**Mergers and Acquisitions and Corporate Restructuring**

**Learning Outcomes**

When you have completed this module, you should be able to:

1. Explain the reasons for engaging in M&A activity.
2. Recognize when the different forms of M&A activity should be utilized.
3. Select suitable take-over defences to protect companies from unwanted acquirers or to increase their take-over bids.
4. Formulate an appropriate take-over bid for a business.
5. Evaluate the division of synergies between the acquirer and target.
6. Identify common problems with M&A activity.
7. Discuss the rationale for employing other forms of corporate restructuring, including divestitures, spin-offs, split-offs, split-ups, and tracking shares.

**Introduction**

Mergers and acquisitions (M&A) increase the value of a firm through the creation of synergies. These synergies can take many forms, such as higher prices due to reduced competition, increased sales from improved distribution, lower operating costs because of economies of scale, tax savings from loss carryforwards, or improved strategic and financial management.

M&A can be either friendly or extremely hostile. In most cases, the management of two companies mutually agree to merge their operations or have one company acquire the other firm. If the parties do not agree, one may attempt a take-over by appealing directly to the other company’s shareholders. The bidding process followed is quite formal and carefully monitored by securities regulators to ensure all investors are treated fairly. Take-overs are expensive transactions, so the offeror recruits a large group of outside advisors consisting of investment bankers, lawyers, and accountants to help determine a fair value for the firm, guide them through the bidding process, and counter any defensive measures the target company might take to stop or delay the acquisition. The target company also uses outside advisors to ensure that the offering price is fair and to negotiate aggressively with the offeror. These advisors are very successful, as the target company’s shareholders usually receive a sizeable price premium that includes nearly all the potential synergies.

Besides M&A, companies can restructure their operations using divestitures, spin-offs, split-outs, and split-ups to re-focus on their core business, redeploy capital, pay down debt, or outsource production. Corporate restructuring is usually poorly perceived by the public because of the plant closures and layoffs that can sometimes result. Although these actions are difficult for employees, they are essential if the economy is to remain efficient and managers are to maximize their firm’s share price.

* 1. **| Rationale for M&A**

M&A occur when two companies voluntarily agree to combine their operations through a merger, or one company buys another company from its owners in an acquisition. A significant price or take-over premium is usually paid relative to the target company’s current share price because of the synergies that can be realized by combining the two firms. The equation “2 + 2 = 5” is used to indicate that the combined firm is worth more than the sum of its parts.

**Types of Synergies**

There are many different types of synergies from M&A.

**Revenue generation synergies.** A horizontal M&A occurs when a company buys a direct competitor. This will likely reduce market competition and allow the company to raise its prices. Unit sales may also increase as the firm gains access to more creative advertising, improved selling and distribution systems, new sales territories, or better store locations. Greater product selection makes the company more appealing to retail customers or to business-to-business clients who want to source more products from fewer suppliers. Because horizontal M&A may be harmful to the public by lessening competition, governments must approve all acquisitions.

**Cost reduction synergies.** HorizontalM&A can offer considerable economies of scale, economies of scope, and other efficiencies. Economies of scale occur when fixed operating costs are spread over a greater number of units. Economies of scope result when specialized services like R&D, marketing, and selling and distribution are used to support a greater variety of products. Centralized functions such as senior management, accounting, legal, marketing, sales and distribution, and R&D are combined, and duplicative staff and space are eliminated. Manufacturing capacity is consolidated in a smaller number of larger plants. Seasonal fluctuations in sales and production are balanced by adding more products and sales in new geographical areas. Lower prices and higher quantity discounts are realized with increased buying power. Net working capital, especially cash and inventory, falls as a percentage of total assets through consolidating resources.

Vertical M&A offers to buy either a supplier or a customer. Backward integration can reduce costs by eliminating the profits of suppliers, improving coordination in the supply chain, improving quality, and securing access to key inputs like natural resources or technology. Forward integration allows companies to eliminate their distributors’ profits, provide better customer service, and learn first-hand about their customers’ needs. Backward integration is becoming less popular due to the greater use of just-in-time inventory and contracting out, and the desire by firms for more flexible operations.

**Financial synergies.** A target company may have high agency costs that reduce its share price. These costs can result from excessive cash balances, sub-optimal use of financial leverage, poor management, and unprofitable growth. If the offeror can address these problems, the target’s market value will rise. Increasing dividends or stock repurchases reduces excessive cash and unprofitable growth by returning unneeded funds to shareholders before they are wasted on low-yielding short-term investments or negative net present value projects. Eliminating unused debt capacity increases the firm’s return on equity through greater use of financial leverage. Poorly performing executives with excessive pay and perks are removed, and the hidden value of the target’s assets is realized through better management. Larger firms have lower financing costs due to increased market power when dealing with financial institutions. Improved equity analyst coverage for bigger companies creates a more liquid market for the target’s shares, leading to a higher price.

**Taxation synergies.** Canada’s Income Tax Act (ITA) allows businesses to carry non-capital losses, which occur when a company loses money, back three years and forward twenty years. These losses are applied against past business income, reducing income taxes owed, resulting in a tax refund. If the losses cannot be fully used in the past three years due to insufficient business income, they can be carried forward until they are fully utilized, resulting in lower income taxes in future years. If a target company is experiencing financial difficulties, it may have a large balance of unused loss carryforwards with a low probability of being realized. If this company were acquired, the offeror could combine the target’s operations with its own. The likelihood of realizing the loss carryforwards would significantly increase as the offeror could now carry these business losses forward against the future profits of the larger revitalized business. In the past, offerors in unrelated businesses would buy companies to use their loss carryforwards and not continue operating the business. To prevent this abuse, the ITA now specifies that offerors can only use the target’s carryforwards if the target’s business continues and there is a reasonable expectation of profits in the future.

Tangible and intangible assets are also written up to reflect the higher prices usually paid for them in an acquisition. Capital cost allowance is calculated based on these higher values, which lowers the offeror’s taxable income.

**Facilitate growth.** External growth through M&A is generally faster and much safer than internal or organic growth. Internal growth requires the company to recruit new staff that may be in short supply; develop complex new technologies and management expertise; build additional production capacity; and take market share away from established competitors. External growth also limits new capacity, which reduces competition and helps raise prices. Due to supply and demand imbalances over the economic cycle, companies may find that the cost of buying existing capacity is lower than the replacement cost of building new capacity.

**Strategic planning.** M&A are invaluable to executives when implementing their strategic plans. They can be used to expand a product line quickly, enter a new market, or apply existing competencies to related fields in a congeneric merger. M&A allows companies to grow internationally; circumvent tariffs, quotas, and other trade barriers; follow their customers overseas; or secure low-cost labour in emerging markets. M&A help gain access to critical resources. Traditionally, these are natural resources like oil, natural gas, or metals, but they can also include intangible assets such as sales forces, distribution systems, new technology, or specialized skills such as product design or financial engineering.

**Reasons Not to Engage in M&A**

There are many legitimate reasons for engaging in M&A, but there are situations where they are not justified.

**Personal motives**. Executives have large egos, and many will pursue growth at any cost to make their companies bigger and more prestigious. Instead of paying out surplus cash as dividends or stock repurchases, they often recklessly expand through acquisition into more glamorous industries like the movies or high technology, where they have little expertise, thinking their superior management skills are easily transferable. Prestige may not be their only motive, as research shows executive pay is highly correlated with a company’s size and less so with its profitability.

