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BASICS OF MERGERS, ACQUISITIONS AND CORPORATE RESTRUCTURING: THE NIGERIAN EXPERIENCE

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ABSTRACT: The paper is primarily concerned with examining the role of mergers and acquisitions (M&As) in corporate restructuring as an instrument of enhancing efficiency, size and developmental roles. The last few years have witnessed an astronomical increase in world of corporate restructuring through M&As. The trend has been influenced by factors such as prospects of cost saving due to economies of scale as well as more efficient allocation of resources; enhanced efficiency in resource allocation and risk reduction arising from improved management at points of allocation and utilization of resources.

M&As especially in the banking industry are now a global phenomenon giving the internationalization of finance. Size has become an important ingredient for success in the globalizing world since no country can afford to operate in isolation in the world of corporate restructuring and finance. M & As is here considered necessary for the smooth operation of the Nigerian economy and eventual general development of all the sectors requiring finance for corporate restructuring. The policy thrust of this paper is on mergers, acquisition, takeover and consolidation for restructuring as the justification strategic issue and regulatory framework.

1. INTRODUCTION

Mergers and acquisitions (M&As) are a global phenomenon, with an estimated 4,000 deals taking place every year. However, they are not a recent development; four periods of high merger activities, also known as merger waves, occurred in the United States (1897–1904, 1916-29, 1965-69 and 1984-89) before the current one that began in the early 1990s. These later waves have attained exceptional levels in terms of sheer value and volume of transactions. In the United States, M&As have been instrumental to the decline in the number of banking organizations – between 1980 and 1997 they decreased from 12,333 to 7,122. Europe has also experienced similar M&As, examples include: Unicredito/Credito Italiano and Generale

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Bank/Fortis in 1998; and Credit Suisse/Winterthur Group and Vereinsbank/Hypobank in 1997. Between 1980 and 1995 the number of banking establishments in Europe fell, particularly in Denmark (-57 percent) and France (-43 percent) (ILO, 2001:3).

In Nigeria, M&As have been taking place in the past, the spate rose only in the recent years of the 21st century as a major strategic option in the Nigerian corporate environment is a response to the economic reform programme of the Federal Government as enunciated in the National Economic Empowerment and Development Strategy (NEEDS). The immediate trigger was the directive given by the Central Bank of Nigeria (CBN) to the banking industry for each bank to increase its shareholder capital to N25 billion by 31 December, 2005. Considering the huge burden of raising such funds from the capital market via public offer and foreign investment by the existing 89 banks, many chose the M&As option.

Proponents of financial sector consolidation argue that institutions need size to spread growing information technology and processing costs over larger revenue bases. Another key factor is the need for greater market capitalization, with governments and financial sector regulators accepting financial operators’ arguments that greater size is crucial to cost-cutting and strong national institutions. Smaller countries are also encouraging consolidation to counter growing competition from larger institutions in neighbouring countries.

2. DEFINITION OF CONCEPTS/TERMS

Brief definitions of the key terms are hereunder given as this would assist in understanding the manner in which they differ:

**Merger:** It could be seen as the fusion of two or more companies into one company usually on equal terms. It involves the combination of all or part of assets, liabilities and the undertaking and business of two or more companies.

**Acquisition:** It is the take-over by one company with sufficient shares in another company to give the acquiring company control
over the target company. It involves the purchase of all or substantial interest in a company by another company such that the acquired company becomes the subsidiary of the acquirer. Acquisition could be either hostile or friendly. An unfriendly acquisition can also be referred to as takeover. A friendly acquisition can be announced as merger but where the purchase is unfriendly, it is an acquisition. Ultimately acquisition tends to be used when a company in general terms absorbs a much smaller one; and merger when companies are of the same size.

Both M&As involve mutual consent of the Board of Directors and eventually, the shareholders. However, there is a school of thought that argues that merger of equals is difficult to come by hence all so-called mergers are regarded as acquisitions. It is based on this reason they are used synonymously.

