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## Merger and Acquisition Synergy Study: The Case of Ukraine

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**Abstract:** The article examines theories and mechanisms of mergers and acquisitions, analyzes recent publications of international and national scholars and experts, provides various points of view on definition and interpretation of mergers and acquisitions, and offers the author's version of this concept. The article considers synergies that are competitive from an economic point of view, analyzes trends and the latest M&A schemes, suggests possible scenarios in the Ukrainian market, problems and ways to solve them, and draws certain conclusions. Merger and acquisition (M&A) have become a foremost strategic alliance for business, product and logistics in global environment. Using meta-literature review, a general analysis was carried out on M&A to assess motives, methods, financing sources, announcement effects, cross-border competitions, success-failure, valuation issues, and business strategies. It is highlighted in the study the main problems and weaknesses of Ukrainian companies that hinder effective IPOs are the following: a requirement on the part of domestic legislation to issue shares of companies in the national currency; prohibition by Ukrainian legislation to issue more than 25% of shares abroad; the need for the company to comply with all the requirements of a public company; the need to demonstrate stable and long-term dynamics of financial indicators and other components of financial statements; availability of financial resources to go through all stages of preparation and conduct of the IPO (5-20% of the placement amount); inconsistency of the provisions of national legislation with the requirements of foreign stock exchanges; differences in accounting and tax reporting with foreign companies. Despite the fairly widespread global use of M&A transactions in the corporate sector, Ukrainian market is not yet able to effectively use them as a tool for crisis management and preservation of the economic potential of companies due to serious legal gaps, economic problems of corporate and public administration, high political and financial risks of an unstable economy, low business culture and ethics.

**Keywords:** mergers, acquisitions, synergy, companies, competitive advantages, investors, value.




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### Merger and Acquisition Synergy Study: the Case of Ukraine

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## Introduction

Increased competition in the global marketplace has prompted most organizations to turn to mergers and acquisitions as an important strategic choice. Mergers and acquisitions (M&A) is a mechanism that contributes to rapid growth of companies, increasing managerial efficiency and maximizing profits. The relevance of the study lies in the fact that mergers and acquisitions are associated with the enhancement of a company's competitiveness in the marketplace, and in unstable economic conditions, these factors have a decisive impact on the company's survival.

Globalization and increased competition between businesses have become a trend in recent years, not only in the global economy but also in the national economy. The struggle for competitive advantages, integration of companies from different segments of the economy, and the creation of international companies are reflected in mergers and acquisitions. Recently, mergers and acquisitions have become one of the most widely used strategies for restructuring market giants to increase investment attractiveness and business value.

There are two different directions for implementing a restructuring strategy: integration and disintegration (Kaiser, Obermaier, 2020). The integration direction of the restructuring strategy refers to the potential for inorganic growth of the company. Since the company's organic growth implies growth through internal resources and investments in the development of its existing business, this area is in line with the investment strategy as one of the areas of the overall financial strategy. Inorganic or external growth of a company is primarily achieved through the integration of companies in the form of mergers and acquisitions (Medina et. al., 2020).

It is well known that in the modern economy, companies at a certain stage of their operation resort to expansion through mergers and acquisitions, which are one of the forms of corporate relations development (Hossain, 2021).

The emergence of mergers and acquisitions has its roots in the history of US industrial production in the late 19th and early 20th centuries. It was in the period from 1897 to 1904 that the first wave of mergers and acquisitions was described in the economic literature. Since then, the US economy has experienced four more waves. In the foreign economic literature, these transactions are called "mergers and acquisitions" (Cho, 2022).

In the modern economic literature, the terms "merger" and "acquisition" are often used synonymously, but even more often they are used in the phrase "mergers and acquisitions" (M&A) to refer to a single phenomenon inherent in the corporate control market. This situation is due to the fact that these transactions have the same economic nature, namely, a change of control over the company.

It should be noted, however, that there is currently no consensus in the academic community on the interpretation of this concept. The development of a unified approach may be hampered by the complexity and ambiguity of these processes, as well as their peculiarities for foreign and Ukrainian practice. Therefore, the concepts of M&A in foreign economic literature and legislation are not consistent with the definitions existing in Ukrainian literature and legislation.