**Unrelated diversification.** M&A that take companies into unrelated industries are referred to as conglomerate M&A, and the resulting company is called a conglomerate. These acquisitions are usually less profitable due to a lack of management expertise in the new field. Once the executives who proposed the expansion eventually leave the company or are terminated, the conglomerates often sell off these poorly performing business units and re-focus their operations on what they know best. They may do this themselves or be forced to do so when they are acquired in a take-over. Firms that specialize in disassembling poorly performing conglomerates are called “chop shops.” They find that the breakup value of the conglomerate is considerably higher than its current value as a going concern. In the criminal world, “chop shops” are where thieves disassemble stolen cars so the parts can be resold.

**Increase the sustainable growth rate.** A company may increase its sustainable growth rate by purchasing a cash cow. These are generally mature companies that produce more cash than the firm can profitably reinvest. Buying another firm to finance growth is a drastic measure, especially if the new company is in an unrelated industry where the offeror has little expertise.

**Diversify operations.** Companies sometimes justify buying a company in a new industry by saying they are diversifying operations to reduce risk and provide more stable returns for their shareholders. Shareholders can achieve the same diversification by buying shares directly in these companies themselves. The investments will also be better managed by leaving more knowledgeable staff in place.

**Maintain sales growth.**  If a company is having difficulty meeting stock analysts’ sales growth estimates through internal development, it may decide to buy growth using M&A. Increasing use of acquisitions is a potential warning sign that a company’s current sales growth rates are not sustainable.

**Take a company private.** A shareholder or management group may take a poorly performing company private to protect their positions in the firm. Private companies can also avoid the scrutiny of the public financial markets and are protected from being taken over by other firms that want to improve operations. Shareholders may benefit if a significant price premium is paid when the company goes private, but the efficiency of the economy falls due to a lack of market oversight.

**Tax deferral.** Surplus cash paid out as a dividend or stock repurchase is taxed when investors receive it. Management may acquire a company to defer taxation on these excess funds, but the large take-over premium paid when the company is purchased usually far exceeds any tax savings.

* 1. **| Types of M&A**

Companies can combine their operations using either a merger or an acquisition. The preferred method depends on the circumstances, so it is crucial to understand the advantages and disadvantages of each approach.

**Merger.** Two companies combine their operations by establishing a new legal entity that contains the assets and liabilities of both firms or by moving the assets and liabilities of one company into the other. The parties must reach a mutually acceptable agreement after a careful due diligence review of each other’s financial records. The shareholders of both companies need to approve the deal, usually by a two-thirds majority vote. If the two parties cannot agree, then one of the firms can approach the shareholders of the other company and try to convince them to vote in favour of the combination in a proxy fight. If they can get at least two-thirds of the shareholders to vote in favour of the combination, it can proceed. Under the Canadian Business Corporations Act (CBCA), any shareholder who does not agree to a successful combination may require that the merged company buy their shares at a fair price determined by an independent appraisal. CBCA is the act regulating federally incorporated companies in Canada.

**Acquisition.** The offeror purchases the shares of the target company for either cash or shares in the offering firm. A friendly take-over is when the target’s management supports the acquisition, and a hostile take-over is when they do not. M&A are usually friendly, but hostile take-overs receive the most media coverage. The offeror may buy less than 100% of the firm to save capital for other projects while still controlling the target for strategic reasons. If the offeror buys 100% of the target, they can follow up the acquisition with a merger to realize cost synergies from not maintaining two separate legal entities. If the offeror purchases 90% or more, they can force the remaining minority shareholders to sell under the CBCA, so the merger can still go through. The CBCA requires that the minority shareholders receive the same take-over bid. Offerors may choose to leave their targets as a separate legal entity even if they own 100% to facilitate the future sale or partial sale of the company once any operational problems are addressed or if the offeror’s business strategy changes.

**Cash offer.** No new voting shares are issued in the offering firm, so there is no potential loss of control. The offeror will also not have to share any of the synergies that are not already included in the take-over bid paid to the target. If the take-over premium is small compared to the total synergies and the offeror is confident in their synergy estimates, a cash offer would be preferred. Target shareholders also must pay taxes on any capital gains realized when their shares are purchased in a cash acquisition. This may cause them to negotiate a higher take-over bid, making the acquisition more expensive for the offeror. Instead of paying cash, offerors sometimes pay the target’s shareholders with debt or preferred shares in the offeror, but the purchase transaction is still taxable.

If the offeror does not have sufficient cash, they may have to borrow against the assets of the offering or target firm to finance the acquisition. When offerors borrow heavily against the assets of the target firm, it is referred to as a leveraged buyout (LBO). The bonds used to finance an LBO are generally not investment grade (i.e. below BBB) because of their higher financial risk and are called “junk” bonds. The effect of this higher debt burden is viewed differently by experts. Some feel it forces a poorly performing target company to be more efficient, lay off unneeded employees and close unprofitable business units. Others think it prevents targets from operating efficiently due to a lack of funds caused by high debt servicing requirements.

The offeror sometimes makes an overly generous bid for the target company, called a “bear hug,” to ensure its offer is accepted. If the target company’s management does not sell, this would expose them to potential legal action, given the significant losses that its shareholders would experience.

**Stock offer.** New voting shares in the offering firm are issued to the target instead of paying cash. This can lead to control problems for the offeror, but the offering or target firms will not be burdened by higher debt. If the two companies are both Canadian, any capital gains resulting from a stock acquisition are not taxable until the new shares in the offeror are eventually sold by the target’s shareholders, providing a tax deferral. Stock acquisitions are usually preferred by offerors when their shares are overvalued because they must issue fewer new shares to the target. A stock acquisition also allows the offeror to share risks with the target when synergy estimates are uncertain.

**Mixed offer.** Compensation paid to the target firm is sometimes a mixture of cash and the offeror’s stock. Many times, an offeror will start the bidding process by proposing an all-stock deal. If other offerors make a bid or the target’s board of directors resists the take-over, the offeror may reduce the stock portion of the bid and substitute cash. Target shareholders may prefer the certainty of cash over stock, especially if the take-over synergies are uncertain or the offeror’s share is overvalued. A mixed offering can also address some of the concerns of an all-cash or all-stock deal, such as loss of control or excessive debt.

**Acquisition of assets.** Offerors may decide to purchase specific assets of a target firm instead of the entire company. This saves them the trouble of selling off or closing the parts of the business they do not want. Targets could also have liabilities, exposures to potential litigation, or union difficulties that the offeror seeks to avoid. Finally, offerors may foresee problems buying the entire target company because of a substantial minority interest that will resist the sale. If the offeror purchases most of the target’s assets, the courts may decide that they are buying the entire firm and assign them the liabilities as well to protect the creditors.

* 1. **| Take-over Bids**

Until recently, securities regulation in Canada was a provincial jurisdiction where each province had its legislation. Most countries, including the U.S. through its Securities and Exchange Commission (SEC), have recognized that national securities regulation is more effective given that public companies typically raise funds in several jurisdictions. Despite this, provincial governments were unwilling to give up their authority, although they did agree to form the Canadian Securities Administrators (CSA). This is a national body composed of federal, provincial, and territorial governments that prepares national policies relating to securities regulation. These national policies are usually adopted and implemented by each province’s securities commission with few or no modifications. In a November 2018 decision, the Supreme Court of Canada finally gave the federal government the power to establish a national securities regulator, but there has been limited progress to date. The Supreme Court also indicated that the federal and provincial governments should continue to work together cooperatively.

