

TABLE OF CONTENTS

An Analysis of the Causes Behind the
Business Combination Frenzy,
1979-1986

A Thesis
Presented to
the Chancellor's Scholars Council
of Pembroke State University

In Partial Fulfillment
of the Requirements for Completion of
the Chancellor's Scholars Program

by
Jerome T. Upton
April 24, 1986

Introduction	i
Historical Perspective	1
The Current Merger Wave	9
The Motives Behind the Current Wave	12
The Raiders	27
Discussion of the Takeover Process	29
Significant Cases	30
Conclusion	37

INTRODUCTION

For the past eight years, the American economy has experienced an increase in both the number and size of mergers in business. The magnitude and far-reaching effects of this phenomenon merit a serious study.

The first question that comes to one's mind is "Has this phenomenon occurred previously in a magnitude anywhere similar to that of the current wave?" If it has, then there is the possibility that one could determine what factors are specifically favorable to its occurrence.

The economic conditions should be examined both in their general perspective as well as the way in which they translate into motives for specific companies to be involved in mergers and acquisitions if this answer is to be complete. This will lead to a general survey of the economy during those periods in which large numbers of mergers occurred. Additionally, it will study actual companies to determine what factors motivated them to merge.

In the interest of brevity, it is not possible to study each case exhaustively, but a short description of a few classic examples ought to be included.

Therefore, the paper will follow this format:

- An historical perspective of the phenomenon
- A general analysis of economic conditions favoring mergers
- An in-depth examination of the specific motives behind actual cases
- A brief review of the takeover process
- A sketch of three of the most notorious merger cases

After completing the study, conclusions will be drawn and a prognosis of the phenomenon will be given. At this point it appears that capitalism itself, in association with certain economic conditions, promotes the merger movement. However, it is only possible to determine this accurately by proceeding with the study.

One further point must be made. The terms merger, acquisition, takeover, or combination are used throughout the paper to represent any type of business combination. In their technical context, these terms have different meanings:

merger- a combination of two or more business enterprises into a single enterprise.

acquisition- the purchase of the assets of a business.

takeover- the act of seizing control of a business entity through the purchase of its stock.

combination- the combining of two or more business firms.

However, business journalists use them interchangeably.

HISTORICAL PERSPECTIVE

Although mergers and acquisitions have occurred throughout the history of American business, there have been three distinct periods in which this activity was especially notable. The first period dates from 1895 to 1904, and has been labeled "Merging for Monopoly."¹ The second merger wave occurred between 1920 and 1929 and has been called "Merging for Oligopoly."² The third merger wave, which took place in the 1960s (1960-1970), is described as "Conglomerate Merging."³ While each period was unique, there were certain factors common to all three. A bullish stock market, significant breakthroughs in technology, and a stronger economy have been common to all three periods. In addition, there are some environmental factors present in the current wave that are similar to past waves. Thus, a review of merger history will provide a foundation upon which a clearer understanding of the current period can be gotten.

The First Merger Period

While the first period of "merger mania" dates from 1895, it actually began with the recovery of the economy after the panic and recession of 1893. The business environment rapidly improved and the stock market became bullish as investment became a national obsession. In addition, the development of the railroad had transformed local markets into a national market. David C. Whitten writes in his book, The Emergence of Giant Enterprise, 1860-1914, about the effects of the railroad on the business environment,

"The local markets of the pre-Civil War United States were suddenly thrown open for national competition..."⁴ Where companies were once limited to regional markets because a means to transport their goods quickly and efficiently was not available, the development of the railroad gave them a way to market throughout much of the country.

With the opening of the national market, competition flourished. Companies took advantage of the larger national market by increasing production; and with the increased output, came the development of production techniques that were more efficient.⁵ As a result, overcapacity occurred.

To survive in this severely competitive atmosphere, businesses merged horizontally (i.e., to merge with businesses that produce the same products).⁶ This type of combination served two purposes. First, by combining with a competitor, competition could be eliminated or lessened (revenues could increase). Secondly, economies of scale could be attained because of the increased production capacity of the merged firms. With the elimination of some competition and the attainment of economies of scale (and thus the lowering of production cost), businesses were able to exert some monopolistic power over markets. The increased power and efficiency of these merged businesses caused the remaining smaller firms to either merge with the larger business or fold.⁷

John D. Rockefeller embodied this phenomenon in his creation of Standard Oil. He began by combining two oil refineries and from that point on he pursued the market until he controlled 90% of it in the United States.⁸ Before Rockefeller's pursuit of an empire, the competition had been so intense that the price of oil had dropped over 50%.⁹ He realized that by acquiring firms, there would

be the elimination of some competition and an increase in profits through economies of scale. As Standard grew larger and production efficiencies increased, he used his new power in the refinery industry to create a near-monopoly. According to Ida Tarbell, Rockefeller spoke to his competitors in this manner: "You can't compete with Standard. We have all the large refineries now. If you refuse to sell, it will end in your being crushed."¹⁰ His approach worked. In Standard's "heyday" Rockefeller made this statement:

Three years ago, I took over the Cleveland refineries. I have managed them so that today I pay a profit to nobody. I do my own buying, I make my own acid and barrels, I control the New York terminals of both the Erie and Central roads, and ship such quantities that the railroads give me better rates than they do any other shipper.¹¹

The first wave ended around 1904, when the economy experienced a recession and the government began to use the Sherman Act effectively in the prosecution of monopolies.¹² Many mergers of this period failed as the economy soured. Also contributing to the failure of these mergers was the lack of managerial skills and techniques to effectively run the larger business.

The Second Merger Wave

The next and smallest of the merger waves occurred from 1920 to 1929. Economic conditions were similar to the previous merger period in that the economy was rapidly improving and the stock market very bullish. The wave was preceded by the development of the automobile and the radio. This created new industries and re-

quired larger facilities for mass production.¹³ In addition, with the ending of WWI, many industries were overproducing and therefore very competitive. In response to the business environment, businesses used merging as a way to survive through growth. In some instances, it was necessary for firms to combine in order to compete against the larger firms created during the first merger period.¹⁴

The first two waves differed in some respects. When the first period ended, the federal government increased its involvement in the elimination or prevention of monopolies. With the increased enforcement of the Sherman Act, and the passing of the Clayton Act in 1914, larger businesses found it more difficult to combine. Therefore, in this period, merging took place between the smaller firms in an industry; there was also an increasing movement to integrate vertically (the combining with a supplier of resources).¹⁵

Responding to the development of the communication industry (which was aided by WWI), Sosthenes Behn created ITT. He did this by acquiring smaller firms in both the U.S. and abroad with the intent of creating an "International System." Behn saw the potential of connecting the U.S. with foreign countries, and therefore pushed ITT into this niche marketing strategy. To move quickly toward this strategy, Sosthenes Behn adopted an aggressive acquisition policy, as Table 1 confirms.¹⁶

ITT
(figures are in millions)

	<u>1926</u>	<u>1929</u>
Consolidated Revenue	22.7	100
Earnings	7.1	17.7
Assets	131	535
Debt	9	64
Common Stock	.5	1.95

This type of corporate growth was not the result of internal growth, it came about only through a progressive acquisition program. In Behn's plan he not only expanded geographically, but also acquired businesses that manufactured communication equipment (vertical integration). Behn's strategy was typical of the period.

The second merger wave ended abruptly with the crash of the stock market in 1929. Firms that had been pursuing aggressive growth strategies found themselves in financial trouble--many even folded. This was a trying time for ITT as it fought for its life.