**Takeover:** Usually involves the unilateral offer by a company (the bidder or offeror) to the shareholders of another company (the target-victim or offeree) to purchase their shares so as to gain control of the target company. Usually, the bidder deals directly with the shareholders by offering them an attractive premium over the companies quoted market prices.

Takeover has been described as unfriendly acquisition because it usually results in total control of the affairs of the takeover/target company affecting both management and staff members.

**Consolidation:** Occurs when two companies lose their separate identities and unite to form a completely new seamless outfit, totally integrated and fused hence corporate restructuring. Other types of corporate restructuring as a result of M&As in companies are; divestitures and spin-offs. The driving force behind divestitures and spin-offs are elimination of non-core businesses and/or to raise cash. A divestiture involves the outright sale of a subsidiary, division, segment or product line of a company. This is usually done because the subsidiary does not fit into the core or future strategy of the combined entity. A divestiture eliminates a non-essential subsidiary and raises cash for the company.
A spin-off occurs when a subsidiary becomes a new legal entity, separated completely from the parent company. Usually, shares in the new entity will be distributed to the shareholders of the parent company on a pro rata basis. In a spin-off, cash is paid to the parent company and the shareholders do not receive any shares in the new entity. The funds received will usually be re-invested in the company.

Types of Mergers
Basically, there are three broad classifications of mergers. These are:

- **Horizontal Merger**: This form of business integration involves the fusion of companies in the same line of business, that is, involving or among competitors. The fusion of two or more insurance companies, two or more banks, two or more publishing companies are examples of horizontal mergers and acquisitions. This type of business integration if not well regulated has the tendency to create monopoly.

- **Vertical Merger**: This is the fusion of companies that are engaged in complementary activities. It involves companies in related industries but operating at different points in the production and distribution process. The acquisition of a paper mill by a publishing company or acquisition of a tyre manufacturing company by an auto company are examples of vertical mergers. The objective is to ensure steady supply of raw materials or create outlet for the products/services.

- **Conglomerates Merger**: This is fusing together of two or more completely unrelated lines of operation. The aim of this sort of integration is for diversification.

Types of Acquisitions

- **Predatory** – Acquisition of competitors to dominate and lead the industry.
- **Defensive** – Acquisition of a competitor to protect against market infringement, technological obsolescence, product obsolescence and legal constraints.
- **Pre-emptive** – Acquisition of competitors trying to acquire the acquirer.
• Premeditated strategic – Acquisition with a well-planned, vision-led, mission-driven purpose aimed at achieving a well-planned strategic objective.

• Idle purposeless – Pursued for its own sake just to be the biggest player competing.

3. PURPOSE OF MERGERS AND ACQUISITIONS

The purpose of a merger is to enjoy synergy. Four types of synergy may be identified:

• **Sale synergy**: Arises from the use of common channels of distribution, sales administration and warehousing facilities.

• **Operating synergy**: Results from higher utilization of existing facilities, personnel and other assets over which overheads can be spread and bulk purchasing can be done, for the merged companies.

• **Investment synergy**: Accrued from the joint utilization of plant, machinery and equipment, common raw materials and sources (if applicable), transfer of research and development benefits and utilization of common tooling for production.

• **Management synergy**: Arises from two merging companies complementing each other’s management depth and breadth and resulting in a well-rounded management team (Drucker, 1984).

Apart from synergy, there are other reasons for mergers.

• The merger candidates are too small on their own to compete effectively with the market leaders; this was the case when A.G. Leventis merged with Leventis Stores Limited, Leventis Motors Limited and Leventis Technical Limited in 1982 and 1990, respectively.

• The merger candidates produce too many style variation of their products relative to the volume of its units cost to remain competitive;

• The merger candidates cannot rely on generating enough sales volume for their distribution network to keep their dealers profitable and strong; and

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- The merger candidates are not generating enough income from the investment due to economic problems such that their stock market values do not reflect their asset values. This was the case of the merger between John Holt Investment Limited (the merger candidate) and John Holt Limited, in 1988.