Professor of Economics P. A. Gaughan (2007) identifies three forms of corporate reorganization: mergers, acquisitions and consolidation. He defines a merger as a combination of two companies in which one ceases to exist and the other continues to operate. According to P. A. Gaughan (2007), consolidation is a process by which two or more companies form a completely new company. He interprets the term "takeover" as a type of merger, but the process in this case is expressed in the form of hostile takeover (Gaughan, 2007). In other words, the merger process is primary, and the takeover process only determines whether the merger is friendly or hostile.

R. S. Foster and R. Lajoie (1998), speaking about mergers and acquisitions, define an acquisition as a transaction that results in the company becoming the property of the acquirer. In this case, the acquirer establishes control over the acquired company and assumes all its assets and liabilities. The analysis of merger types considered by the authors (reverse merger, forward merger)

leads to the conclusion that a merger is considered as a narrower technical term for defining accompanying legal procedures that may or may not follow the acquisition (Foster, Lajoux, 1998).

D. DePamphilis (2021) distinguishes between organizational (legal) and economic aspects of mergers. The organizational aspect is manifested in the retention of the status of a legal entity by one of the parties to the deal after the merger. Economics determines the direction of the merger (horizontal, vertical or conglomerate). According to the author, the takeover process implies that as a result, one company becomes the owner and gains control over another. Acquisitions can be made by purchasing the assets or shares of another company. Under this mode, the company retains its legal status in the process of acquisition and continues to operate as a subsidiary (DePamphilis, 2021).

Thus, according to D. DePamphilis (2021), the difference between mergers and acquisitions is that in a merger one legal entity ceases to exist, while in an acquisition both companies remain independent legal entities, only the owner of the shares changes (DePamphilis, 2021).

From a legal perspective, experts believe that integration of companies can take various forms. For example, F. Evans and D. Bishop (2001) interpret a merger as a legal subtlety resulting from the merger of two companies, as a result of which one company dissolves into another, or a new legal entity is formed from the two (Evans, Bishop, 2001).

In the authors' opinion, it is advisable to use a single term "mergers and acquisitions", and therefore, given the importance of the definition in the modern world scientific knowledge, we consider it possible to propose the following definition of mergers and acquisitions:

- mergers and acquisitions are a set of deals between business entities that involve a change of ownership, merger of entities that continue to operate under the auspices of the company initiating the transaction, or transfer of a controlling stake in one of the parties to the deal to the other.

## **Materials and Methods**

The article uses informational, comparative, institutional, and comprehensive approaches, and adheres to the principles of objectivity, specificity, and systematicity, which allowed for a detailed and comprehensive study of the synergy of mergers and acquisitions. The principle of systematicity played an important role in the research along with the following general scientific methods used: content analysis, induction and deduction, descriptive, retrospective, comparative methods, generalization and grouping. The classification method is used in the analysis of sources and literature, as well as for theoretical and methodological analysis in determining essential characteristics of the key concepts of the study of mergers and acquisitions. The method of content analysis is used to analyze official documents, and the method of analysis and synthesis is used to process the available literature. The comprehensive use of various methods and approaches in the paper contributes to a more objective study of the topic.

The materials of this article can be used as a theoretical and methodological basis for studying the M&A market at the level of professional discussion.

## **Results**

### **Synergistic effect of mergers and acquisitions**

From an economic point of view, the M&A strategy acts as a tool to ensure competitive advantages of the merged company through the consolidation of its capital and more efficient and rational use of its opportunities in the market (Kulishov, 2023). There are several targets that characterize in one combination or another economic feasibility of mergers and acquisitions – operational, financial, investment, strategic, and others (Arbidane et al., 2021). All of them are based on the need to ensure the interests of the owners. However, the main reason for the implementation of integration processes is the desire of companies to obtain a synergistic effect: an integrated business creates more value for shareholders than each of its divisions separately (Botelho et al., 2021). For

the purposes of corporate control, two main types of synergy are considered – operational and financial (Table 1).