The Third Merger Wave

Occurring in the 1960s and peaking in 1969 was the third and largest merger wave. Reinforcing the merger activity of this period was a strong economy, and thus a bullish stock market. Also, the further development of the airplane and television had created new markets as the automobile and radio did prior to the second wave.¹⁷ Firms moving into these new industries were required to adjust--this often meant expansion of facilities. In general, the economy was very similar to the previous merger periods. However, the type of merger that was common in the 1960s was much different than those of the earlier periods; the government was largely responsible for this. After the second merger wave, the government amended the Clayton Act to provide it even greater control over combinations. Basically, the Clayton Act prohibited the acquisition of stock or assets when the result would be the lessening of competition or the creation of a monopoly.¹⁸ But not only did the government have more power to deal with mergers, but it also was more active during this period in the enforcement of antitrust laws. This made it

difficult for businesses to combine either vertically or horizontally; the response to the government's increases power and enforcement was the acquisition of unrelated businesses (conglomerate merging). The federal government was not prepared to deal with this.

Also pushing the conglomerate movement was the realization of the risk that results from the production of only one product. The end of WWII was harsh on firms that produced only for the government. With the ending of the war and the drastic cut in defense spending, military suppliers found themselves on the verge of folding. From this came the move to product diversification to offset the fluctuating business cycle (and therefore the reduction of risk). This is thought to have been the primary motive behind the conglomerate movement of the 1960s.¹⁹

Occurring at the same time were two questionable motives for growth. First, the merger movement appeared to be a business fad. Growth seemed good since in the mind of the public "a growing company was a healthy one." Secondly, accounting procedures did not effectively cover the merger. Financial statements were easily manipulated to make the newly merged firm appear healthier than it actually was.²⁰ The early 1970s destroyed these illogical combinations.

The aggressive acquisition strategy of ITT during this period, under the direction of Harold Geneen, was typical of the 1960s mergers. In the late sixties, ITT acquired firms at the rate of one per week.²¹ When defending his acquisition strategy, Geneen said that he acquired to balance: the domestic and foreign markets, the capital intensive and labor intensive products, consumer goods and capital equipment.²² Diversification was the obvious motive

here, but certainly not the only one. When Geneen became the CEO of ITT, he promised to double earnings in five years. He did; and he did it through acquisition. Robert Sobel, in his book, ITT: The Management of Opportunity, writes, "The conglomerateurs were more concerned with finance than with the development of ongoing enterprises; they were more interested in the bottom line than in supporting extensive, long-term research and development programs."²³ But Geneen was not only obsessed with diversification and the bottom line, but he was also psychologically involved with his acquisitions, as was his predecessor Sosthenes Behn. Robert Sobel notes, "Geneen wanted recognition from Wall Street in addition to what he already had from the financial and business press..."²⁴ The association of power, control, and satisfaction are prevalent.

The third merger period ended with a downturn of the economy, as had the previous periods. The huge conglomerates that had been created during this period suffered in the recession of the early 1970s. Surprisingly, ITT did well in the early seventies due to the remarkable talents of Harold Geneen.

The review of merger and acquisition history showed that the phenomenon was a reaction by firms as an attempt to adopt to a changing business environment. Mergers have been consistently associated with a strong economy and a strong stock market. In a strong economy growth is both possible and desirable. One way, and perhaps at times, the only way that growth can be effectively achieved is through merger or acquisition. In addition, changes in the structure of the economy have been linked to each merger wave. Malcolm S.

Salter and Wolf A. Weinhold, noted merger researchers, write, "Many mergers accompanied or were stimulated by massive changes in the economy infrastructure. Typically, these radical changes in the economy lead to new market definitions and/or new production and distribution technologies."²⁵ The first merger wave followed rapid rail building and dramatic improvement in efficiency. This opened new distribution channels. Preceding the second period was the development and widespread marketing of the automobile and radio, which created new demand and required mass production. Before the wave of the 1960s, television and the airplane appeared as integral parts of the American business fabric, and served to create new industries and markets. To take advantage of these market possibilities, mergers/acquisitions were a logical approach.

Competitive advantage surfaced repeatedly as a force behind the movement. During the first merger period, businesses sought economies of scale. This allowed production cost to fall and enabled the firm to underprice competitors. The second period was marked by firms integrating vertically, but largely for the same reason as that of the first wave; businesses were again hoping for economies of scale. Firms were convinced that they could become more efficient by gaining control over their resource suppliers. The mergers of the 1960s were a response to the business cycle and the desire to reduce risk. Firms felt that they could outdistance their competitors by diversifying into unrelated businesses that countered the business cycle; this allowed more consistent earnings.

The review of merger history has led to the discovery of four factors that fostered the activity. They are listed below:

1. A strong economy
2. A strong/bullish stock market
3. A change in market definition
4. A competitive advantage

Even though these factors were prominent in the past three waves, some of them will be rediscovered as the current merger wave is discussed.

THE CURRENT MERGER WAVE

The late seventies (1978-1979) marks the beginning of the current merger and acquisition wave. At this time, the American economy experienced a great deal of instability due to the inflated price of goods and services. As a result of inflation, the stock market was undervalued; investors perceived a great deal of risk in the market. In addition, foreign competitors had become more efficient in operation and had begun to push American firms out of the international market. In fact, not only did foreign firms drive Americans out of the foreign market, they also invaded the American market. Thus, the influx of foreign goods, accompanied by the already competitive American market, made for an overproduced market and one in need of serious restructuring.

It would seem that one of the primary factors starting the current movement has been the deflated valuation of the stock market. At the beginning of this merger wave, stock prices were grossly undervalued. "In the late 1970s corporate America's equities were being valued relative to their productive capacity at only 50% of the rate they were in the early to mid-1960s."²⁶ Businesses with excess cash at this time and who were also trying to grow, could find no better way to do it than through merger or

acquisition. Even with the bullish market of 1985, Carl C. Icahn said, "The cheapest place to buy planes is on the floor of the New York Stock Exchange."²⁷ The undervaluation of the stock market has provided businesses with a cheaper means of growth.

Not only did the stock market entice American businesses to combine, but the increased efficiency and prominence of foreign firms has also been a contributing factor. "As the merger wave began to swell in 1978 and 1979, American firms were rapidly losing market share to foreign competitors in steel, automobiles, electronics, computers, and other products."²⁸ As a response to foreign competitors and the saturated American market, American firms began to acquire. Malcolm S. Salter and Wolf A. Weinhold in their book, Merger Trends and Prospects for the 1980s, write, "The acquisitive behavior of U.S. corporations during the 1970s was also reinforced by the large scale entry of foreign firms into the American market."²⁹ This factor is still prominent. The recent GE and RCA merger were specifically linked to the enormous competition of foreign firms in the technological industries.

With the Reagan administration came a different attitude toward mergers and acquisitions. The president has adopted a laissez-faire approach to business in general. In 1986 it was said that, "President Reagan is preparing to propose sweeping changes in anti-trust laws to ease restrictions on corporate mergers, especially in industries hobbled by overseas competition."³⁰ Even though this statement was made in the mid-1980s, with the coming of President Reagan and his "big business" approach, companies had to feel more at-ease in their attempts to acquire.³¹ In response to this idea,

many may argue that, although President Reagan has adopted a "loose" approach to mergers, there is an increasing amount of legislation taking place regarding the merger phenomenon. However, a review of current literature makes it obvious that the proposed legislation is not likely to be passed. In 1985, there were 50 bills introduced regarding mergers and acquisitions, but none of these bills made it out of committee.³²

Also contributing to the "urge-to-merge" has been the deregulation of many industries. Regulation of industries protects firms from competition as price controls are set for all competitors. With deregulation, price control protection is eliminated and firms are forced to compete vigorously. The result has been another era of overproduction. The oil, financial, airline, and trucking industries are examples of this. "Deregulation in the finance and oil industries helped to promote mergers..., but it had a more variable effect in the transportation sector."³³

In addition, there have been changes in the definition of markets. The rapid development of technology has created new markets and altered others.³⁴ Businesses see mergers as a way to purchase the needed technology. Also, the change in consumer demographics has created and altered markets. Individuals that are over 60 years of age are increasing in number; they are demanding products that are specifically made for them. Here again, the way businesses have adapted to and explored these markets has often been through the acquisition of another business.