In addition, Giwa (1989) as cited in Osaze 2006 argues succinctly that five other specific factors may create the need for merger between companies.

- The mutual needs that the merging companies are trying to satisfy which includes a combination of strengths in order to eliminate their individual weaknesses and exploit perceived opportunities. Thus company X might be financially strong with a cash surplus balance deriving from excellent cash generating products and services, but which have limited room for expansion and are experiencing declining future prospects. While company B may have an excellent product/service portfolio with extensive opportunities for expansion but little cash to exploit them. A merger will thus create the necessary balance in the form of available expansion opportunities with excellent products and adequate cash to exploit them for profitable future growth.

- Possible synergies that can be exploited to the advantage of the merging companies may exist especially if they have similar policies and compatible products. This way they will experience few operational frictions in a merger.

- The existence of broad similarities in the market, organizational structure and investment plans of the merging companies. The similarities could also be cultural, human resources and reward systems which would serve as an efficient means of pooling resources to achieve economies of scale, enhance growth deal better with the competition and improve profitability.

- A downturn in economic activities arising from a recession usually leads to low industrial capacity utilization. Idle capacity costs money to maintain and strains cashflow.
Therefore, companies may find it necessary to merge in these circumstances to garner their productive strengths and improve their economic viability.

Mergers also serve as a means of financing growth in an era of cash squeeze, liquidity crisis, high inflation, high and floating interest rates and low rates of return, particularly for companies that are unwilling to introduce new capital into their business. Whenever and wherever exploitable opportunities arise in one company, a merger through share exchange and acquisition of the assets of another creates a larger, more resource-based organization that can profitably exploit these identified opportunities.

Furthermore, in some cases mergers between companies may serve as a cost-effective method of achieving business restructuring as the new organization that emerges becomes leaner, more efficient than both individually.

Above all, some other advantages that companies expect to benefit from M&As include:

- Diversification or integration;
- Improved market share;
- Exploitation of market power;
- Acquisition of managerial skills;
- Streamlining of operation;
- Acquisition of needed technology;
- Economies of scale;
- Potential for value creation; 1+1 = 3 effects.

As a result of these potential benefits, target companies will often agree to be acquired when they know they cannot survive alone.

4. STRATEGIC ISSUES IN THE MERGER PROCESS

According to Giwa (1989) as cited in Osaze (2006) once the factors above have been clearly spelt out and the merging companies are convinced that it would serve better the interests of their individual
shareholders and society at large if they combine forces, then the respective management of both merging companies must clarify the following strategic issues about their merger partners before setting the final legal paper work in motion:

- Obtain details of the history, business and general profile of the company;
- Clearly define its business mission, goals and objectives as well as strategic direction;
- Study and analyze in detail the business portfolio of the company;
- Clearly identify the business opportunity in the company and delineate the cash flows from the question marks, the dogs and the stars;
- Study in detail the competitive strengths and weaknesses of the company as well as its organizational structure;
- Make a forecast of the future of the company, its plans, programmes of action and prospects; and
- Identify and note the company's business, reward system, culture, human resource system, decision support system, business strategies as well as the nature and strengths of its products and services.

This rigorous process is aimed at determining how the potential benefits, costs, risks and sensitivities of the merger will assist in achieving corporate goals and objectives with some other alternative route to the achievement of these goals. If the merger/acquisition route proves better over all then it should be undertaken and the necessary legal framework for its execution set in motion.

In the final analysis, what is of utmost importance in any merger arrangement is the ultimate success of the merger itself, from the planning stage to the execution and integration stages. The success of any merger is thus a function of the extent of commitment of the participants involved to manage human and cultural change in order to preserve organizational value and create the necessary synergy. It is also a function of effective planning and execution of
the merger to ensure a smooth integration. This depends on correct leadership, clear and simple reporting relationship and a deep "understanding of the newly acquired business leading to selective and synergistic changes" (Osaze, 2006).

