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# **MERGERS AND ACQUISITIONS;** **CONSIDERATIONS IN THE COVID 19 ERA**

Authored by –  
Arpit Chauhan & Aarsha Prem

## **Abstract**

*The aim of this research paper is to discuss what the companies must do and areas they must focus on while entering into a merger and acquisitions. Highlights of various articles, news and papers have been analysed to find the main foci and provide the most effective solutions. The impact of COVID 19 on various deals have been discussed. Through examples of successful and failed combinations considerations in the COVID19 era have been discussed.*

**Keywords-Merger, Acquisition, Combination, COVID, Adidas merger, Reliance-netmed merger, CMS- TMC merger, Ranbaxy, BedBathBeyond case, Soft Bank- We work, Xerox- HP**

## **Mergers and Acquisitions**

A merger is the voluntary combination of two companies on largely equal terms into a new legal entity. Acquisitions are generally the involuntary purchase of a company by another.

Mergers and acquisitions are typically done to expand a company's reach, expand into new markets and service, or to gain shares. All of this is directly proportional to the shareholder value.

Mergers are done with the aim of gaining market share, reducing costs of operations, expansion and increasing profits which should benefit the firms' shareholders. Once merged the shares of the new company are distributed among the existing shareholders of the companies involved. Example- CMC merger with TCS<sup>1</sup>.

In acquisition the purchase of more than 50% of a target firm's stock and other assets allows the acquirer to make decisions about the newly acquired assets without prior approval of the company's other shareholders. Example- Sun Pharmaceuticals acquired Ranbaxy<sup>2</sup>

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<sup>1</sup> <https://economictimes.indiatimes.com/tech/software/cmc-to-merge-with-tata-consultancy-services/articleshow/44836933.cms?from=mdr>

<sup>2</sup> <https://mnacritique.mergersindia.com/sun-pharma-acquires-ranbaxy/>

Section 5 of the Competition Act<sup>3</sup> states that a transaction shall be qualified as Combination when a) control, voting rights, assets or shares of a company are acquired by a person; b) acquisition of control of an enterprise where the acquirer already has direct or indirect control over another entity engaged in identical business; or c) a merger or amalgamation between enterprises.

Mergers and Acquisitions can take place by

1. purchasing assets
2. purchasing common shares
3. exchange of shares for assets
4. exchanging shares for shares

## **Steps involved in mergers and acquisitions**

Before understanding the impact of Covid 19 on mergers and acquisitions it is important to understand the steps involved in a successful combination.

Step 1- Research into market growth and trends

Step 2-Identifying the candidates for merger or acquisition

Step 3- Planning and Strategizing

Step 4- Determining valuation and terms

Step 5- Negotiations

Step 6- Due Diligence

Step 7- Initiating transaction

Step 8- Monitor Ongoing Performance

Step 9- Finalising the merger or acquisition

## **Present scenario**

The pandemic of COVID 19 took the world by surprise and crumbled the market. A massive number of businesses have collapsed and millions have been laid off in a short span. Supply chain, consumer patterns and production have all been adversely affected. Mergers and acquisitions have taken a heavy blow by almost reaching a standstill by the end of 2020.

One of the reasons is that companies have been forced to redirect their resources and focus to maintaining the health of their own companies and save their existing portfolios. subsequently long term plans have taken a back seat.

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<sup>3</sup> The competition Act 2002

Even parties to pending M&A transactions have abandoned deals that were pending, such as Xerox retracting its \$34 billion offer for HP, after having postponed meetings with HP shareholders to focus on coping with the coronavirus pandemic<sup>4</sup>. Soft Bank has sacked its \$3 billion tender offer for We Work shares, quoting the coronavirus impact together with the failure of a number of closing conditions<sup>5</sup>. Bed Bath & Beyond has commenced litigation in Delaware with respect to delays in the pending sale of one of its divisions to 1-800-Flowers for \$250 million<sup>6</sup>. Boeing suppliers Hexcel and Woodward have mutually terminated their \$6.4 billion merger of equals transaction noting the “unprecedented challenges” caused by the pandemic<sup>7</sup>. The pandemic has considerably increased the time for elements of a merger or acquisition, including the negotiation period, due diligence, obtaining consents, acquiring permissions and the other processes required to make the merger or acquisition a success.

## Affect of Covid 19

### **1. Force Majeure (FM)**

Under force majeure when the performance under a particular contract is hindered by an uncontrollable event the contract is suspended. Covid being an unforeseeable condition forced companies to rethink their cooperation. The mergers and acquisitions in this state have seen suspension in some cases whereas they have been terminated in the others.

### **2. Funding**

The pandemic has severely affected the stock market and has forced the companies to retreat funds to ensure the continuance of their organisations and provide healthcare to the employees. Because of the business turmoil created by the pandemic, sellers and/or merger parties are having difficulty aligning the value of the contract. Since it is impossible to predict future profits, carrying out the earn out mechanism is challenging. It is the process by which the buyer's payment is valued in relation to the seller's post-closing financial success.