Mention also has to be made of the increasing size of mergers and acquisitions. In the current wave, especially when it began, only the larger of more successful firms had the resources to in-

vest in a takeover/merger. In addition, whereas these more successful companies would once have grown in the international market, this market is not as favorable as it was in years past. Notice in Table 2 the increased number of mergers taking place whose value is in excess of \$100 million.³⁵

TABLE 2

<u>\$100 Million Mergers</u>	
1975	15
1977	41
1978	80
1982	116
1984	200

Thus, six factors in particular are obvious in the current wave: the undervalued stock market, the increased foreign competition, the philosophies of the Reagan administration, the deregulation of some industries, the changes in some markets, and the increased size of mergers.

THE MOTIVES BEHIND THE CURRENT WAVE

The first five factors, which are listed above, have created a business environment especially conducive to mergers. And underlying these mergers and acquisitions (with the exception of those prompted by raiders) is the desire to survive through growth. Don Gussow in his book, The New Merger Game, writes, "The management of these companies knows that the best way to grow aggressively and substantially is through a sound merger and acquisition program."³⁶ The acquiring or merging with another business is the fast-

est way to grow. Exxon's purchase of Reliance Electric is an example. Exxon had developed a revolutionary motor but had no means of refining or producing it. To satisfy their need for growth in this area, they purchased Reliance Electric to further develop, refine, and produce the motor.³⁷ It would have taken years to build a plant and make it operational for this purpose.

Acquisition is, at times, the cheapest method of growth. Many corporate stocks are undervalued in relation to their assets; this is exactly what the raiders have noticed. For this reason, obtaining control of the firm through the purchase of stock is economically ideal. In 1984 there was a substantial amount of consolidation in the oil industry. This occurred primarily due to the undervalued stock of many oil firms; it was simply cheaper to grow through merger.

Consideration must also be given to the fact that growth through acquisition appears to be much safer. The acquired firm is already operational and usually has established a market share. When growing internally, one not only has to organize his assets and make them operational, but he also has to compete for a share of the market. This is a difficult and risky task. Procter and Gamble's acquisition of Richardson-Vicks, for example, was not only less expensive than would have been the development of the products, but was also not as risky.³⁸ Richardson-Vicks, with two proven products, "NyQuil" and "Oil of Olay", already had a command of the market. P&G would not have to develop, produce, and then compete for a market share. There is less risk involved.

Finally, in addition to growth being cheaper, faster, and a safer means of expansion, it is also fashionable. The public regards growth and success as interchangeable terms. And growth through

merger or acquisition is certainly given to the public by the press.

The general motive behind the current merger movement therefore is growth-- growth in order to survive. Within this general classification, however, there are certain more specific goals:

1. The achieving of stability during cyclical change
2. The obtaining of economies of scale
3. The increase of distribution channels
4. The acquisition of an expert manager or management team
5. The establishment of a new corporate direction
6. The acquisition of a firm as a response to competitors actions
7. The acquisition of tax advantages
8. The acquisition of technology

Somewhat related to these goals are two that result from them, namely, defense against merging, and the personal psychological goals of those involved in the process.

To illustrate the combined list of often goals, particular cases will be used. In some instances the same case may be used more than once since, in fact, merging frequently is far more complex than a single goal can explain.

The Achieving of Stability During Cyclical Change

Frequently regarded as the primary motive for growth is the desire to achieve stability during cyclical swings of the economy. Firms often accomplish this goal by acquiring firms that produce goods or services that are negatively correlated with the purchasing businesses' goods or services. For example, the acquired firm's product may be more profitable as the economy recedes, while the acquiring firm's product will become stronger as the economy strengthens. Table 3 on page 15 will aid in the discussion.³⁹ Notice first

that Conglomerate, Inc., and Positive Correlation, Inc. are positively correlated and therefore their returns increase or decrease together as the economy strengthens or recedes. Also, notice Negative Correlation, Inc.; this firm's product is more profitable in exactly the opposite periods (measuring against Conglomerate and Positive, Inc.). Columns four and five simulate the merger of Conglomerate and Positive, Inc., and also the merger of Conglomerate and Negative, Inc. The consistent rate of return in column five depicts the desire to achieve stability during cyclical change.

TABLE 3

Yr.	Congl. Inc.	+ Corr. Inc.	- Corr. Inc.	Congl.& + Corr.	Congl.& - Corr.
1	14%	16%	10%	15%	12%
2	10	12	16	11	13
3	8	10	18	9	13
4	12	14	14	13	13
5	<u>16</u>	<u>18</u>	<u>12</u>	<u>17</u>	<u>14</u>
Mean	14%	14%	14%	13%	13%
Deviation	2.82	2.82	2.82	2.82	.63

This is the theory of diversification: to reduce the risk associated with the business cycle. The move is logical since a study of history shows that the business cycle is becoming more volatile. "... the 1970s was a period of increasing economic uncertainty and instability. The business cycles became both more volatile and more erratic in their occurrence..."⁴⁰ A business that has invested its resources in only one area could be in trouble as the business cycle runs its course.

An example of this involves Edward L. Hennessy's (CEO of Allied Corp.) acquisition strategy. Business Week noted, "In the process,

he built a company with 4.3 billion in net sales into a 10.5 billion giant resting on five major diversified business lines, adding automotive, aerospace, and an assortment of industrial, electronics, and health products to balance out the company's cyclical chemicals and volatile oil and gas businesses"⁴¹

In addition, lenders often perceive diversified firms as a safer investment and therefore offer lower interest rates to them. However, with this type of growth it is often difficult to manage. Tremendous managerial skills are needed.

The Obtaining of Economies of Scale

The classical theory of economies of scale has certainly influenced the current wave. With the influx of cheaper foreign goods into the American market, American firms are looking to gain economies of scale. With increased size, more units are produced and spread over the same fixed cost. "Economies of scale are the natural goal of horizontal mergers. But such economies have been claimed in conglomerate mergers too. The architects of these mergers have pointed to the economies that come from sharing central services such as office management and accounting, financial control, executive development and top-level management."⁴² Tables 4A and 4B demonstrate economies of scale.

TABLE 4A

Cost of Goods Manufactured		Income Statement (per unit)	
Sales price (unit)	\$10.00	Revenue	\$10.00
Units produced	1,000	Variable cost	<u>\$6.00</u>
Variable cost (unit)	\$6.00	Contribution margin	\$4.00
Operating expense	\$2,000	Operating exp. (2000/1000)	<u>\$2.00</u>
		Operating profit	\$2.00

TABLE 4B

Cost of Goods Manufactured		Income Statement (per unit)	
Sales price (unit)	\$10.00	Revenue	\$10.00
Units produced	2,000	Variable cost	<u>\$6.00</u>
Variable cost (unit)	\$6.00	Contribution margin	\$4.00
Operating expense	\$2,000	Operating exp. (2000/2000)	<u>\$1.00</u>
		Operating profit	\$3.00

Notice that the only variable in the table is the units produced. As production increases from 1,000 to 2,000 units, the operating expenses per unit decreases and thus allows more profit. This theory was used when St. Louis-San Francisco Railway merged into Burlington Northern. The railways were consolidated, the payroll was cut by 15,000, and the ratio of operating expenses to revenue dropped from .88 to .82; the industry average was .90.⁴³ But the reduction of operating expenses is not the only factor behind the theory; often marketing efficiencies can be obtained. "Marketing efficiencies are frequently at the core of strategic acquisition programs. Acquisition of products that use the same distribution channels can benefit from great savings in sales and promotion staffs."⁴⁴

In addition, as firms grow through acquisition and increase their size, "synergy" occurs. Synergy refers to the fact that two firms working together as one can accomplish more than the firms could achieve as individual entities. This is evident in the hopes expressed by the CEO of LTV, Raymond A. Hay, regarding LTV's merge with Republic Steel. "...the combined resources of the two companies will create a stronger steel operation than either party can accomplish as a stand-alone company."⁴⁵ This term is used in almost

every merger and can be the deciding factor in the decision to merge.