CSA recognizes the vital role take-over bids play in the economy as a source of management discipline and a means of efficiently reallocating economic resources. In regulating take-over bids, CSA’s primary concern is protecting shareholders and providing a fair and transparent process that allows them to make a fully informed decision about the sale of their securities. National Policy 62-104 Take-over Bids and Issuer Bids provides rules relating to take-over bid disclosure and the bidding process.

**Take-over Bid Disclosures**

A formal take-over bid circular must be sent to all shareholders when an offeror attempts to acquire shares in a target company that will result in the offeror’s total ownership stake being 20% or more of the shares of the target company, including any shares the offeror already owns. The take-over bid circular is signed by the offering company’s CEO, CFO, and at least two members of its board of directors. Accountants should recognize that 20% or more ownership is the level at which a company typically acquires significant influence over another firm under International Financial Reporting Standards.

A sizeable price premium is typically paid by an offeror when they acquire a controlling interest in a target company, so the current shareholders, management, and other potential investors must have complete information relating to any potential take-over bids. As part of an early warning system for investors, a share purchase by a domestic investor that exceeds 5% in total over 12 months (or 10% for foreign investors) must be disclosed publicly. When an investor’s ownership share exceeds 10%, it must be disclosed publicly along with each subsequent 2% increment in ownership.

A popular investment strategy is to search out companies that are likely take-over targets and invest in them early to realize the price premium. Sometimes the target’s share price begins to rise before the public announcement of the take-over bid as rumours spread. Investors should be careful not to trade based on any material, non-public information they receive about a potential take-over, or they may be found guilty of insider trading.

**Take-over Bid Process**

The steps in the take-over bid process include:

1. The target company provides a list of all security holders to the offeror so the circulars can be distributed.
2. Take-over bid circulars are sent to all shareholders and share rights or options owners who are given at least 105 days to respond to the bid.
3. The circular includes the bid price, whether it will be paid in cash and/or stock, and the percentage ownership the offeror plans to acquire. The bid must be the same for all security holders, and all financing must be in place before the start of the bid process to ensure the offeror can fulfill its obligations.
4. The offeror cannot buy target company shares, rights, or options during the bid period.
5. The Offeror cannot pay more than the quoted price, and the same price must be paid for all securities purchased 90 days before or 20 days after the bid period to ensure the fair treatment of all investors.
6. Variations to the take-over bid circular can be made during negotiations between the offeror and the target. Security holders must be notified of any changes and given at least 35 days from the date of the change till the revised bid closes.
7. The stock exchange maintains a record of all securities offered for sale.
8. Shares offered up for sale can be withdrawn before the end of the bid period.
9. If more securities are offered up than sought, the offeror can either buy all the securities offered up or only purchase the securities sought on a prorated basis.
10. If an insufficient number of securities are offered up, the offeror may withdraw the take-over bid, or they may continue with the purchase and try to increase their ownership to the desired level with another bid in the future.
11. Targets must send a directors’ circular to all security holders within 15 days of the take-over bid being received. In this document, they recommend acceptance or rejection of the bid. They may also state that they cannot comment at this time but will provide an opinion later once they have completed their review. This must be done at least seven days before the end of the bid period. Any changes to the directors’ circular must be reported to security holders before the end of the bid period.
12. Directors’ circulars typically include an investment report called a fairness opinion from a valuation expert commenting on the reasonableness of the bid price. Reports from experts can only be included with their consent.
13. Individual directors can also send additional circulars to security holders if they disagree with the opinion of the board of directors.
14. Directors must disclose any benefit granted or to be given for loss of their position if the bid goes through, so security holders are aware of any conflicts of interest.
    1. **| Take-over Defences**

The continuous threat of being taken over pressures a company’s management to reduce agency costs to maximize its share price. If the share is not trading near its maximum, buyout firms specializing in corporate take-overs have a strong incentive to acquire the company, fix its problems, and resell it at a much higher price.

Take-over defences are actions undertaken by target firms to impede a take-over. Sometimes they are used by managers of poorly run companies to protect their positions. They are also used by shareholder groups like a company’s founders to maintain control. In these instances, the defences are not in the best interest of the company or the economy. In other cases, managers do not use them to protect their jobs or maintain control, but to “play hard to get” to secure the highest take-over bid possible for shareholders.

Governments and regulatory bodies recognize that the interests of the target firm’s management and shareholders may differ concerning take-over defences. CSA’s National Policy 62-202 Take-over Bids – Defensive Tactics states their primary concern is the “protection of the bona fide interests of the shareholders of the target corporation.” They will strike down defences if the rights of shareholders are violated.

Managers and shareholder groups, with the help of highly skilled investment bankers and lawyers, do try to impede corporate takeovers by implementing a variety of takeover defences. These defences can be implemented either before or during a take-over attempt. Establishing a strong defence beforehand is recommended as it is less likely to be challenged by regulators or the offeror in the courts. Defences include:

**Just say no.** Management can convince its board of directors and shareholders that the take-over is not in their best interests. They say the bid is too low or the shares to be received in a stock swap are overvalued. Unions, community groups, politicians, customers, and suppliers are recruited to help them, and excessive litigation is used to slow down the take-over process.

**Find a better offer.**  If a company is fearful of a potential offeror because of the actions they might take, like replacing existing management, they may try to find another offeror, or “white knight,” who is more likely to leave them in place. This will also create more competition for the target company, leading to a higher take-over bid. If the white knight is smaller in size and only able to buy a minority stake in the company to help discourage the take-over, they are called a “white squire.” White implies goodness, and squires were the shield and armour bearers of knights during the Middle Ages.

**Buy the offeror.** Management may discourage an acquisition by threatening to take over the company that is attempting to buy it. This is called a reverse take-over strategy or a Pac-Man defence after the popular video game. The offeror is discouraged from going forward with the acquisition due to the potential for a long legal battle. This type of defence is not common and is only taken seriously if the target company has sufficient financial resources to follow through with its threats.

**Standstill agreements.** Management may prevent a take-over by negotiating a targeted repurchase of the offeror’s shares only at a significant price premium to eliminate their opposition. This is called “greenmail” and is prohibited by securities regulators in Canada as it is a form of bribery and not in the best interest of all shareholders. Standstill agreements may still be entered into for other consideration, like a seat on the board of directors, to provide the offeror with an avenue to express their concerns about the company’s performance.

**Anti-takeover amendments.** A company’s corporate charter can be modified to impede take-overs in different ways. (1) A supermajority voting provision stipulates that two-thirds or more (i.e. not the standard 50%) of the shares, excluding those already owned by the offeror, are needed to approve an acquisition. (2) Hostile investors who recently purchased large blocks of shares are prevented from voting their shares without the permission of the board. (3) Staggered director elections prevent potential offerors from quickly gaining positions on the board of directors to influence the take-over decision. (4) A fair price amendment stipulates a formula for calculating the take-over bid that usually results in a higher price that must be paid to all classes of shareholders regardless of their voting rights. These amendments 1) prevent offerors from reducing the cost of a take-over by buying the voting shares only, 2) protect shareholders from take-over bids made during temporary market declines in the target’s share price, and 3) generally make the takeover more expensive. Anti-takeover amendments are sometimes referred to as “shark repellent.”

**Sell desired assets.** An offeror may buy a target company to gain access to specific assets like patents or real estate leases and then sell off the unneeded portions of the business once the acquisition is completed. Management may prevent the take-over by selling these key assets to either the offeror or other investors first. This will likely hurt the company’s long-term growth prospects and its share price, but management positions will be secure. This practice is called “selling the crown jewels” or a “scorched earth strategy.” The scorched earth strategy is the practice of retreating armies destroying resources such as food or transportation infrastructure so they cannot be used by the enemy.

