

Thinking Managers

Robert Heller of www.thinkingmanagers.com questions the rationale behind the growing trend towards mergers and acquisitions.

The Curse of Conglomerates

Going back to 2000, the global value of the buyouts on which the private equity sector has burgeoned was just \$28 billion – certainly a healthy sum, but compare it to the \$502 billion total to which the deals had grown by 2006.

Almost exactly the same impressive figure was achieved in just the first half of 2007. This is one gold-mine producing an incredible bonanza.

Compiled by Dealogic, these astounding numbers are quoted in the Harvard Business Review for September in an article by Felix Barber and Michael Goold.

Looking at the strategies involved, it brings to mind the 1960s and 1970s when I spent quite some time analysing the 'conglomerates' and witnessing their voyage from heroes to has-beens. In 'The Naked Manager', my book published in 1972, I made this comment on the firms involved:

“The respectable and disreputable alike used financial techniques to pile together unconnected businesses... The purchases were shoved into common accounting and reporting systems, and left to paddle their own canoes, leaky or buoyant, subject to varying degrees and forms of helpful and unhelpful head office intervention.”

The demise of the conglomerates was inevitable. So why, exactly, and how do these causes relate to the private equity boom of today?

Firstly, exhibited in each sector is a reliance upon the assumption that a range of transferable management skills exist which apply in all cases. But in reality, not all managers can transfer simply between several different businesses.

The privateers exerted themselves by priming the asset for resale. Sometimes, there is barely time for a quick wash and brush-up before they are returned back to the public sector. It is pure fantasy to claim that amazing transformations are achieved, along with all blessings to the business and the economy.

The defunct conglomerates had no problem with revamping and repackaging their buys and placing them back onto the stock market. However, this was easier said than done. All managers are severely challenged by the need to diversify, and once again this was the case in these 'expert' hands.

Large companies regularly have difficulty in paying enough attention to lesser units, and according to Barber and Goold, this has resulted in a continuous supply of businesses for sale that meet the private equity criteria precisely: “stable cash flows, limited capital investment requirements... modest future growth, and above all the opportunity to enhance performance in the short to medium term.”

Until 2004, says Dealogic, they offered enough to fuel amazing growth for private equity leaders; but the supply of unwanted corporate assets big enough to feed the privateers' huge expansion began to diminish, which brought about a big switch to buying whole companies. This strategy change has moved the financiers closer to the old conglomerates. The necessity to get involved in business strategies and even to replace whole top managements is quite a step from just tightening up financial controls.



About the author: Robert Heller is one of the world's best selling authors on business management.