The Increase of Distribution Channels

As a firm expands its market coverage from regional to national, or national to international, distribution channels must be obtained. What better way to obtain distribution channels and move into new geographical markets than through merger or acquisition. PepsiCo's purchase of Seven-Up, for example, not only increased its product mix, but it also provided new distribution centers in different geographical areas.⁴⁶ PepsiCo, given the success of its new product "Slice", appears to be acquiring distribution channels to market this new product.

In Stroh's purchase of Schlitz in 1981, Stroh was not only trying to gain economies of scale, but was also trying to push its product nationally. "Buying Schlitz gave Stroh's immediate access to a national distribution network."⁴⁷ Again, with the merger of American Stores into Skaggs (a drug store chain) reveals the goal of moving into new markets. The merger blended American Stores grocery business with Skaggs drug expertise; the Jewel (a subsidiary of Skaggs) acquisition expanded American Stores geographically.⁴⁸

The Acquisition of an Expert Manager or Management Team

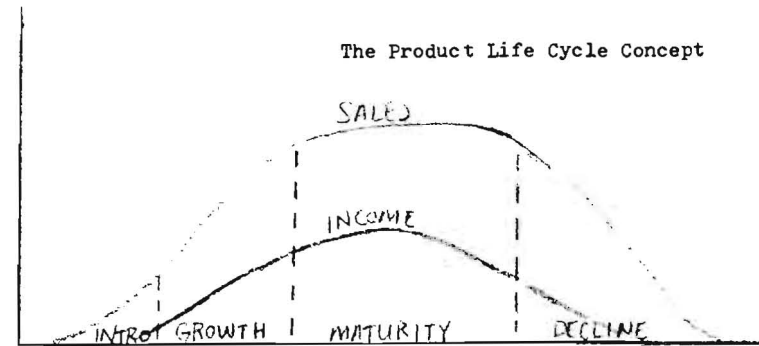
The complex business environment has made the managing of a business both difficult and demanding. Top management is required to work 12 to 15 hours per day and make crucial decisions "on the spot." A proven manager may be hard to find and a good manage-

ment team is considered a rarity. The market is "wide open" for proven managers. The management of a targeted firm, and its ability to produce, can be a deciding factor in the decision to merge. In the case of the Burlington Northern merge, not only did the firm pursue St. Louis-San Francisco Railway to gain economies of scale, but it was also after the CEO of the targeted firm. Immediately after the acquisition, Burlington Northern placed the acquired firm's CEO into its top position.⁴⁹ Another example is the purchase of Ginos by Roy Rogers. As Roy Rogers was trying to grow quickly through acquisition, it realized the need to purchase good management to reduce the risk of this quick expansion policy. It would have taken a significant amount of time to develop managers in its own program. In the acquisition of Ginos, Roy Rogers not only acquired additional geographical coverage, but it also got an established and experienced management team.

The Establishment of a New Corporate Direction

Eventually, a firm's products or services may become obsolete. This is an unavoidable part of the product life cycle concept (refer to Figure 1).⁷⁸ The figure simply shows the stages that a product passes through in its life. Especially important is the income curve; note that income begins to decline in the maturity stage of the product's life. A firm must begin its search for new products long before the actual decline of the products demand. To survive, a firm must look for opportunities to shift corporate direction toward other growth areas. As a firm's product or service moves into and then past the maturity phase, the firm must

FIGURE 1



pursue alternative markets. This is often accomplished through merger or acquisition. "Given the near history of the last recession, there is a realization in many industries that they have to find niches in their traditional businesses or move into new ones."⁵⁰ A good example of this is the tobacco industry. With the increased promotion of the harmful effects of tobacco and the enormous lawsuits that already have been filed, the industry foresees the possibility of a drastic decline in tobacco consumption. This explains R.J. Reynolds acquisition of Nabisco.⁵¹ And while R.J.R. was acquiring Nabisco, Philip Morris found its partner in General Foods.⁵² Both Nabisco and General Foods were growing firms which made them an excellent choice for firms in a declining industry.

The Acquisition of a Firm as a Response to Competitors Actions

A well-planned merger can aid a firm in its search for a

competitive advantage. However, in some industries firms merge not to obtain a competitive advantage, but to keep up with its competitors. In the early 1980s, with the merge of Shearson Lehman and American Express, the financial industry began to feel pressure to merge. Soon after the announcement of the merger, Phibro-Salomon (Salomon Brothers) began to actively search for a partner. This phenomenon is also prominent in the banking industry. With the deregulation of the industry, and with the mergers that have resulted, banking executives feel pushed to merge. Edward E. Crutchfield of First Union Corporation states, "People say: Why don't you go slow?" He then continues, "You don't go slow because your competitors who are acquiring franchises in other states won't let you go slow. They are not making any more of these franchises. There are only a limited number of good banks available to acquire."⁵³ Crutchfield is attempting to keep up with his competitors. In fact, First Union is competing with competitors for acquisitions.

There is often competition between businesses for a targeted firm. CEOs often feel compelled to acquire a firm to prevent a competitor from doing so. This activity has been seen in the banking and oil industries, but the airline industry provides the best example with Sonic Air. Writing about the chairman of Sonic Air, Ray Thurston, Fortune said, "Thurston admits that he himself laid the groundwork for trouble, at first by rushing the merger." Then he explains his situation, "if the other suitors had managed to pull the sale out from under him, it would have been only a matter of time before the combined clout of the newly merged companies would have weakened Sonic's position in West Coast markets."⁵⁴ There had already been substantial acquisitions in the airline industry, and Thurston realized that he needed to make a move to re-

gain his position in the industry.

The Acquisition of Tax Advantages

"Often the buyer looks at the target company's net operating losses as an 'asset', because it will use those losses to offset some of its own taxable profits."⁵⁵ Not only are tax losses often looked for by an acquiring firm, but capital intensive firms are also often targeted because of substantial tax credits and deductions. Baldwin, once the piano manufacturing giant, has now moved into the financial industry. Vice president of Baldwin, R.S. Harrison, says, "...Baldwin is committed not so much to particular businesses as to increasing shareholder wealth through two paramount tactics: acquiring cash at low or no cost and avoiding or deferring income taxes."⁵⁶ Almost all of Baldwin's acquisitions have resulted in favorable tax consequences. Baldwin owns insurance companies, savings and loan companies, and mortgage banking and service companies. These companies are very profitable but they generate very few tax deductions (investment credit, depreciation, etc.). To offset these profits that are not shielded, Baldwin had moved into the business of leasing. In this capital intensive business, a substantial amount of investment credits are generated (a direct reduction of taxes payable resulting from the purchase of specified equipment). Also, there are huge deductions for depreciation which acts to shield revenue.

Another example of the desire to gain favorable tax consequences through acquisition is Ryder's pursuit of Frank B. Hall and Company (an insurance brokerage firm). Ryder, a truck rental company, attempted to takeover Hall and Company while at the same time Hall

and Co. was pursuing Jartran (truck rental company). "Both firms recognize that a truck rental company is a capital intensive business which generates investment tax credits and that an insurance brokerage firm is a service business which generates significant 'non-sheltered' income."⁵⁷ Obviously, the two firms would complement each other nicely.

Accounting procedures can also affect taxes. There are two methods of accounting for the purchase of a firm: Pooling and Purchasing. The pooling method is used only when the targeted company is purchased with at least 90% of the acquiring firms common stock.⁵⁸ The procedures that accompany this method are simply the adding of categories on the balance sheet together, resulting in consolidated statements. This type of "merger structure" is tax free. On the other hand, the purchase method requires the revaluation of assets and usually results in the write-up of assets; this means more depreciation for the acquiring firm.⁵⁹ The purchase method is the most commonly used and is the method that most acquiring firms want to use due to the resulting favorable tax consequences.