**Shareholder rights plans.** To make take-overs less attractive, a company can modify its corporate charter so its management can issue a special type of common share right to its shareholders. These rights allow shareholders, excluding the offeror, to buy additional shares in the target at a substantial discount only when an offeror announces a take-over bid or acquires a certain percentage of the company. This has the effect of significantly diluting the target’s share price and makes the acquisition much more expensive for the offeror. This is referred to as a “poison pill” with a flip-in provision and can usually be cancelled by the target if the take-over becomes friendly and management wants shareholders to accept the offer. Poison pills can also have flip-out provisions that allow the target’s shareholders, excluding the offeror, to buy shares in the offering firm at a substantial discount if the acquisition is completed, which will dilute the offeror’s share price. Sometimes, an offeror will try to secure enough board seats before a take-over to cancel a poison pill. To prevent this, a “dead-hand” provision may be employed that only allows continuing directors who were on the board before the take-over bid to vote on whether to cancel a poison pill. In Canada, shareholder rights plans are reviewed by securities regulators and will be stricken down if they are not in the best interest of shareholders. Their main advantage is that they delay the take-over process, giving new bidders a chance to make a higher offer.

**Issuance of retractable bonds.** Target companies can see their debt levels rise dramatically after a take-over, as many offerors borrow heavily against the target’s assets to finance the acquisition. This higher level of financial risk hurts the existing bondholders, so their bond indenture typically has a provision allowing them to resell their bonds to the company at par or a premium if there is a change in control. This feature, called a “poison put,” raises the cost and uncertainty of the acquisition since the offeror will have to refinance the entire firm.

**Generous severance payments.** Upper-level, mid-level, and lower-level management may receive generous severance pay benefits that are paid out when a company is acquired. These benefits are referred to as “golden, silver, and tin parachutes,” depending on the level of management. Not only do these high payouts make take-overs more expensive, but they encourage senior managers to stay and fight any acquisitions instead of seeking employment elsewhere, knowing they will be well compensated even if they are unsuccessful.

**Increase management and employee ownership.** Managers and employees are fearful of acquisitions as layoffs, plant closures, and other restructuring measures frequently accompany them. Encouraging management and employees to buy more shares through stock options or employee ownership plans makes acquisitions more difficult. Management can also negotiate significant cross-holdings of shares with other friendly corporations so they can support each other during any take-over attempts.

**Establish control blocks and dual-class shares.** Many of Canada’s largest corporations are controlled by their founding families using dual-class shares. These families may own less than 50% of the company but maintain a control block by issuing subordinate voting (i.e. fewer votes per share than the founder’s shares) or non-voting shares to other shareholders. This allows the company to raise needed equity from these investors while greatly limiting their right to vote. Many countries and stock exchanges do not permit dual-class shares as they violate the principles of good corporate governance, leading to higher agency costs. The federal government appears to support their use as they help to protect high-profile, family-owned Canadian companies from being acquired by foreign firms.

**Increase financial leverage.** Many acquisitions are financed by borrowing heavily against the target’s assets. A target firm can intentionally increase its use of financial leverage before any take-over attempt by issuing large dividends, repurchasing a significant number of shares, or buying another firm itself. Any potential offerors will have difficulty securing sufficient funding because of the added leverage. Using a “fat man” strategy, management might also buy a large, poorly performing company that makes any future turnaround by an offeror more difficult.

**Maximize share price.** Eliminate potential synergies by improving growth projections, making optimal use of financial leverage, avoiding unprofitable diversification, paying out excess cash balances as dividends or stock repurchases, increasing the regular dividend, selling off underperforming divisions, or even hiring a public relations firm to improve the company’s image. Offerors will lose interest if a company has few potential synergies.

**Go private.** A shareholder or management group can defend their position by buying out the other shareholders and delisting the company, thus preventing any offerors from making a public take-over bid. When management takes a company private, it is called a management buyout (MBO) or a leveraged buyout (LBO) if management borrows heavily against the target’s assets due to a lack of capital. Sometimes, employee groups such as unions take a company private to save their jobs and pensions in an employee buyout.

**Raise antitrust concerns.** Under the federal Competition Act, the Mergers Branch of the Competition Bureau reviews all M&As in Canada to assess whether they will substantially lessen competition. If it is felt they will, the government may disallow the transaction or order changes to address any concerns. Target companies or other groups, such as employees, customers, or competitors, may appeal to the government to act in their favour.

**Raise nationalist or security concerns.** Under the federal Investment Canada Act, the Foreign Investment Review Agency reviews most new investments or acquisitions of existing Canadian companies by foreign firms. These transactions are only approved if they have a net benefit to Canada and are not injurious to national security. Investments by government-controlled corporations from unfriendly nations such as China or Russia are more scrutinized.

* 1. **| Calculating a Take-over Bid**

The discounted cash flows or market multiples models are used to analyze M&A. A take-over bid range with lower and upper limits is established based on whether the offeror or target receives the estimated synergies. The exact take-over bid depends on the negotiating skills of the parties, the strength of the target’s take-over defences, and whether any competing bids are received.

The take-over bid can be paid in either cash or stock. If the stock is used, an exchange ratio is calculated that indicates how many shares of the offering firm will be issued for each share of the target company. As discussed, targets should be wary of offerors using overvalued shares to reduce the number of new shares they must issue in a stock or mixed offer.

**Discounted Cash Flows**

When using the discounted cash flows method to determine the upper price limit, offerors should add the estimated annual after-tax synergies to the current annual after-tax cash flows of the target. They should also add any tax savings from loss carryforwards that can now be utilized and deduct any after-tax advisory costs relating to the M&A. The discount and tax rates used should reflect the riskiness and effective tax rate of the target and not those of the offeror. Also, if the offeror plans to change the target’s capital structure (i.e. weights of debt and equity) after the M&A, the beta used to calculate the target’s cost of equity should be adjusted using the formula:

BLevered = BUnlevered (1 + (1 − t) (

B – Beta

t – Effective tax rate

D/E – Debt-to-equity ratio

**Market Multiples**

When using market multiples to determine the upper price limit in the M&A, the offeror can use either the comparable company or the comparable transaction approach. With the comparable company approach, the offeror first values the underlying target company using market multiples. To incorporate the estimated synergies, the offeror then calculates an average take-over premium based on recent take-over transactions available through different information sources such as FactSet Mergerstat Review.

The comparable transactions approach values the target directly using recent take-over transactions only. In one step, these market multiples are used to value both the underlying target company and any take-over premium.

**Preferred Method**

Some users prefer the discounted cash flows model because it allows the offeror to incorporate better the company’s plans, estimated synergies, and any changes to the target’s capital structure or effective tax rate. However, it can include unreliable assumptions and estimates of key inputs, such as the growth and discount rates, that significantly affect the results.

Other users prefer the market multiples model as it is based on current market data from comparable companies and transactions. This information is readily available and objective so that it can be more easily defended to all parties, including the courts. If the comparable companies or transactions are not representative, the results will be distorted.

When using market multiples, the comparable company approach is considered more accurate than the comparable transaction approach because it first values the underlying company without synergies using other closely related peers. Once a fair value for the underlying company is established, then take-over transactions are used to estimate the take-over premium. The offeror must ensure these transactions are recent, not outliers, sufficient in number and value, reflective of the target company’s industry, and not collected when stock markets were significantly over- or undervalued. In practice, meeting these requirements is difficult.

With the comparable transaction approach, the take-over transactions are used to value both the company and the take-over premium together. The companies that these take-over transactions relate to are usually not as representative of the target as those used in the comparable company approach when valuing the underlying firm, leading to more unreliable valuations.