**Table 1.** Basic theories that explain the motives for conducting mergers and acquisitions of companies.

<b>Theory</b>	<b>Motivation</b>
Theory of operational synergy	Improving operational efficiency
Economies of scale (output)	Increasing production efficiency due to increased production volumes thanks to reaching customers, suppliers or competitors.
Financial synergy theory	Decreasing the cost of capital
Diversification and improvement of creditworthiness	Positioning the company in fast-growing market segments: – new products – current markets; – new products – new markets; – current products – new markets.
Strategic restructuring	Transactions are carried out to adapt more quickly to changes in the external environment than could be done due to internal sources and reserves of the corporation as a result of: – innovation; – legislative changes; – political transformations.
The Pride of Managers (Richard Rolle)	Managers of acquiring corporations are confident that their valuation of the target company is more accurate than that of the market. This circumstance forces them to overpay for overvalued synergies.
Purchasing undervalued assets (Tobin q-ratio)	Analyzing investment attractiveness of the company taking into account the analytical coefficient q-Tobin. Companies interested in expansion choose to invest in properties whose market value is lower than the replacement value of their assets.
Eliminating inefficient management (agency problems)	Replacing managers who do not act in favor of owners.
Managerialism	Increasing the size of the company to increase the amount of power and remuneration of managers
Optimizing taxation	Reducing the tax base, obtaining tax benefits, releasing duplicate assets
Strengthening market power	Increasing the controlled market share in order to set prices above the competitive level
Revaluating the company's value	Revaluating the share capital of the acquiring company by investors

An important component of mergers and acquisitions is the mechanism of diversification and creditworthiness, which is a source of positive synergy, due to which it is possible to significantly reduce the cost of capital thanks to a reduction in the overall riskiness of operations (Kulishov, 2023). On the other hand, diversification can help bring a corporation's key product to new markets with greater growth potential. Table 2 shows possible areas of diversification (Yin, 2016).

Thus, diversification:

- contributes to the stabilization of the company's income flow in the long run;
- allows withdrawing part of the capital from industries that are experiencing a long-term recession;
- contributes to the reduction of transaction costs, more efficient use of complementary resources and available production capacities at different stages of the production process.

**Table 2.** Ansoff's growth strategy matrix.

Product Market	Current	New
Current	Low growth Low risks Penetration Strategy	Higher Growth Higher Risks Market Development Strategy – Relative Diversification
New	Higher Growth Higher Risks Market Development Strategy – Relative Diversification	Highest Growth Highest Risks Diversification strategy

Noteworthy is the theory of managerial pride or the "winner's curse", which was created in 1986 by Richard Roll, professor at the University of California, Los Angeles (Roll, 1986).

According to the pride theory, mergers and acquisitions are the result of an individual decision by the acquiring company management. Even if the merger does not have a synergistic effect, this decision is made because managers believe that their valuation is correct and that the market valuation of the target company does not fully reflect its development potential (Trout, Rivkin, 2008).

The pride theory is an attempt to explain why, despite the existence of many qualitative studies of corporate mergers and acquisitions, the motives behind them and the conditions under which these mergers and acquisitions increase the aggregate market value of a corporation have not yet been fully revealed. Using data published in more than forty different empirical papers, Roll concluded that, in fact, mergers and acquisitions do not carry synergies at all, and if they do, these synergies are almost always overestimated by managers who are overly optimistic.

The above considerations indicate that any offer that exceeds the market value of the company is economically unjustified. However, this is only true if we assume that market prices reflect optimal investor behavior. Market prices are average prices that can reflect individual behavior of market participants, and in times of uncertainty, investors often make irrational decisions, meaning they involve mergers and acquisitions, according to Roll.

Roll believes that at least part of the increase in the target company's stock value during the acquisition is not due to the synergies expected from the acquisition, but to the simple transfer of funds from the acquiring company to the target company, i.e. the property premium.