The Acquisition of Technology

Technology is another serious phenomenon. It is expanding at a record pace. Firms often develop a product, and perfect it, only to find it obsolete due to technological developments in the interim. Firms that are laggards in its industry (technologically) find that the only way to catch up with competitors is through the purchase of technology. Kenneth Davidson in his book, Mega-Mergers, writes about technology, "To keep up or catch up, firms have turned to

merger transactions."⁶⁰ Burroughs, under the direction of Michael Blumenthal, had to adopt an aggressive acquisition plan to catch up with its competitors. For this reason, Burroughs purchased Memorex to close the gap between itself, IBM, and NCR. Burroughs, once at the top of the market in office automation, lost its market share due to poor research and development program. The company could not keep pace with technology by internally improving itself.

In another case, General Motors acquired two technologically-oriented firms. Again, it was an attempt to close a technological gap (GM versus Japan). In 1984, GM bought Electronic Data Systems because of its knowledge of management systems. In this area GM felt that it must improve. In 1985, GM purchased Hughes Aircraft. General Motors wanted to obtain technological advantages from Hughes. "The world's largest automaker hopes to use the skills of its two new units to move into special areas of technology, especially with the Saturn Project, which aims to build a small car that can compete with Japanese models."⁶¹ Research and development was simply too slow a process to close the gap created by the Japanese.

General Electric's acquisition of RCA was also motivated by the need for technology. GE chairman, John Welch, said, "We will have the technological capabilities, financial resources, and global scope to be able to compete successfully with anyone, anywhere, in every market we serve."⁶²

Defense Against Merging

With mergers increasing throughout the 1980s, there has been a rise in the number of defensive combinations. There are many firms

who have been targeted for takeover but wish to remain independent. Many tactics are used by businesses to thwart a takeover attempt; one of the most common moves is to acquire another firm. This not only increases the size of the targeted firm and makes a takeover more expensive, but it often leverages (the use of debt) the firm in such a manner that would make a takeover suicidal. In addition, and as a last resort, a targeted firm may find a willing acquirer that would be more favorable than the pursuing business. This has been labeled by the business community as a "white knight."

Western Airlines is a company that may find itself using the defensive merger tactic. The company is ripe for a takeover in that its stock is undervalued and it is cash heavy.⁶³ American Airlines has already approached Western in hopes of initiating "merger talk." However, Western Airlines wishes to remain independent and is prepared to take the appropriate measures to insure this. Through acquisition, Western would first be using the excess cash that is enticing many airline companies. But more important, a merger would increase the size of the company and make a takeover prohibitively expensive.

A firm can also find a willing acquirer (white knight) to prevent an unfavorable business from acquiring it. This tactic has been used by Gulf in its avoidance of T. Boone Pickens. Pickens, it was reported, was going to liquidate the company and distribute the funds to shareholders.⁶⁴ Management at Gulf felt this would be unfair to shareholders and therefore searched and found a white knight in Chevron (Standard Oil of California). Two additional examples are provided under the heading "Significant Cases."

1. Conoco and DuPont
2. Bendix and Allied

The Personal Psychological Goals of Those Involved in the Process

Kenneth M. Davidson in his book, Mega-Mergers, states, "There exists a suspicion that large corporate acquisitions are undertaken to satisfy the imperial aspirations of chief executive officers (CEOs)."⁶⁵ Large firms are powerful and are viewed by the public as successful. The CEOs of these firms receive the credit for success and the power associated with the larger business. It is tempting to acquire. John D. Rockefeller's thirst for power was noted earlier, as well as that of Sosthenes Behn and his dream of an International System; Harold Geneen, Behn's successor, wanted status on Wall Street. Currently, Hasbro's acquisition of Milton Bradley is said to involve the power motive. It is said of Hasbro's chairman, "Hassenfeld, 42, has long wanted to be king of the hill in toys."⁶⁶ Additionally, it is said of Hassenfeld, "Winning Milton Bradley takes Hasbro closer to Hassenfeld's goal of becoming the top U.S. toy company."⁶⁷

Also searching for power through acquisition is takeover artist Rupert Murdoch. Murdoch is acquiring businesses in the communications industry in hopes of covering most all of the world markets; presently, the takeover specialist is pursuing Warner Communication. Tom O'Hanlon, writing for Forbes, states,

By the time Rupert Murdoch retires to his Australian farm in the 21st century, his current vulgar image will have faded, and he will be regarded as a sage who followed opportunity where it led and put together a global empire in what may be the 21st century's greatest industry, communication. 68

In addition to the psychological aspects of power and success, there is the "sport of acquisition." In a study done by Wayne Boucher on the CEOs role in a merger, one panel member states, "Nothing is more fun than an acquisition as an escape from the

boredom of day-to-day business. The urge to merge is to break from the routine, to deal with high rollers, to find challenges, to make quick tough decisions."⁶⁹ One gets the feeling that the merger is treated much like a game, and the ultimate goal is to acquire simply for the sport of it. Corporate raiders certainly are in this category, although their movements are usually more economically motivated. T. Boone Pickens, Carl C. Icahn, Irwin Jacobs, Ted Turner, and Sam Zell are noted for enjoying their business. These individuals are raiders. Patricia Gray writes in The Wall Street Journal, regarding raider Sam Zell, "For Mr. Zell, money long ago stopped being the lure. These days, he stalks companies for the sport of it."⁷⁰ Mr. Zell says, "If it ain't fun, don't do it."⁷¹ Sam Zell, through his Chicago-based holding company, Equity Financial and Management Corporation, has taken over ITEL Corporation, Great American Management and Investment Inc., and has acquired a sizeable number of apartment complexes and office parks.

THE RAIDERS

Riding the coattails of the current merger wave have been individuals that have come to be called "corporate raiders." A corporate raider is an individual, usually operating as CEO of a firm, who watches companies on the market for deflated stock prices relative to the firms corporate assets. When they find an undervalued company, these individuals attempt to gain control of the company through the purchase of its stock. In addition, raiders often look for excess cash or overfunded pension plans. "Especially inviting are companies whose excess cash could catch a raider's

eye."⁷² A cash heavy company, or a company with an overfunded pension plan makes the takeover cheaper. The raiders simply use the excess assets of the targeted company to finance part of the takeover itself. ITT has been under siege because of its cash position. The conglomerate has been divesting its unprofitable subsidiaries (acquired in the late 1960s) and has a great deal of cash on hand.⁷³ In addition, its stock is considered to be grossly undervalued. Several raiders are "eyeing" ITT.

A common phenomenon in the raider game is the "greenmail" tactic. A raider will buy a percentage of the shares of the targeted firm (a threatening percentage), only to have the company buy the shares back. This is often exactly what the raider wants. T. Boone Pickens has made several "fortunes" in this manner. In his bid for Unocal, he was greenmailed. Gulf also used this tactic, and then found a white knight to prevent Pickens from another attempt.

An interesting sideline to the greenmail tactic is the cyclical nature that it can produce. Disney Corporation is an example. Corporate raider, Saul P. Steinberg, acquired a percentage of the Disney stock; Disney felt the percentage to be threatening to the independence of the firm. They saw no alternative other than to buy the raider's stock. A sizeable premium was paid to Steinberg. As Steinberg was acquiring the Disney stock, the price of it was going up. Speculators wanted to get in on the takeover action because of the huge sums that could be made by selling their shares at a premium. However, when Disney bought Steinberg's shares, the stock bottomed out. Investors not only knew that a takeover had been prevented, but that Disney was now in worse financial condi-

tion because of the greenmail. Disney's shares were again undervalued, so Irwin Jacobs, another raider, begins to buy shares of Disney and appears to be preparing for a takeover attempt. What can Disney do? If they use the greenmail tactic again, will it not only decrease its value on the stock market and thus invite another raider?