### **3. Negotiations**

During the pandemic mergers and acquisitions have fell through mainly because due diligence before a combination and negotiations required have been hampered.

<sup>4</sup> <https://www.cnbc.com/2020/03/31/xerox-ends-its-hostile-takeover-bid-for-hp.html>

<sup>5</sup> <https://www.cnbc.com/2020/04/02/softbank-terminates-3-billion-wework-tender-offer.html>

<sup>6</sup> <https://www.jdsupra.com/legalnews/beyond-mae-covid-19-related-m-a-44816/>

<sup>7</sup> <https://www.businesswire.com/news/home/20200406005143/en/Woodward-and-Hexcel-Announce-Mutual-Termination-of-Merger-Agreement>

#### **4.Delays**

The pandemic has created a circumstance where the process of meetings, approvals, registration, notices and agreements have been postponed due to the restriction on the working hours and worker strength along with the various rounds of lockdown

#### **5.Due diligence**

The buyers face the most overwhelming challenge with the dilemma from a financial perspective but also from a legal circumstance, when there are occasions when the business may have committed white collar fraud, which may have lowered its valuation, and prior transactions have failed. And, when the buyers conduct due diligence, the sellers may not want to reduce the value of their businesses as a result of the prior sale, and they may want to fix the issue but are unable to do so due to the pandemic. So not only is due diligence difficult for the buyer but the seller is also facing hindrances mending their image.

#### **6.Risk**

Outside dates are the dates on which the parties jointly agree to close the transaction in accordance with the MAE provision. There were several businesses that had already entered into some sort of M&A deal before the pandemic struck, and all of those deals were halted due to the pandemic. As a result, the parties' agreed-upon completion deadlines for the transaction could not be met.

Since the pandemic certain transactions fell apart as the sides were unable to agree on a specific date because of the parity, due to technological limitations, was unable to transfer the files from offline to online mode. This is also a factor that has been influenced by covid.

Since the pandemic, more companies switched to virtual platforms, which has aided wrongdoers because companies who were involved in some kind of issue that was preventing them from completing a successful transaction have a technological advantage to resolve their issues and improve their valuation, but it also increased the chances of them being caught and breach of contract being committed. As a result, both the parties now face a greater risk.

## **Case study**

1. In 2005, ADIDAS announced its intention to buy REEBOK for \$3.78 billion. In a fierce rivalry between ADIDAS, PUMA, NIKE, REEBOK, and a footwear industry led by NIKE, ADIDAS gave REEBOK a 34 percent premium on the previous closing price for the reebok. For REEBOK, it was simply an amazing bargain.<sup>8</sup>

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<sup>8</sup> <https://www.adidas-group.com/en/investors/investor-events/reebok-acquisition/>

2. Both Adidas and Reebok developed specific plans for increasing market share and lowering expenses through their synergy. Adidas planned to recreate the scene with its high-quality merchandise, while Reebok planned to aid with its stylized quotient.
3. Since then, we've been watching the successful merger. Things weren't as difficult back in 2005 when it was handled
4. ed offline, and the ADIDAS-REEBOK transaction and consideration is straightforward.
5. There were several factors that contributed to the successful merger, including:
  - The cultural blend-back then,
  - no activities were held remotely and
  - technology was not as sophisticated,
  - people from both organisations blended so easily and seamlessly that they gave the organisation a new name.
6. However, they are not the only factors that contribute to the merger's success; prior considerations are often required and they are the primary basis for determining whether or not the consumer will benefit from the Merger.
7. Tax considerations, payment forms, due diligence, representation and guarantees, insurances, and so on are all important factors to consider when engaging in any M&A deal.
8. Any consideration must be carried out exactly as the future demands. Before any deal, it is self-evident that there are certain problems that are impeding the organization's growth and must be addressed, whether they are tax-related, cultural-related, or share-related. There could be ethical disputes that are preventing the organisation from growing more, and they could be resolved by diligence.
9. Because of the simpler circumstances in 2005 and all being offline, M&A transactions were more efficient than M&A transactions during the pandemic 2020, according to a poll, where 51 percent of transactions went into a "temporary pause."<sup>9</sup>
10. One of the most significant purchases was set to take place prior to the outbreak of the pandemic, in which Boeing allegedly planned to buy an 80 percent interest in Embraer's commercial aircraft

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<sup>9</sup> <https://hbr.org/2020/06/what-ma-looks-like-during-the-pandemic>

division. The merger was proposed in 2019 and was set to be finalised in 2020, but the pandemic struck the aviation market so hard that Boeing terminated the joint venture agreement<sup>10</sup>.