So, the classic explanation of feasibility of mergers and acquisitions lies in the synergistic theory, i.e. it is the acquisition by the acquiring company of the added economic value created as a result of the purchase of the target company. Quite often, the synergistic effect is also referred to as the "2 + 2 = 5" rule.

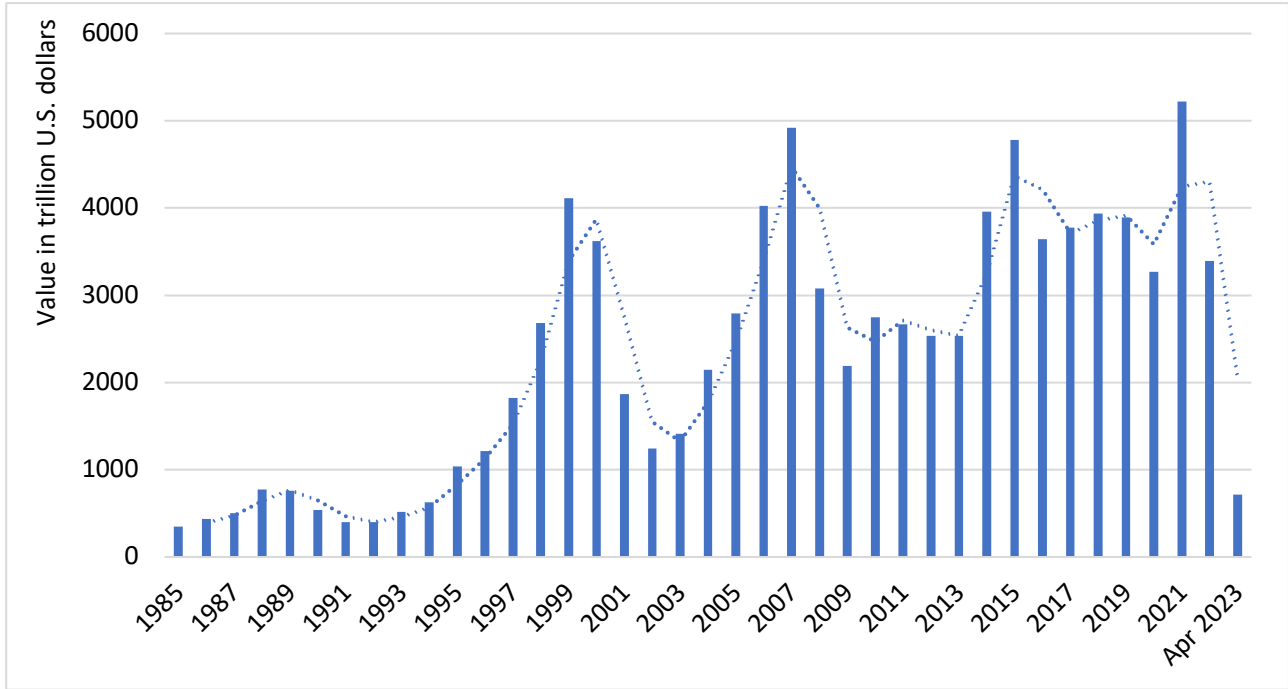
The essence of the synergistic reason is that a new company resulting from a merger can enjoy a wide range of benefits (synergies) resulting from the pooling of these companies' resources (Holubčík et al., 2023).

### Analysis of trends and the latest M&A schemes

Record levels of deal-making, both in terms of volume and value, persisted from the end of 2020 and during the first six months of 2021 (Figure 1).