This type of activity has caused many companies to rewrite its corporate bylaws disallowing the greenmail tactic.⁷⁴

DISCUSSION OF THE TAKEOVER PROCESS

A means in which to effectuate a merger is the "takeover process." This method, which is often used by both the firm in a pursuit of growth to survive, and the raider, is effective because it involves using the stock market to obtain control of a targeted company; through the stock market, enough of a firm's shares may be purchased so that control can be achieved, and then a merger can be forced.

This technique is appealing for two reasons. First, the stock market has been undervalued throughout the current wave. Purchase or merger through the stock market is economically rational. Second, the takeover process does not require the interaction of the acquirer and management of the targeted firm. Takeovers allow the dealing to take place between the acquirer and the shareholders of the target.

As an example, suppose that firm "A" wants to obtain control of firm "B". B has created an important technological process, which A hopes to acquire, yet its stock is undervalued. To gain

control of B, A could approach B's management with the offer of a merger agreement, or A might consider buying the assets of B; however, it is more likely that a cheaper price would be possible through a takeover. If using the takeover process, firm A would then buy as much stock as it could on the open market at the undervalued price (up to 10%). When A has 10% of B's shares, then A must file with the FTC a statement regarding its intentions (investment or takeover). Subsequent to the filing of this notice, A would then make a "tender offer" to the shareholders of B for a specified price per share, and a specified percentage wanted. (the acquiring firm hopes to entice the targeted shareholders to sell their shares). The tender offer price will be above the market price and the percentage wanted will push the firm close to 51%. (with 51% of a firm's shares control is established). At this point, B may either allow the takeover and then the merger, or it can use defensive measures in an attempt to prevent the takeover. If B adopts a defensive posture, then a war may follow as A looks for ways to circumvent the many barriers that B could put in its way.

The takeover process obviously is an extremely complex process, consuming much of both time and money.

SIGNIFICANT CASES

Three merger cases are included at this point to provide examples of the merger activity that is occurring in business today. These cases have received much public attention, and have often been the basis upon which the government has enacted merger legislation. While the DuPont-Conoco and the Allied-Bendix cases demon-

strate "merger wars" that have occurred, the Chevron-Gulf case shows the government's concern regarding the mergers in the oil industry.

Chevron (Standard Oil of California) and Gulf

In 1984, a substantial amount of consolidation took place in the oil industry. Contributing to this was the undervaluation of oil stocks in the market. Influencing the depressed price of oil stocks at this time was the uncertainty regarding the oil industry. Americans had curtailed their use of oil; this resulted in overproduction in the industry. In addition, oil reserves were becoming harder to find and therefore drilling expenses were rapidly increasing. Obviously, there was a serious amount of risk associated with the oil industry.

The largest acquisition taking place in this period was Chevron's purchase of Gulf (\$13.3 billion). And with this acquisition, a great deal of debate took place in the U.S. Senate as to the effects of consolidation in the oil industry. George M. Keller, chairman of Chevron, and T. Boone Pickens, a corporate raider who initiated the Chevron-Gulf merger, were ordered to appear before the Senate. The information that interested the Senate concerned the merger's effect on oil exploration. With merging going on throughout the industry, and the combining of oil reserves, would this not reduce exploration by U.S. firms and create a greater reliance on foreign firms in the future? The Senate realized that, through the merger, Chevron would have huge reserves of oil and could curtail its own exploration. In defense of the merger, Keller assured the Senate

that the exploration of oil would not be sidetracked. Keller said, "This merger will bring together SOCAL's (Chevron) and Gulf's technical and human resources in a new combination that we believe will provide a more effective program of exploration than the companies are carrying on today."⁷⁵ Keller further defended the combination by explaining Pickens' plan for the oil company. Pickens, it was rumored, planned to liquidate the company if he took control. Thousands would lose their jobs if this were allowed.

Pickens was also required to testify. In his statement, he strongly opposed any regulation of the merger activity taking place in the oil industry. Pickens argued that the industry was restructuring itself and mergers were the way of accomplishing this. He also firmly believed in mergers as promoters of efficiency in mismanaged companies; mismanaged companies are usually inefficient, unprofitable, and are perceived by investors as risky investments (therefore, their stock price falls and invites a takeover). Also, in response to the Senate's fear of reduced oil exploration, Pickens argues that oil reserves are becoming more difficult to find--the problem is not the reduced exploration for oil. Pickens' statement was convincing and very much in favor of the Chevron-Gulf merger. The merger was not delayed.

The Chevron-Gulf merger was initiated by T. Boone Pickens' threatened takeover of Gulf. To avoid this takeover, Gulf approached Chevron hoping that the firm would become its white knight; they faced liquidation if T. Boone obtained control. However, no company rescues another without more logical reasoning. Chevron did have much to gain from the purchase. Listed below are some of the growth motives that pertain to the merger:

1. Gulf had a substantial amount of oil reserves
2. Chevron would obtain access to new geographical markets
3. Economies of scale could be further attained
4. Synergy would result (the firms would be more effective together than apart)

Allied and Bendix

Without a doubt, one of the most famous cases in the history of mergers and acquisitions occurred in 1982 when Bendix attempted to acquire Martin Marietta. The scenario began on August 25, 1982 as Bendix offered \$43.00 a share for 45% of Martin Marietta's stock. At this time, Martin Marietta's stock was undervalued; this combined with its highly technological processes made it an attractive target. Bendix, in its attempt to takeover (or force a merger) Martin Marietta, expected very little, if any, trouble from Marietta. They were certainly wrong. On August 30, in response to Bendix's tender offer, Martin Marietta made a counter offer for Bendix (this is called the "Pac-Man" approach). Bendix took this move lightly and still expected the takeover to proceed as planned. Martin Marietta also altered its corporate bylaws stating that if Bendix bought the shares tendered by Martin Marietta shareholders, then Marietta will be required by law to buy the shares tendered to it by Bendix shareholders. Another interesting fact was that Martin Marietta was incorporated in Maryland. The corporate law of Maryland states that the board of directors can only be elected at a shareholder's meeting; also, shareholders must be given ten days notice prior to this meeting. However, Bendix was incorporated in Delaware. Corporate law in this state specifies that the board

of directors can be elected by a majority of shareholders at any time. So, although Bendix had made its tender offer five days before Martin Marietta, Marietta would have the first chance of control (Bendix must give Marietta's shareholders ten days notice before they could elect themselves to the board of directors). Martin Marietta, after the twenty day waiting period required by the FTC, and if tendered enough shares, could elect themselves to the "board" at Bendix immediately.

The turning point in this ordeal occurred when Marietta struck a deal with the CEO of United Technologies Corporation, Harry Gray, to back up Marietta's tender offer should it fail. With this move, Marietta added credibility to its tender offer. In fact the agreement was so convincing that the trustee administering the ESOP (Employee Stock Ownership Plan) at Bendix tendered his shares (23%). Meanwhile, Bendix is tendered or bought 52.7% of Marietta and continued to buy until it had 70% (of Martin Marietta's shares). But Bendix could not control Martin Marietta because it had no position on the board of directors, and could not elect itself to the board without a ten day notice to shareholders. Within this ten day period Marietta would be able to takeover Bendix. After a long and heated battle in the courts, and with Marietta the winner, Bendix accepted its fate and found a white knight in Allied Corporation.⁷⁶

The Battle for Conoco

To set the stage for the Conoco battle, mention has to be made of the owners of this company's stock. The shareholders were

bank trust departments, insurance companies, and mutual funds. These investors in general are not interested in the long-term. Their job depends on the ability to produce quick returns; one of the fastest ways to make big money is to get involved in a takeover, where large premiums are paid. In addition to the investors desire for short-term profits, Conoco was in a very risky situation (its oil reserves had a chance of being expropriated). This factor, which drove the stock to all-time lows, in addition to its profit-oriented investors, made Conoco ripe for a takeover.