* 1. **| Evaluating the Division of Synergies**

Offerors and targets can evaluate the division of synergies in M&A transactions using the following formula:

VA = VB + VT + S – C

VA – Value of the offeror post-M&A

VB – Value of the offeror pre-M&A

VT – Value of the target

S – Synergies

C – Cash paid to the target

**Example**

|  |  |  |
| --- | --- | --- |
|  | **Offeror** | **Target** |
| Pre-M&A stock price | CAD 14 | CAD 9 |
| Number of common shares | 70 | 25 |
| Pre-M&A market value | CAD 980 | CAD 225 |
| Synergies | CAD 95 | |

Cash offer – CAD 10.00 per share

Stock offer – 0.75 shares of the offeror for one target share

Mixed offer – CAD 5.00 per share, 0.35 share of the offeror for one target share

|  |  |
| --- | --- |
| **Offeror’s Perspective** | |
| **Cash Offer** | |
| VA = 980 + 225 + 95 – (10) (25)  VA = 1,050  1,050 / 70 = 15 | The offeror had 70 shares worth CAD 14 each before the takeover, which is worth CAD 15 after, for a gain of CAD 1.00. He received CAD 70 (70 shares x CAD 1.00 gain) of the CAD 95.00 in synergies. The remainder went to the target. |
| **Stock Offer** | |
| VA = 980 + 225 + 95 – 0  VA = 1,300  70 + (0.75) (25) = 88.75  1,300 / 88.75 = 14.65 | The offeror had 70 shares worth CAD 14.00 each before the takeover, worth CAD 14.65 after, for a gain of CAD 0.65. He received CAD 45.50 (70 x CAD 0.65) of the CAD 95.00 in synergies. The remainder went to the target. |
| **Mixed Offer** | |
| VA = 980 + 225 + 95 – (5) (25)  VA = 1,175  70 + (0.35) (25) = 78.75  1,175 / 78.75 = 14.92 | The offeror had 70 shares worth CAD 14.00 each before the takeover, worth CAD 14.92 after, for a gain of CAD 0.92. He received CAD 64.40 (70 x CAD 0.92) of the CAD 95.00 in synergies. The remainder went to the target. |
| **Target’s Perspective** | |
| **Cash Offer** | |
| Received CAD 10.00 cash for each of the 25 shares | The target received CAD 10.00 for each of the 25 shares previously worth CAD 9.00. He received CAD 25.00 (CAD 1 x 25.00) of the CAD 95.00 in synergies. The remainder went to the offeror. |
| **Stock Offer** | |
| Received a 0.75 partial share in the offeror worth CAD 10.99 (0.75 X CAD 14.65) for each of the 25 shares in the target | The target received CAD 10.99 for each of the 25 shares previously worth CAD 9.00. He received CAD 49.75 (CAD 1.99 x 25) of the CAD 95.00 in synergies. The remainder went to the offeror. |
| **Mixed Offer** | |
| Received CAD 5.00 cash plus a 0.35 partial share in the offeror worth CAD 5.22 ((0.35) (CAD 14.92)) for each of 25 shares in the target for a total of CAD 10.22 (CAD 5.00 + CAD 5.22). | The target received CAD 10.22 for each of the 25 shares previously worth CAD 9.00. He received CAD 30.50 (CAD 1.22 x 25) of the CAD 95.00 in synergies. The remainder went to the offeror. |
| **Note: The synergies of the offeror and target add up to CAD 95.00 for the cash, stock, and mixed offers. Small differences are due to rounding errors.** | |

* 1. **| Success of M&A**

M&A occur because of the synergies that can be earned by combining the operations of two companies. The success of M&A from the target or offeror’s perspective depends on 1) the portion of the estimated synergies each party receives based on the agreed-upon take-over bid, and 2) whether the estimated synergies are realized. The risk of not realizing synergies is shared in a merger as both the target and offeror receive shares in the combined firm. If these synergies are not realized and the share price falls, both parties suffer. The same is true in a stock acquisition, but in a cash acquisition, only the offeror is hurt since the target is paid in cash.

**Track Record**

Industry research indicates that target firm shareholders receive sizeable take-over premiums compared to the pre-announcement price of their shares. The premium averages 20% for mergers and 30% for acquisitions. Acquisitions return more than mergers because of the hostile nature of the take-over process. Stock acquisitions are less profitable than cash acquisitions because 1) stock swaps are used when the offeror’s share is overvalued, 2) offerors pay more in cash acquisitions to compensate for taxes, and 3) cash take-over bids are used to prevail in bidding competitions between offerors as cash is more appealing to target firms.

Industry research also indicates that offerors lose money in M&A on average. When an offering firm announces an acquisition, its share price usually falls as the market does not feel it will be a profitable transaction. In the longer term, the performance of an offeror also lags its industry peers. This is due to the very competitive nature of the M&A market, where the offeror must pay all the estimated synergies to the target to be successful. When the actual synergies realized turn out to be considerably less than the amounts estimated, the offeror loses money on the transaction in what is called the “winner’s curse."

The winner’s curse can be explained by agency theory. Instead of acting in the best interest of shareholders, managers are:

* More interested in completing a take-over deal than making a profit and overestimating synergies to justify whatever take-over bid is needed to prevail.
* Overconfident in their ability to accurately estimate synergies, resulting in higher take-over bids.

* Focused on empire-building where their egos dominate. The goal of the firm is no longer to maximize its share price but only to become bigger and more powerful, and enter new industries that raise the CEO’s pay, perks, and personal profile.
* Able to hide unsuccessful M&A more easily because the target is usually much smaller than the offeror.

**Successful M&A**

The key to a successful M&A is not to overpay for the target company, especially when stock markets are overvalued. Offerors should discipline themselves only to buy companies when prices are down; objectively estimate synergies; adhere to strict take-over bid maximums; be prepared to walk away from negotiations if prices become inflated or the number of other bidders becomes too high; and question the wisdom of M&A if the stock market reacts negatively to the announcement by bidding down its share price.

Offerors should also ensure that the target company is a good strategic fit for their organization and that they are not venturing into an unrelated industry where they lack expertise. This includes determining whether the target has a similar organizational culture or if joining the two companies will be problematic, as valuable employees like scientists or engineers become disgruntled and leave to pursue other options. Once shareholders approve the M&A, management must act quickly and decisively to combine operations, but also be fair and not unilaterally impose their people on the new company, thus alienating existing employees.

* 1. **| Other Forms of Corporate Restructuring**

Besides M&A, there are other actions management can take to restructure a company’s operations to improve its performance and maximize its share price.

**Divestitures**

Divestitures occur when a company sells off specific assets such as land or patents, a product line, or an entire business unit to new owners. There are three ways to divest operations:

**Sell-off.** Specific assets, a product line, or a business unit are sold to another company.

**Equity carve-out.** A business unit is established as a separate legal entity, which is then taken public in an initial public offering (IPO). Equity carve-outs are used when no company is interested in buying the business unit directly, or it is felt that a higher price can be received in an IPO.

**Liquidation.** If an interested buyer cannot be found, a product line or business unit might be closed, and the assets sold on a piecemeal basis, possibly as part of a formal bankruptcy.