11. Although Embraer sued Boeing for "wrongful termination," we can see from this example how the entire considerations for M&A transactions have shifted from what they were prior to the pandemic. Putting such considerations into action has been a task in and of itself.
12. One of the most realistic problems is to exercise due caution at times of conflict, when modern laws of social distancing and travel limits find it difficult to carry out these considerations.
13. Due diligence issues such as employment, materials contracts, IT structures and data protection, loan covenants, and so on have become more pertinent owing to the pandemic.
14. Aside from due diligence, some considerations such as agreements have shifted. While the underlying framework of the deal has not changed, a few provisions have changed as a consequence of the pandemic, such as MAE and MAC clauses, earn-out clauses, purchase price adjustments, and so on.
15. Much like Boeing, which was hunting for profits but couldn't get them after the pandemic struck, firms that had deals before the pandemic hit or were in the early stages of considering M&A transactions are now using the "Temporary Pause" due to the pandemic as accessing the possible business turnaround time and revaluation of their contract and bargaining.
16. There were a few concessions, such as Google Cloud, Black Rock, Dependency, Nestle<sup>11</sup>, and others, who were ready for some kind of M&A transaction. This was accredited to the fact that these businesses operated remotely and were not affected by the pandemic in the same way that others were.
17. Many firms were interested in profitable M&A transactions during the pandemic, and one of the most notable of these is The Reliance Retail, which bought the majority of stakes in Netmeds<sup>12</sup>.
18. Reliance did a rather accurate assessment and consideration of the contract with netmeds. Unlike other businesses, Reliance was unchanged by the pandemic and understood that purchasing medical institutions would result in a large profit, similar to the agreements negotiated by Amazon with many online pharmacies.

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<sup>10</sup> <https://boeing.mediaroom.com/2020-04-25-Boeing-Terminates-Agreement-to-Establish-Joint-Ventures-with-Embraer>

<sup>11</sup> <https://www.fooddive.com/news/lets-make-a-deal-how-nestle-is-using-ma-and-multibillion-dollar-divestit/593601/>

<sup>12</sup> <https://www.thehindubusinessline.com/companies/why-the-netmeds-acquisition-is-significant-for-reliance-industries/article32393500.ece>

## What can be done?

1. The most important step to merger or acquisition is understanding. Especially in a period like this, the companies must reconsider the timing at the preliminary documentation stage (eg. non-binding letters of intent, memorandums of understanding, non-binding offers and non-disclosure agreements) such as exclusivity period, due diligence dates and timing of the offers, as the process could now be different and prolonged.
2. Parties should especially focus on COVID-19's impact on revenues and debts, suppliers, distributors and customers, insurance policies and risks, and accordingly re evaluate the valuation and terms.
3. Any business was affected by the pandemic, excluding those who were able to keep their customers. A significant financial hit can occur only if one loses a client. Companies must realise that developing good relationships with their customers can only result in earnings. Companies must get engaged and develop relationships with their customers virtually in order for them to support the firm more and therefore to praise them in this difficult situation.
4. During the pandemic, almost everyone realised that they needed to accept technological advancements and work in tandem with them because, as competition increased, companies needed to advance in the tech sector. As a result of this, the majority of corporations worked out how to do due diligence virtually. Due diligence can be performed by generating a clean virtual room and leveraging the data there. Companies must realise that this is the simplest and most effective method of conducting due diligence. Traditional due diligence does not continue to execute data intensive due diligence, however interactive due diligence can.
5. *Force majeure* provisions in and termination rights under key contracts, new employment law and data privacy-related issues and mitigation and contingency plans and scenarios regarding the COVID-19 pandemic should also be re visited.
6. The buyers in M&A deals should also be aware of the new rules that are being released by the government during this period including new rules regarding employment law and workplace health and safety rules or data privacy rules on employees' personal health data or sector-related restrictions.

7. Buyers may also request specific warranties on any COVID-19 business contingency plans or financial assessments and financial projections. Open conversation is key, where the seller discloses any contingency regarding any covid situation or the buyer requires a prolonged period of guarantee or indemnity.
8. Since there are a lot of changes in the market currently it is important to revise the terms and conditions of the contract before signing. The condition of the market and limits of workers along with the financial condition of the company must be considered.
9. Uncertainties remain but the lack of preparation which was an issue at the beginning of 2020 is no longer an obstacle as businesses can identify the opportunities available to them now, so as to better position themselves for success in 2021 and beyond.
10. No risk no reward. The company must be willing to take planned risks so as to reap the maximum benefit out of the combination. Multiple bets must be made, in order to diversify investment and minimize risk.
11. The management of the companies involved in mergers and acquisitions must be resilient, patient and able to adapt to the ever-changing business dynamics in the industry in this Covid period.

## Conclusion

The present condition is a great lesson at understanding how the market should be. The market is dynamic and to stay in it, you must remain versatile. While high-value mergers and acquisitions always make headlines, not all of them result in success, failures linked to factors, like cultural integration, geographical and geopolitical issues, and market dynamics, often stomp on the expected success. Awareness about the changing market, audience and business is the priority. Before finalising a contract re visiting the terms and conditions is greatly important to ensure that both the parties have a win win and the stance of both the parties is clear. The objective behind M&A is that two separate companies together create more value compared to being on an individual stand. Alone we can do so little, together we can do so much.