Dome Petroleum opened the bidding on May 5, 1981 attempting to obtain a 20% ownership in Conoco. Dome wanted only the Conoco subsidiary, Hudson Bay Oil and Gas Co. Dome planned to trade the 20% (which would be acquired through the tender offer) for the Hudson Bay. Although Dome wanted only the 20% interest, to its surprise 53% of the shares were tendered. This clearly showed that Conoco could be taken over easily; a fact that was not overlooked by other predators. Conoco settled with Dome Petroleum by allowing them to purchase Hudson Bay Oil and Gas Co.

As the tender offer by Dome Petroleum served notice to the business community that Conoco could be easily taken over, the firm began to search for a white knight. It found its partner in Cities Services and moved toward a merger agreement. In this merger, Cities Services was trying to invest to avoid a takeover (defensive merger). At the same time that Conoco and Cities Services were negotiating for a merger, Seagrams relayed to Conoco its interest in the company. Although Seagrams made a reasonable offer and agreed not to purchase a controlling percentage of Conoco, the firm refused the offer.

On June 25, 1981, as Conoco and Cities Services agreed to a merger, Seagrams announced a tender offer for 40% of Conoco's stock at \$73.00 per share. This offer was substantially better than the Cities Services offer and thus killed the previous agreement. Conoco again found itself searching for a white knight.

In its search for a white knight, Conoco received offers from Mobile, Texaco, and DuPont. DuPont was chosen because it was felt that the merger between Conoco and DuPont would be approved by antitrust officials. Mobil and Texaco (both of which are large oil firms) were eliminated because of possible antitrust prosecution that would result. On July 6, DuPont tendered for 40% of Conoco's shares at \$87.50 per share. This bid, in excess of Seagram's offer, killed the Seagram bid. Conoco also took Seagrams to court to eliminate it from the bidding. Seagrams had initially told Conoco that it only wanted to invest in the company. Shortly after making this claim, Seagram's filed notice with the FTC and The Justice Department that it wanted control of Conoco. The courts ruled in favor of Seagrams.

Immediately after court approval, Seagrams raised its bid to \$85.00 for 51% of Conoco's shares. Also surprising everyone, Mobil entered the bidding war with an offer of \$90.00 for 50% of Conoco's stock. Reacting to these new bids, DuPont raised its offer to \$95.00 for 45% of the stock. Conoco was fairly certain that it could not eliminate Seagrams, but it did feel that Mobil's attempt could be extinguished. To do this, Conoco hired the public relation firm of Kekst and Company to spread antitrust propaganda. It was effective. Although Mobil raised its bid several times, and its bid reached \$120.00 per share, shareholders would not tender their

shares to Mobil for fear of antitrust violation if the merger took place.

DuPont persevered and survived as the winning firm. There was an exchange with Seagrams in which DuPont exchanged 20% of its stock for the Conoco shares Seagrams had been tendered. DuPont now owns a firm that will help diversify its volatile chemical business.

The three cases that have been presented show the complexity of the takeover or merger process; also shown were some of the goals for growth. In all three cases, whether the merger was an aggressive maneuver or a defensive one, the growth was a means of survival.⁷⁷

CONCLUSION

The research of mergers and acquisitions has led to the conclusion that the desire for growth has been the general motive. In the first chapter, "Historical Perspective," the growth theme became obvious as firms either grew horizontally, vertically, or in a conglomerate manner. And the discussion of the current merger wave showed how firms have expanded in all possible directions in reaction to economic conditions. Growth, alone, however, does not precisely explain the presence of the phenomenon. Mergers, in all four waves, have been significantly involved in business strategies because they are a means of survival.

However, this survival technique (merger or acquisition) occurs only under certain economic conditions. In all of the merger waves (both the three historical and the current wave), there was an expanding economy; the market demanded a higher level of

industrial performance and output. In addition, as the economy became strong so did the stock market. Investors saw opportunity in the stock market because of its undervaluation. Another factor that has been common to the merger waves is that of "threat"-- a threat that jeopardizes the survival of businesses. The first wave was largely attributed to the intensely competitive business environment; the degree of competition actually threatened the survival of several firms. Currently, the movement of foreign firms into the U.S. market has not only threatened the future of American firms, but has also jeopardized entire industries. The response to the latest threat, that of foreign competition, has been the merging or combining of firms to survive.

Ironically, the free market itself promotes mergers. Associated with the free market is competition, which is considered the motivator ("invisible hand"). But within competition, as Karl Marx noted, is contained the seed of its own destruction. American firms are compelled by competition to pursue efficiency and to gain whatever advantages that it can over rivals. In actuality, this pursuit of a competitive advantage leads to the desire for monopolistic power. And there is no faster and, at times, more efficient way of attempting market dominance than through merger.

Also, it has been shown that in the American economy is the tendency to overproduce. Why does this occur? The free market allows the entrance and exit of firms at will; therefore, as a market becomes profitable, businesses respond by moving into it. Eventually, the market is saturated, resulting in lower profits. As this occurs, merging is often used to correct the imbalance that was created; the stronger and more profitable firms buy those

that are weaker.

Mergers have been shown to be a reaction to the free market when conditions are conducive to growth. Also discussed was the mergers potential in aiding a monopoly pursuit--a negative aspect of the activity. However, mergers and acquisitions provide the free market with flexibility and allows for the more efficient use of assets. Inefficient firms, and firms in receding markets, are purchased or acquired, and are therefore redeployed and used in a more productive manner. Associated with the three previous merger waves, and the current wave, has been the changing or re-defining of markets. In the current movement, the rapid pace of technology and the change in consumer demographics have drastically altered markets. Many firms have chosen the merger as a means of adapting to this changed demand--in fact, it is the fastest way to react. The merger transaction has allowed a fast and efficient redeployment of assets, and therefore has allowed the survival of both American firms and industries.

In the American economy, mergers and acquisitions are used for growth, but as with any other tactic that a business uses to adjust in a free and competitive market, it is a survival technique.

The merger phenomenon follows a noticeable cycle. First, economic conditions become favorable to the merger. Then, when the stock market becomes strong or bullish and the economy strengthens, mergers increase in number--they, the merger, peak at the same time as the stock market and economy. Finally, the merger wave always ends with a receding or recessionary economy. This cycle has been followed by all three of the previous waves.

In predicting the future of mergers, many feel that the movement may not have peaked. Although the stock market is adjusting, as stock prices increase, there are still undervalued firms on the market; opportunities can be found. However, the government has been increasing its investigation on the effects of mergers on the economy. If the government increases its enforcement of antitrust regulation, the movement is certain to decline. The Reagan administration, however, has interfered little thus far in the merger activity, and probably will not drastically alter its philosophy in the future. In addition, foreign competition is still a threat to American firms, and a contributor to the "urge to merge."

Look for an increase in the number of mergers.

The merger and acquisition phenomenon is common only to the free market. It provides the American economy with a flexibility that will allow both its firms and industries to survive.

NOTES

1 Malcolm S. Salter and Wolf A. Weinhold, Merger Trends and Prospects for the 1980s(Graduate School of Business Administration, Harvard University), p.2.