There are several reasons why a firm may choose to divest part of its operations:

* Refocus on its core business and reverse previous strategic decisions to expand into unrelated fields where the company lacked the expertise to succeed.
* Redeploy investment capital into faster-growing, more profitable businesses.
* Sell to another company that has the technological and financial resources to succeed and will share potential synergies with the target by paying a substantial premium.
* Outsource production to more efficient producers, allowing the company’s existing facilities to be sold.
* Sell the unneeded parts of a business acquired in a recent M&A to help pay for the acquisition.
* Pay down excessive debt built up during previous acquisitions or expansions to avoid financial distress.
* Sell part of a business when stock markets are overvalued to realize the best possible price for shareholders.
* Sell the crown jewels as a take-over defence.
* Comply with government conditions for the approval of an M&A that specify the company must divest part of its operations to a third party to ensure there is adequate competition in a product market or geographical region.
* Sell a poor-performing or undervalued business unit to a management group that wants to attempt a turnaround.

**Spin-offs, Split-outs, Split-ups**

Spin-offs, split-outs, and split-ups all involve moving some portion of a company’s assets and liabilities into one or more new companies, but the ownership structure varies after restructuring.

**Spin-off.** A portion of the assets and liabilities of the original company is placed in a new company. Existing shareholders are given the same prorated share ownership in the new company as they have in the original company.

**Split-out.** A portion of the assets and liabilities of the original company is placed in a new company. Some shareholders receive shares in the new company in exchange for their shares in the original company, allowing them to take control of a specific part of the firm.

**Split-up.** All the assets and liabilities of the original company are divided among two or more new companies, and the existing shareholders are given the same prorated share ownership in each of the new companies as they had in the original company. The original company ceases to exist.

There are several reasons why a company may spin off or split out part of its operations or split up the entire firm, including:

* Provide greater autonomy to a business unit so it can be managed more effectively compared to when it was part of a larger diversified company.
* Use stock options in the new business unit instead of the diversified company to better reward management performance in that unit.
* Eliminate the effect of a poorly performing business unit from the company’s overall results to address shareholder complaints and give them the option to sell their shares in this unit.
* Receive a price premium from stock analysts for being a pure play instead of part of a diversified company. Pure plays can be more accurately valued due to their simplified operations, and they usually focus on just one industry, allowing investors to allocate capital to different areas of the economy more precisely.
* Remove unwanted business units from a target firm before an acquisition to produce a more focused company that will likely receive higher take-over bids from potential offerors.

Industry research shows that the stock market initially reacts favourably to divestitures, spin-offs, split-outs, and split-ups and that the financial performance of both the parent company and the discarded unit improves. This is especially true when the company reverses previous conglomerate mergers into unrelated fields.

**Tracking Shares**

Tracking shares are created when a company’s operations are divided into two or more business units, and a share price is estimated for each unit based on its profits. These share prices are used to construct separate stock option plans for each business unit that better measure management’s performance compared to a stock option plan that is based on the company’s overall share price.

With tracking shares, unlike a spin-off, management retains the operating, financial, and taxation synergies of being one larger company since no business unit is spun off. For instance, centralized services such as accounting, human resources, and legal can be shared; lower interest rates can be negotiated due to greater negotiating power; and loss carrybacks and carryforwards can be applied to more business income. A problem with tracking shares is that business units can waste considerable resources arguing over the cost allocation and internal transfer pricing arrangements used to determine the profit of each unit.

* 1. **| Corporate Restructuring at Canadian Companies**

As discussed, M&A and other forms of corporate restructuring are essential if the economy is to remain efficient and managers are to maximize their firm’s share price. Nutrien, Aecon Group, Hudson’s Bay Company, and Bombardier provide practical examples of the different motives companies have for restructuring their operations.

**Nutrien**

Nutrien is a Canadian fertilizer manufacturer based in Saskatoon with over 1,700 retail stores, 500,000 grower accounts, and 20,000 employees in 14 countries. It is the world’s largest producer of crop nutrients, which include potash (potassium), nitrogen, and phosphate fertilizers. Nutrien leads the global industry in potash production and is third in nitrogen capacity.

Nutrien was formed in January 2018 through the merger of Potash Corporation of Saskatchewan and Calgary-based Agrium. This agreement allowed the new company to limit industry capacity and stabilize prices in response to a depressed fertilizer market caused by a ramp-up in world production and the break-up of a Russian-Belarus potash cartel. Nutrien also combined Potash Corporation’s strength in mining with Agrium’s industry-leading global retail network and generated cost synergies of CAD 500 million in the first year. To capitalize on its retail network, Nutrien plans to expand sales of related farm products such as seeds, pesticides, and other farm supplies.

The Saskatchewan government initially owned Potash Corporation, but it was privatized in 1989 and subsequently grew by purchasing several smaller producers. Investment Canada denied a 2010 take-over bid by Australia-based BHP Billiton because it did not provide a net benefit to Canada. The Saskatchewan government was concerned about a potential loss of tax revenues and felt potash was a strategic resource that Canada should control. In 2015, Saskatchewan Potash offered to purchase the Canadian assets of K+S AG, a German producer, so that they could limit output at its new mine, but the offer was turned down.

Under the merger agreement, Potash Corporation and Agrium investors would receive 0.4 shares and 2.23 shares in Nutrien for each of their shares. This gave Potash Corporation and Agrium shareholders 52% and 48% of the new company in what was termed a “merger of equals.” Agrium’s CEO was to become the CEO of Nutrien, and Potash Corporation’s CEO would be the chairman of the board of directors. An initial agreement was reached in September 2016, but it took until January 2018 for competition regulators in Brazil, Canada, China, India, Russia, and the U.S. to give their approval. Brazil and Russia were quick to agree, as was Canada’s Competition Bureau, which issued a no-action letter, meaning they did not feel the merger would substantially lessen competition. They indicated that there was little overlap in the assets of the two companies that would limit competition. It was felt that the merger of Potash Corporation and Agrium would also serve as a defensive measure against any future takeover attempts from outside Canada.

Approval from the U.S., China, and India was critical as they were major potash customers. China and India approved the merger but required that Nutrien divest its international operations in the Middle East, Israel, and China to increase competition. China also asked for Nutrien’s continued commitment to Canada Potash Exporters (Canpotex), which manages all of Saskatchewan's potash exports outside of the U.S. and is jointly owned by Nutrien and U.S.-based Mosaic. The U.S. Federal Trade Commission was concerned about the increase in market concentration with only two major fertilizer producers in North America (Nutrien and Mosaic), but they gave their approval conditional on Nutrien selling U.S. assets in Ohio and Colorado to create more competition in the super phosphoric and nitric acid markets.

The Saskatchewan government was concerned about the location of Nutrien’s headquarters, given that Agrium was based in Calgary and Potash Corporation had promised to maintain its head offices in Saskatchewan when it was privatized in 1989. Nutrien agreed to locate them in Saskatoon, where it would build a major new office complex. Considerable operations would remain in Calgary.

**Aecon Group**

Aecon Group is Canada’s 4th largest construction firm with revenues of CAD 3.3 billion in 2018. The Calgary-based company serves both public and private clients across three business segments, including infrastructure, industrial, and concessions. Industrial is the largest segment, focusing primarily on mining and energy projects. The company has a limited international footprint with only 7% of its sales outside Canada.

In August 2017, Aecon announced that it was interested in being acquired by a large international construction firm to provide it with the global exposure, expanded business connections, and capital necessary to bid on larger, more complex projects outside Canada. By October 2017, Aecon received a CAD 1.5 billion offer at CAD 20.37 per share from China Communications Construction Company (CCCC). This offer was a 50% premium over Aecon’s August 2017 share price and was quickly approved by Aecon’s board of directors and shareholders, but it did raise concerns among competitors and politicians. Industry groups complained about unfair competition from China, while politicians felt national security was at stake after two recent purchases of major Canadian companies by Chinese firms.