Finally, the success of a merger also depends on the "linkage of the merger closely with parent strategies and above all ensuring that necessary resources (technology, people and funding) are made available (Munis and Kramer 1989:8 as cited in Osaze 2006). But the most important resource is people.

5. THE NIGERIAN EXPERIENCE

Prior to the recent response to the economic reform programme of the Federal Government of Nigeria as enunciated in the National Economic Empowerment and Development Strategy (NEEDS), and 6 July, 2004, when the Governor of the Central Bank of Nigeria (CBN), Prof. Charles Chukwuma Soludo announced far reaching reforms of the banking industry, the trend in the history of corporate marriage in Nigeria is that most had been at the convenience of the foreign shareholders, i.e. consequential mergers.

This explains why take-over bid had not been a common occurrence in the Nigerian capital market. In view of the fact that the bloc-holdings of between 40 percent and 60 percent of most quoted companies are in the hands of foreign shareholders, merger/acquisition transactions in Nigeria had taken place with little or no problem. The current global trend of increasing incidence of mergers/acquisitions is being imbied in Nigeria as witnessed in the banking industry and now in the insurance industry. Experience so far indicates that adequate guidance is critical for smooth conclusion of arrangements.

Most M&As in Nigeria have typically been undertaken under the following scenarios:

1. Where a major shareholder of a company seeks to acquire a controlling equity stake in the company e.g. SBIC Africa Holdings Limited's acquisition of a 48.9% equity stake in Stanbic Merchant Bank Nigeria Limited in addition to the 40% already held.
2. Acquisition of the shareholding of federal and state governments in companies via privatisation programme e.g. the acquisition by Scancem International ANS of 40% shareholding in Cement Company of Northern Nigeria Plc.

3. Merger of companies in which one of the companies is a shareholder in the other e.g. the merger of Agip Nigeria Plc and Unipetrol Nigeria Plc (now Oando Plc).

4. Merger of companies that have common principal shareholders e.g. the merger of Nichemtex Industries Plc with United Nigerian Textiles Plc.

5. The new Total Nigeria Limited was created through two successive mergers, the first when the former Total joined with Belgian oil company Petrofina to form TotalFina in 1999, and the second when TotalFina combined with French oil company Elf Aquitaine in 2000 to create TotalFinaElf. On May 6, 2003, the group adopted the new name of Total. The new company reflects the prestigious Franco-Belgian oil and gas heritage that dates back to the 1920s. The dynamic synthesis of the corporate cultures and expertise of three companies represents a wealth of technological and human capabilities that positions Total favourably to operate in the future of energy. Hence most merger activities before now in Nigeria have been transnational mergers for example (Exxon-Mobil and Chevron-Texaco).

6. **REGULATION AND MERGERS/ACQUISITIONS IN NIGERIA**

A merger is a legal transaction and must be effected in compliance with the provisions of the law. The Companies and Allied Matters Act 1990 and The Investment and Securities Act 1999 provide the primary legal framework for effecting M&As in Nigeria. All mergers, acquisitions or combinations between or among companies (both private and public) are subject to the prior review and approval of the Securities & Exchange Commission ("SEC") and The Nigerian Stock Exchange ("The NSE"), where at least one of the companies involved is quoted. Before granting its approval, SEC considers the
effect of the proposed deal on the competitive environment, with a view to ensuring that the deal does not restrain competition or create a monopoly.

- Legal and regulatory framework

The main legal framework for the regulation of mergers, acquisitions and takeovers in Nigeria for both public and private companies is vested in the Investment and Securities Act, 1999, Section 8(0), 99 to 102. Section 8(0) of the ISA 1999 empowers the Securities and Exchange Commission (SEC) “to review, approve and regulate mergers, acquisitions and all forms of business combinations”. Specifically, Section 99(2) provides that “Notwithstanding anything to the contrary contained in any other enactment, every merger, acquisition or business combination between or among companies shall be subject to the prior review and approval of the Commission.