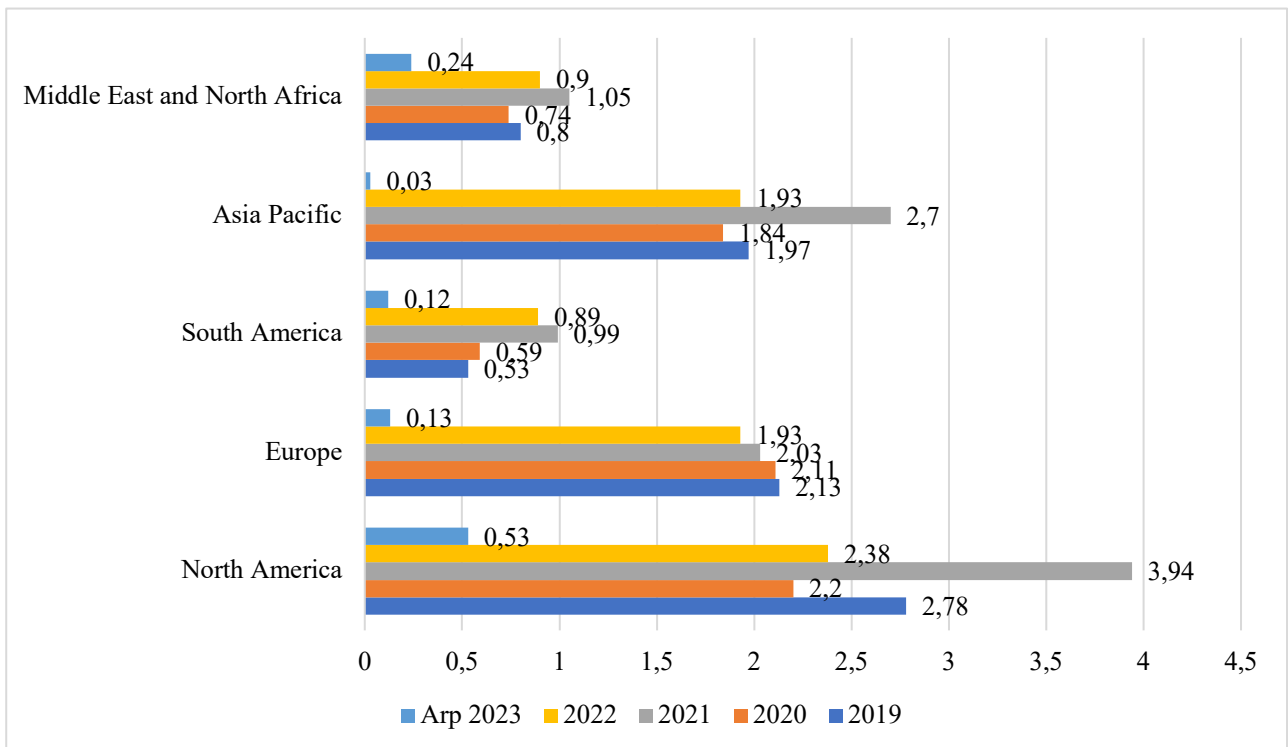
Mergers and acquisitions continued growth in early 2021, contributing to a record global deal value of more than \$1 trillion per quarter over the past 12 months. Capital inflows led by SPACs

(special-purpose acquisition companies) were an important catalyst, as increased PE investments and corporate acquisitions – especially those focused on technology assets. Technology, media and telecommunications companies accounted for a third of all megadeals in the period, but that number increases to half when looking at companies with a technology-driven business model regardless of their sector.



**Figure 1.** Value of mergers and acquisition (M&A) transactions worldwide from 1985 to April 2023, in trillion U.S. dollars (Statista, 2023a).