Under Canadian law, the Aecon acquisition had to be approved by the Competition Bureau and Investment Canada. The Competition Bureau gave a no-action letter indicating it would not substantially lessen competition. In May 2018, after several extensions and considerable pressure from opposition parties, the federal government issued an order under the Investment Canada Act instructing Aecon not to proceed with the acquisition. They did not provide reasons, but it was felt their denial was based on national security grounds given Aecon’s defence and nuclear contracts in Canada and the Chinese government’s 63% ownership stake in CCCC.

Aecon complained the government’s decision would limit its ability to expand internationally, but said it would respect it. In September 2018, Jean-Louis Servranckx replaced John Beck as CEO and announced the company would now focus on addressing its growing backlog of domestic contracts and expanding its infrastructure business, considering recent government spending announcements. Aecon established a goal to become Canada’s largest infrastructure construction company. It also adopted a One Aecon strategy to “capitalize on and combine the strengths and synergies” of the entire company instead of operating as separate business units. To focus on construction, Aecon sold its contract mining business to Edmonton-based North American Construction Group for CAD 199.1 million in 2018. Finally, Aecon indicated further domestic or selective international acquisitions were likely given the new CEO’s considerable overseas experience.

**Hudson’s Bay Company**

Hudson’s Bay Company (HBC) was incorporated on May 2, 1670, and is North America’s oldest corporation. For its first 200 years, it helped to open Western Canada through its management of the fur trade. After the founding of Canada in 1867 and the Province of Manitoba in 1870, HBC ceded its control over Western Canada and evolved into Canada’s last remaining department store chain.

HBC used M&A and other forms of corporate restructuring throughout its life to adapt to significant trends in retail management, including the growth and decline of the department store concept, the rise of discount and specialty stores, the expansion of online shopping, and the growing importance of luxury products. Like its former competitor, Sears, HBC will probably go bankrupt in the future because of its inability to adapt to the changing retail environment. The main factor contributing to its likely demise is its management’s preoccupation with financial gamesmanship instead of effectively managing its operations. Basic elements of good retailing, such as strong merchandising, superior customer service, and store cleanliness, were ignored in favour of their latest financial strategy. The following table summarizes the corporate restructuring measures undertaken at HBC since 1960:

|  |  |
| --- | --- |
| **1960s** | Developed into a national department store chain by purchasing Morgan’s in Eastern Canada. |
| **1972** | Purchased Shop-Rite, a catalogue store chain that had customers select products from catalogues at the front of the store before retrieving them from the warehouse in the back. This was a predecessor to online shopping that closed due to declining sales in 1982.  Acquired Freiman’s department store in Ottawa. |
| **1978** | Zellers, a Canadian discount chain, attempted to buy HBC, but HBC purchased Zellers in a reverse takeover.  Acquired the Simpson’s department store chain. |
| **1979** | Kenneth Thomson, a Canadian billionaire investor, purchased 75% of HBC for CAD 400 million in a take-over battle with George Weston Ltd., a Canadian food processing and retail giant. Thomson sold off many of HBC’s unrelated assets, such as oil & gas for CAD 550, allowing the company to focus primarily on retail. |
| **1980s** | Reduced debt levels by selling the remainder of its oil & gas assets as well as its fur auction business and Northern Stores Division that serviced remote Canadian communities. |
| **1990s** | Expanded its Zellers discount chain by purchasing Towers department store in 1990, Woodward’s in 1993, and Kmart’s Canadian locations in 1998. |
| **2006** | Jerry Zucker, an American businessman, purchased the shares of HBC after a protracted takeover battle that involved HBC and competing bids from Onex and other Canadian buyout firms. After the acquisition, HBC’s senior management was dismissed, and the company was taken private. Zucker planned to sell selected real estate assets to raise cash, go ahead with planned management cuts, and reinvest in Zellers, which was losing sales to Walmart. |
| **2008** | After the unexpected death of Jerry Zucker, HBC was sold to NRDC Equity Partners, a New York-based private equity firm with retail expertise. They planned to transform HBC into a more upscale retailer. |
| **2011** | Unable to compete with Walmart, HBC sold most of its Zeller store leases to Target to help them enter the Canadian market, although Target withdrew after only two years. A few Zeller’s stores remained open until January 2020. The proceeds were used to pay down debt and help purchase a U.S. luxury department store chain, Lord & Taylor. |
| **2012** | HBC, including Lord & Taylor and Home Outfitters, was taken public again by NRDC equity partners on the Toronto Stock Exchange. Proceeds from the IPO were used to pay down debt and revamp store locations. |
| **2013** | Purchased the luxury retailers Saks Fifth Avenue and Saks Off Fifth with operations in the U.S. and Europe, and announced plans to open some stores in Canada. |
| **2015** | Purchased German department store chain Galeria Kaufhof and its Belgian subsidiary. |
| **2016** | Purchased a bankrupt Dutch department store chain, and it rebranded as HBC. |
| **2016** | Purchased online flash sales site Gilt Groupe as part of a further expansion into online sales. |
| **2017** | Considered purchasing struggling retailers Macy’s and Neiman Marcus, but did not proceed. |
| **2018** | Credit and debit card information for over 5 million customers at Saks and Lord and Taylor was stolen in one of the largest data breaches in U.S. retail history. |
| **2019** | Closed its Dutch operations and sold its assets in Germany.  Sold Lord and Taylor to Le Tote for cash and equity in Le Tote.  Real estate companies began to contemplate how to respond to losing HBC as a mall anchor. Many of their old Sears locations were still vacant as they considered new options to fill the space, like fitness clubs, movie theatres, new grocery and specialty stores, and office and even residential developments. Other retailers like Payless Shoes, Forever 21, and Barney’s also filed for bankruptcy.  Announced a Q2 loss of CAD 984 million, consisting of a loss from continuing operations of CAD 462 million and a loss of CAD 522 million from discontinued operations. Cash from operations was CAD -423 million.  The shareholder group led by Executive Chairman Richard Baker, who already owned 57% of HBC, reached an agreement with the board of directors to buy the remaining shares for CAD 10.30 cash and take the company private to avoid public scrutiny while it attempted to restructure operations. The minority shareholders will likely approve the bid by year-end after the group raised its take-over bid in response to complaints from minority investor groups. |

**Bombardier**

Bombardier is a world-class Canadian manufacturer of transportation equipment based in Montreal, Quebec. The company was founded in the 1940s by Joseph-Armand Bombardier, who designed the world’s first snowmobile. The company focused on snowmobile and jet ski production until the mid-1970s before expanding into rail equipment, followed by aircraft manufacturing in the 1980s. In 2018, Bombardier had sales of USD 16.2 billion with 68,000 employees at 75 facilities in 28 countries. It was organized into four segments: transportation, business aircraft, commercial aircraft, and aerostructures and engineering services. Corporate restructuring has played an essential role in Bombardier’s development as a transportation giant and one of Canada’s few world-class companies.

In 2003, Bombardier decided to divest its recreational products division to focus on its core train and plane operations. Bombardier Recreational Products (BRP) was sold to a group of investors, including the Bombardier and Beaudoin families (35%), Caisse de Depot et Placement du Quebec (15%), and Bain Capital (50%), which is a U.S. buyout firm. BRP is an industry leader with CAD 5.4 billion in sales in over 100 countries and 12,500 employees. The company is divided into two business segments. It’s much larger Powersport Group contains its iconic Skidoo and Lynx snowmobiles, Skidoo jet skis, Can-Am off and on-road vehicles, and Rotax engines. The Marine Group sells Evinrude outboard motors, Aluma Craft fishing boats, and Manitou pontoon boats. BRP expanded its business through several critical global acquisitions and divestitures.

