience curve benefits. Vertical mergers and acquisitions can save transaction costs and better achieve sales. Leveraged buyouts do not need to invest a lot of money to achieve mergers and acquisitions, non-leveraged buyouts are less risky than leveraged buyouts. Cash-purchasing mergers and acquisitions will consume a large amount of funds of the enterprise, and the later operation will have adverse effects. Share-trading mergers and acquisitions can save a lot of cash for enterprises and provide a good guarantee for the development of enterprises after mergers and acquisitions. Enterprises should choose a suitable mergers and acquisitions method according to different mergers and acquisitions motivations in order to achieve better mergers and acquisitions results.

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