To guide against mergers and acquisitions likely to cause monopoly, Section 99(3) contain anti-trust provisions stating that:

- Such acquisition, whether directly or indirectly, of the whole or any part of the equity or other capital or of the whole or any part of the assets of another company, is not likely to cause a substantial restraint of competition or tend to create a monopoly in any line of business enterprise; or
- The use of such share by voting or granting of proxies or otherwise shall not cause a substantial restraint of competition or tend to create a monopoly in any line of business enterprise.

In view of this section, the Commission is expected to give due consideration to the issue of public interest. If a merger, acquisition or take-over for example, is detrimental to public interest on the premise that it is likely to either cause a substantial restraint on competition or tend to create a monopoly in any line of business enterprise; the Commission can under Section 99(3) and (b) of the Investment and Securities Act 1999 disapprove or prevent the proposal.
Exemptions

Although the provisions of the ISA 1999 on “Mergers, Takeovers and Acquisitions” are all embracing, the Act granted some exemptions. Section 99 subsections 3 and 4 state that:

- “Nothing is this section shall apply to holding companies acquiring shares solely for the purpose of investment and not using same by voting or otherwise to cause or attempt to cause a substantial restraint of competition or tend to create a monopoly in any line of business enterprise”.
- “Nothing in this section shall apply to transactions duly consummated pursuant to the authority given by any Federal Government owned agency under any statutory provision vesting such power in the agency”.

The exemption granted under Section 99(4) of the ISA 1999 is to remove from the purview of SEC, institutions created and given monopolistic power by government to perform specific functions. Such federal agencies include Power Holding Company of Nigeria Plc (PHCN) and Nigerian Telecommunications Plc (NITEL).

Section 100(1)-(6) stipulates the manner in which merger/acquisition transactions are to be executed which includes:

- Summoning of separate meetings of the companies as the court may direct on receipt of application of merger. Sections 100(1).
- Agreement by majority representing not less than 75 percent of share members present to enable scheme qualify for Commission’s consideration. Section 100(2).
- Court to sanction scheme giving specific orders after approval of the scheme by SEC, Section 100(3).
- Delivering of Certified True Company (CTC) sanction order to SEC for registration (within seven days after the making of the order) and a notice of the order published in at least one national newspaper.
Other enactments

Other legislations that had provisions for regulation of merger, acquisition and takeover are:
- Companies and Allied Matters Decree 1990;
- Bank and Other Financial Institutions (BOFID) Act No. 25 of 1991;

7. CONCLUSION

For the uninitiated and those wishing to stay abreast of emerging issues of mergers, acquisitions, takeover and corporate restructuring, that Nigeria is still relatively inexperienced with the aforementioned concepts compared to some advanced economies. The sudden escalation of M&As activities in recent years is therefore interesting.

For almost all M&As deals in Nigeria are effected on a share exchange basis although they also provide a “cash-out” option for those who do not want to buy share. Therefore, as shareholder it is of particular important you cast your vote at the court-ordered meeting. And this paper would create some degree of enlightenment.

REFERENCES


Appendix
Banks that Emerged at the end of December 2005

1. Access Bank
2. Africbank
3. Diamond Bank
4. EcoBank
5. Equatorial Trust Bank
6. First City Monument Bank
7. Fidelity Bank
8. First Bank Plc.
9. First Inland Bank
10. Guaranty Trust Bank
11. IBTC-Chartered Bank
12. Intercontinental Bank
13. Nigeria International Bank
14. Oceanic Bank
15. Bank PHB
16. Skye Bank
17. Spring Bank
18. Stanbic Bank
19. Standard Chartered Bank
20. United Bank of Africa
21. Sterling Bank
22. Union Bank
23. Unit Bank
24. Wema Bank