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| **1970** | Purchased Austria-based Rotax, which produces the engines used in most BRP products. |
| **1971** | Purchased Moto-Ski, an innovative Canadian snowmobile producer that was experiencing financial difficulties. |
| **1989** | Purchased Nordtrac Oy, maker of Lynx snowmobiles in Finland. |
| **2001** | Purchased the assets of Outboard Marine Corporation, including the Evinrude and Johnson outboard motors. |
| **2004** | Sold its industrial vehicle division that offered snow grooming equipment for the ski industry, sidewalk snow removal vehicles, and heavy-duty transporters. |
| **2007** | Discontinued the Johnson brand of outboard motors. |
| **2012** | Exited the sport powerboat industry to focus on supplying marine propulsion systems to other original equipment manufacturers. |
| **2018** | Purchased Aluma Craft Boat Company to expand into the sale of smaller freshwater fishing boats. |
| **2018** | Purchased Triton Industries manufacturer of Manitou pontoon boats. |

BRP completed an initial public offering in 2013. It has subordinate voting shares allowing one vote per share and multi-voting shares with six votes per share. In 2019, the subordinate voting shares had only 13.1% of the voting power in the company. This restricted voting arrangement allows the original investors to remain in control. Currently, the Bombardier and Beaudoin families have 45.7% of the voting power, and Bain Capital has 34.9%. Bain Capital is currently contemplating selling all or a portion of its stake to another investor directly or through a secondary offering.

Bombardier’s transportation segment is its largest business unit with USD 8.9 billion in sales, an order backlog of nearly USD 34.5 billion, and over 40,500 employees in 2018. It produces high and very high-speed trains; commuter, regional, and intercity trains; light rail trains and metros; electric and diesel locomotives; and signalling systems. Like BRP, the transport segment grew through acquisitions and some divestitures.

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| **1974** | Diversified into rail production due to a decline in snowmobile demand during the 1973 oil crisis and received its first contract to produce rail cars for the Montreal subway system. |
| **1975** | Purchased the Montreal Locomotive Works (MLW) and made locomotives for VIA and CN Rail as well as passenger rail cars. |
| **1985** | Sold MLW to General Electric to re-focus on passenger rail cars and due to quality issues with its locomotives. The plant was closed by General Electric in 1993. |
| **1986** | Purchased a 45% stake in Belgian’s BN Constructions Ferroviaires et Métalliques S.A. to begin its European expansion. |
| **1987** | Purchased the assets of U.S. railcar manufacturers Budd Company and Pullman. |
| **1989** | Purchased ANF-Industrie, which is France's second-largest manufacturer of railway equipment. |
| **2001** | Purchased Germany’s DaimlerChrysler Rail Systems GmbH (Adtranz), which serves primarily the German and British markets, making Bombardier the global leader in the rail equipment manufacturing and servicing industry.  Relocated its transportation segment headquarters from Montréal, Canada, to Berlin, Germany, in 2002 to better serve the European rail market, which is the largest in the world. |

Bombardier’s business and commercial aircraft segments together accounted for USD 6.8 billion in sales and 14,170 employees in 2018, making the company the 3rd largest aircraft manufacturer in the world. Surprisingly, the business aircraft segment, with its Learjet, Challenger, and Global family of jets, is nearly three times the size of the commercial aircraft segment. The commercial aircraft segment offered the Dash 8 turboprop, Canadair Regional Jet, and CSeries Jet products. Like BRP and Bombardier’s transportation segment, the aviation segment has grown rapidly through acquisitions but has recently had to divest several assets in the commercial aircraft segment to prevent bankruptcy.

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| **1986** | Entered the aviation industry with the acquisition of Canadair Ltd. Canadair was a federal crown corporation that began as an airplane contractor during WWII but was privatized in the 1980s along with Air Canada and CN Rail by the Conservative government. Its marquee product was the Challenger business jet. |
| **1989** | Purchased Short Brothers, which is a major aerospace manufacturer based in Northern Ireland. |
| **1990** | Purchased U.S.-based Learjet, which produces business jets. |
| **1992** | Purchased de Havilland Canada, which had introduced the Dash 8 turboprop aircraft in 1984. De Havilland was also a privatized federal crown corporation that was first sold to Boeing in 1986 before being resold to Bombardier after significant labour turmoil and business losses. |
| **1995** | Launched Flexjet, a provider of [fractional ownership](https://en.wikipedia.org/wiki/Fractional_ownership), leasing, and short-term rentals for business aircraft. It provided a captive market for Bombardier’s family of business jets. |
| **2006** | Sold the rights for all discontinued de Havilland Canada aircraft designs, including the [DHC-1 Chipmunk](https://en.wikipedia.org/wiki/De_Havilland_Chipmunk), [DHC-2 Beaver](https://en.wikipedia.org/wiki/De_Havilland_Canada_DHC-2_Beaver), [DHC-3 Otter](https://en.wikipedia.org/wiki/De_Havilland_Canada_DHC-3_Otter), [DHC-4 Caribou](https://en.wikipedia.org/wiki/De_Havilland_Canada_DHC-4_Caribou), [DHC-5 Buffalo](https://en.wikipedia.org/wiki/De_Havilland_Canada_DHC-5_Buffalo), [DHC-6 Twin Otter](https://en.wikipedia.org/wiki/De_Havilland_Canada_DHC-6_Twin_Otter), and [DHC-7 Dash 7](https://en.wikipedia.org/wiki/De_Havilland_Canada_Dash_7) to Canada’s Viking Air. They had already purchased the parts and service business for all the older de Havilland Canada aircraft from Bombardier in 2005. |
| **2013** | Sold Flexjet to U.S.-based Directional Aviation in exchange for CAD 185 million and an order for CAD 1.8 billion of business jets. |
| **2018** | After much success with its Canadair Regional Jets, Bombardier launched the CSeries Jet in 2016 but was forced to sell a 50.01% interest to Airbus for CAD 1. Airbus agreed to manufacture the aircraft at its U.S. production facility and has the option to acquire the remaining interest by 2024. There are growing backorders for the new CSeries Jets, but Airbus continues to lose money on the renamed A220.  Sold its Dash 8 turboprop business back to a newly revived de Havilland Canada for CAD 250 million. De Havilland is owned by Canada’s Viking Air, which had purchased rights to earlier DHC 1 through 7 aircraft from Bombardier in 2006. |
| **2019** | Sold its business aircraft training business for the Learjet, Challenger, and Global Business jets to Canada’s CAE for CAD 645 million. CAE is the world’s leading flight crew training company.  Sold its Canadair Regional Jet business to Japan’s Mitsubishi Heavy Industries for USD 550 million. The company will complete its existing backlog of Canadair Regional Jets before ceasing production. Mitsubishi hopes to launch a regional jet with the resources it acquired from Bombardier.  Sold its aerostructures segment to Spirit AeroSystems, a major supplier, for more than CAD 1 billion, including production facilities in Northern Ireland, Morocco, and the U.S. |

With Bombardier’s divestitures of its Dash 8 turboprop, Canadair Regional Jet, and CSeries Jet products and its aerostructures segment, Bombardier has exited the money-losing commercial aviation segment. It plans to focus on its higher-margin business jets and transportation segments and use the proceeds from asset sales to pay down debt after both the Quebec and federal governments refused to provide any further government subsidies.