2 Salter and Weinhold, p. 4.

3 Salter and Weinhold, p. 10.

4 David O. Whitten, The Emergence of Giant Enterprise, 1860-1914(Westport, Connecticut: Greenwood Press,1983), p. 60.

5 Kenneth M. Davidson, Mega-Mergers(Massachussets: Ballinger Publishing Co., 1985), p. 131.

6 Salter and Weinhold, p. 2.

7 Whitten, p, 65.

8 Ida M. Tarbell, The History of the Standard Oil Company (New York: Harper and Row, 1966), p. 180.

9 Tarbell, p. 28.

10 Tarbell, p. 33.

11 Tarbell, p. 62.

12 Davidson, p. 137.

13 Salter and Weinhold, p. 7.

14 Peter O. Steiner, Mergers(Ann Harbor: University of Michigan Press, 1975), p. 52.

15 Salter and Weinhold, p. 4.

16 Robert Sobel, ITT: The Management of Opportunity(New York: Truman Tally Books, 1982), p. 53.

17 Salter and Weinhold, p. 7.

18 Peter Asch and Rosalind Seneca, Government and the Market-place(Chicago: The Dryden Press, 1985), p. 151.

19 Salter and Weinhold, p. 6.

20 Davidson, p. 138.

21 Sobel, p. 8.

22 Sobel, p. 198.

23 Sobel, p. 198.

24 Sobel, p. 202.

25 Salter and Weinhold, p. 7.

26 Salter and Weinhold, p. 35.

27 "How Congress Plans to Cool Merger Fever," Business Week, 2 April 1984, p. 28.

28 Davidson, p. 183.

29 Salter and Weinhold, p. 40.

30 "Reagan to Seek Antitrust Law Changes," The Fayetteville Times, 16 Jan. 1986, A2.

31 John Greenwald, "Let's Make A Deal," Time, 23 Dec. 1985, p. 44.

32 Greenwald, p. 45.

33 Davidson, p. 232.

34 Greenwald, p. 48.

35 Davidson, p. 144.

36 Don Gussow, The New Merger Game(New York: Amacom, 1978), p. 7.

37 Anne B. Fischer, "The Decades Worst Mergers," Fortune, 30 April 1984, p. 263.

38 Greenwald, p. 47.

39 John A. Halloran and Howard P. Lanser, Introduction to Financial Management(Glenview, Illinois: Scott, Foresman and Co., 1985), p. 605.

- 40 "Allied After Bendix: R&D is the Key," Business Week,
12 Dec. 1983, p. 76.
- 41 "Allied After Bendix," p. 76.
- 42 Richard Brealey and Stewart Myers, Principles of Corporate Finance (New York: McGraw-Hill, 1984), p. 704.
- 43 Halloran and Lanser, p. 712.
- 44 Davidson, p. 201.
- 45 "The New LTV Steel: How Republic Will Fit In," Business Week, 16 April 1984, p. 129.
- 46 Patricia Sellers, "PepsiCo Swallows Seven-Up," Fortune,
17 Feb. 1986, p. 11.
- 47 Davidson, p. 202.
- 48 Carol J. Loomis, "The Morning After At Phibro-Salomon,"
Fortune, 10 Jan. 1983, p. 26.
- 49 Anne B. Fischer, "Mergers That Worked," Fortune, 30 April
1984, p. 270.
- 50 Greenwald, p. 45.
- 51 Davidson, p. 238.
- 52 Davidson, p. 238.
- 53 Jim Duff, "North Carolina's Big Three Move Out,"
Business: North Carolina, November 1985, p. 15.
- 54 Ellen Wojahn, "Sonic Air's Boom Goes Bust," Fortune,
Dec. 1985, p. 62.
- 55 "The Tax Muddle That Could Spur More Takeovers," Business Week, 14 May 1984, p. 166.
- 56 Geoffrey Colvin, "The Smart Taxophobe at Baldwin-United,"
Fortune, 8 March 1982, p. 54.
- 57 Davidson, p. 207.
- 58 Paul M. Fischer, William J. Taylor, and J. Arthur Leer,
Advanced Accounting (Ohio: South-Western Publishing Co., 1982), p. 164.

- 59 Fischer, Taylor, and Leer, p. 164.
- 60 Davidson, p. 236.
- 61 Charles P. Alexander, "A Reunion of Technological Titans,"
Time, 23 Dec. 1985, p. 47.
- 62 Alexander, p. 48.
- 63 Stewart Toy, "Why Western Airlines May Not Be Flying Solo
For Long," Business Week, 2 Dec. 1985, p. 68.
- 64 U.S. Congress, United States Senate, Oil Merger Activity,
98th Congress (Washington, DC: GPO, 1984), p. 109.
- 65 Davidson, p. 215.
- 66 "Hasbro: Merging With Milton Bradley To Get Nearer The
No. 1 Spot," Business Week, 21 May 1984, p. 90.
- 67 "Hasbro:", p. 90.
- 68 Tom O'Hanlon, "What Does This Man Want?" Forbes, 30 Jan.
1984, p. 86.
- 69 Davidson, p. 217.
- 70 Patricia Gray, "Unlikely Mogul," The Wall Street Journal,
7 Nov. 1985, p. 1 and 22.
- 71 Gray, p. 22.
- 72 Ford S. Worthy, "What's Next For The Raiders?" Fortune,
11 Nov. 1985, p. 21.
- 73 Worthy, p. 25.
- 74 Worthy, p. 22.
- 75 U.S. Congress, U.S. Senate, p. 109.
- 76 Davidson, pp. 86-100.
- 77 Davidson, pp. 65-78.
- 78 Philip Kotler, Marketing Management (New Jersey: Prentice-
Hall, Inc., 1984), p. 354.

A SELECTED BIBLIOGRAPHY

- Alexander, Charles P. "A Reunion of Technological Titans." Time, 23 Dec. 1985, pp. 48-49.
- "Allied After Bendix: R&D is the Key." Business Week, 12 Dec. 1983, pp. 76-86.
- Asch, Peter and Rosalind Seneca. Government and the Marketplace. Chicago: The Dryden Press, 1985.
- Brealey, Richard, and Stewart Myers. Principles of Corporate Finance. 2nd ed. New York: McGraw-Hill, 1984.
- Colvin, Geoffrey. "The Smart Taxophobe at Baldwin-United." Fortune, 8 March 1982, pp. 52-59.
- Davidson, Kenneth M. Mega-Mergers. Cambridge, Massachusetts: Ballinger Publishing Co., 1985.
- Fischer, Anne B. "Mergers That Worked." Fortune, 30 April 1984, p. 270.
- Fischer, Anne B. "The Decade's Worst Mergers." Fortune, 30 April 1984, pp. 263-270.
- Greenwald, John. "Let's Make A Deal." Time, 23 Dec. 1985, pp. 42-47.
- Gussow, Don. The New Merger Game. New York: Amacom, 1978.
- Halloran, John A., and Howard P. Lanser. Introduction to Financial Management. Glenview, Illinois: Scott, Foresman and Co., 1985.
- "Hasbro: Merging With Milton Bradley To Get Nearer The No. 1 Spot." Business Week, 21 May 1984, p. 90.
- "How Congress Plans To Cool Merger Fever." Business Week, 2 April 1984, p. 28.
- Loomis, Carol J. "The Morning After At Phibro-Salomon." Fortune, 10 Jan. 1983, pp. 74-79.
- O'Manlon, Tom. "What Does This Man Want?" Forbes, 30 Jan. 1984, pp. 78-86.
- Salter, Malcolm S. and Wolf A. Weinhold. Merger Trends and Prospects for the 1980s, Harvard University, Graduate School of Business Administration, Dec. 1980.
- Sellers, Patricia. "PepsiCo Swallows Seven-Up." Fortune, 17 Feb. 1986, p. 11.
- Steiner, Peter O. Mergers. Ann Arbor: University of Michigan Press, 1975.
- "The New LTV Steel: How Republic Will Fit In." Business Week, 16 April 1984, p. 129.
- "The Tax Muddle That Could Spur More Takeovers." Business Week, 14 May 1984, pp. 166-67.
- Whitten, David O. The Emergence of Giant Enterprise, 1860-1914. Westport, Connecticut: Greenwood Press, 1983.
- U.S. Cong. Senate. Hearing Before the Committee on the Judiciary U.S. Senate. Oil Merger Activity. 98th Cong. Washington, D.C.: GPO, 1984.
- Worthy, Ford S. "What's Next for the Raiders." Fortune, 11 Nov. 1985, pp. 20-24.