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VIEWPOINT

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Era of the Not-So-Hostile Takeover

Is the corporate raider back? Headlines on some of the most prominent of recent takeover stories have proclaimed it so, conjuring up visions of management teams being toppled, companies being sold off piece by piece, massive layoffs and stockholders being stuck with securities of dubious value.

That's a vivid image, to be sure, but a totally inaccurate one—whether talking about Kirk Kerkorian's bid for Chrysler, Northrop's acquisition of Grumman or Rockwell International's purchase of Reliance Electric. And it masks a very important fact: the new wave of corporate takeovers is a healthy development for nearly all parties affected.

The current resurgence of takeover activity differs in several ways from the heyday of corporate raiders like Carl C. Icahn and T. Boone Pickens.

BIDS AREN'T REALLY HOSTILE

First and most important, today's merger-and-acquisition climate is almost completely devoid of the hostile bid, that storm-provoking device that characterized some of the biggest takeovers of the 80's. A hostile bid was, of course, an unsolicited offer for a company that had no interest in being acquired. Often it was made by a financial suitor whose primary objective was to maximize a company's value by selling off its parts for more than was paid for the whole.

Now, we're seeing competing bids by strategic buyers, those who believe they can use operating synergy and better management to increase a target company's value.

Consider three recent takeovers that have been described in the media as raider-type deals: Northrop's purchase of Grumman; Rockwell's acquisition of Reliance; and American Home Products' takeover of American Cyanamid.

Originally, Martin-Marietta agreed to merge with Grumman; General Signal arranged to acquire Reliance; and Cyanamid planned an asset swap with SmithKline Beecham.

The important aspect of these transactions was that all of the acquired companies had put themselves up for sale. They were trying to arrange marriages with partners of their own choosing. But companies came along and said, "Wait! If you're thinking about selling, we want an opportunity to bid." Their interest can hardly be characterized as hostile.

And it clearly works to the advantage of a target company's shareholders. If management negotiates the company's sale, the shareholders must either accept or reject the deal in a vacuum, with no competing transaction to weigh it against. But a rival offer from another company gives shareholders a choice.

LENDERS ARE MORE CAUTIOUS Ten years ago, it was not unusual for a bank or other senior lender to provide funds for a leveraged buyout in which the buyer had as little as 5 or 10 percent equity in a target company. Now, lenders are insisting that buyers provide anywhere from 20 to 35 percent or more of the purchase price, resulting in more solidly capitalized companies after they are acquired. The Blackstone Group's acquisition of UCAR International was so structured, as is Boston Ventures' pending purchase of Six Flags theme parks and Seagram's pending acquisition of MCA.

Lenders are being equally conservative in the type of financing they will extend. Gone is the back-ended loan, in which little principal was repaid in the early years and most was due in the final year or two. Today, lenders typically require straight-line amortization, with equal payments spread over a five- to seven-year term.

GREENMAIL IS A DEAD LETTER In the 80's, corporate raiders often would buy a significant minority interest in a target company and threaten the target's management with a takeover unless the raider's stock was bought back at a premium.

But this technique isn't being used today—witness Mr. Kerkorian's attempt to acquire the Chrysler Corporation.

Mr. Kerkorian owns 10 percent of Chrysler's common stock. In the 80's, that much ownership, coupled with a takeover threat, might well have provoked a company's management to offer greenmail. But Chrysler's management has expressed no interest in buying off Mr. Kerkorian, whose bid now appears to be going nowhere.

POISON PILLS ARE KILLING DEALS The success of the poison pill helps to explain further the change in the M&A environment. The courts have usually supported the use of these devices, which allow a company to sell massive amounts of shares to existing stockholders at bargain prices when a raider comes along, driving up the cost of an acquisition. Poison pills recently helped thwart Union Pacific's bid for Sante Fe Pacific and Seagram's march to gain control of Time Warner.

These changes in the M&A arena are truly beneficial to almost all involved: stockholders are receiving greater value, employees are more secure in their jobs and lenders sleep better. The corporate raider may not be forgotten, but he's gone. □

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