Commercial

Mergers and Acquisitions: The Different Types (Article 2 of 3)

There are a number of different M&A structures that companies and deal-makers can opt for but they all have one common goal: to create synergy that makes the value of the combined companies greater than the sum of the two parts. The success of a merger or acquisition depends on whether this synergy is achieved, no matter which form it takes.

Types of mergers

The following are defined by the relationship between the two companies:

Horizontal merger: two companies that are in direct competition and share the same product lines and markets - e.g. two soft-drink manufacturers, both operating in the UK.

Vertical merger: a customer and company or a supplier and company - e.g. a soft-drink manufacturer and a separate bottling company.

Market-extension merger: two companies that sell the same products in different markets - e.g. two soft-drink manufacturers, one operating in the UK only, the other in the rest of the EU.

Product-extension merger: two companies selling different but related products in the same market - e.g. a soft-drink manufacturer and an energy-drink manufacturer.

Conglomeration: two companies that have no common business areas.

Mergers can also be distinguished by how they are financed:

Purchase merger: this occurs when one company purchases another. The purchase is made with cash or through the issue of some kind of debt instrument and the sale is taxable. Acquiring companies will prefer this type of merger as it can provide some tax benefits.

Consolidation merger: a brand new company is formed and both companies are bought and combined under the new entity.

The proposed merger of Ladbrokes and Gala Coral is an example of a horizontal merger. Both companies are in the gambling industry and are set to overtake William Hill as Britain's biggest bookmaker as a combined group. The merged company will be called Ladbrokes Coral and will be listed on the London stock exchange. The deal is set to be worth £2.3bn.

Types of acquisitions

All acquisitions involve one firm purchasing another – there is no exchange of stock or consolidation as a new company. Like mergers, acquisitions are actions through which companies seek economies of scale, efficiencies and enhanced market visibility.

In an acquisition, a company can buy another company with cash, stock or a combination of the two. Another possibility is for one company to acquire all the assets of another company. The selling company will become a shell and will eventually liquidate or enter another area of business.

A 'reverse merger' occurs when a private company that has strong prospects and is eager to raise financing buys a publicly-listed shell company, usually one with little or no business and limited assets. The private company reverse mergers into the public company and together they become a new public corporation with tradable shares. This enables the private company to get publicly-listed in a relatively short time period.

Our next article will deal with the valuation, the M&A deal and why sometimes the deal can fail. Should you have any queries in the meantime, please contact the Commercial team at 3HR Legal.

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