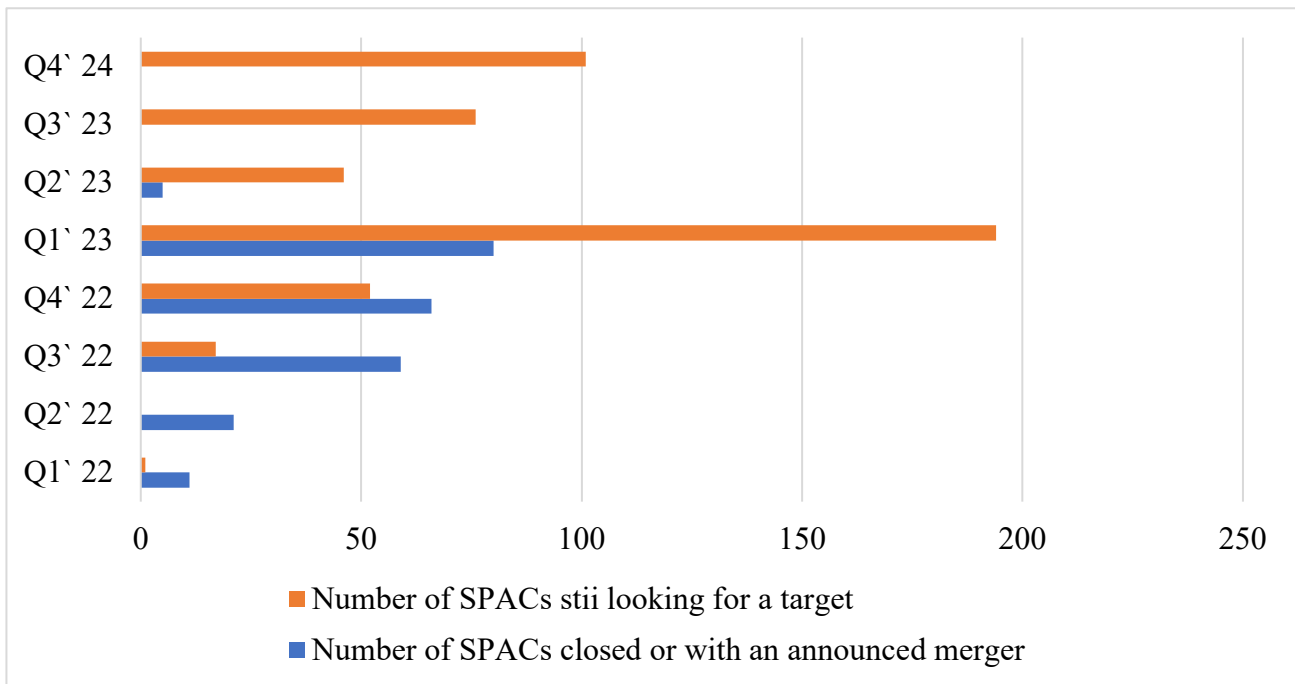
The volume of deals was roughly the same in Asia Pacific, EMEA and the Americas, although deal value was more weighted by the Americas, a similar trend was observed until 2020 (Figure 2).



**Figure 2.** Value of merger to acquisition deals worldwide from 2019 to April 2023, by region, in billion U.S. dollars (Statista, 2023b).

SPACs catapulted megadeals announced in the first half of 2021 to record levels. More than a quarter of the megadeals announced had a SPAC buyer and a large proportion of them (almost 90%) were related to technology. This could amplify the clash that is possible between a SPAC and another market and force buyers to reconsider their strategies to win in the current environment. In addition to SPACs, PE funds were active investors, and the share of PE deals increased from 27% at the beginning of 2019 to 38% in the first half of 2021. The value of PE deals increased as the PE industry itself has grown, as well as the number of more complex deals.

An analysis of early 2021 shows that the number of SPACs grew to a record 274 and raised more than \$80 billion, which is more than the amount raised during the whole of 2020. Such growth has inevitably attracted the attention of regulators, investors, and the media. In April, the SEC issued new financial reporting guidelines for SPACs, which led to a number of transfers, and accordingly, the creation of new SPACs slowed down. Low post-acquisition returns impacted the ability of these SPACs to enter into an agreement yet to secure funding. However, given the popularity of SPACs as a means of bringing certain types of businesses to the public, including high-value, technology-oriented, innovative, or disruptive businesses, demonstrating their long-term operation (Figure 3).



**Figure 3.** Status of SPACs disclosed (January 2019-June 2021) (Statista, 2023c).

The global crisis caused by COVID-19 forced many company executives to review their portfolios during 2020-2021 to review their strategies. These reviews have led to both strategic acquisitions and divestitures, as companies redirect management resources and funds to those parts of the business with the highest growth potential and where they enjoy an excellent competitive advantage. This has led companies to use mergers and acquisitions to acquire opportunities they do not have (often in technology) to expand existing opportunities and amplify that advantage.

Non-traditional sources, such as environmental, social responsibility and corporate governance, are increasingly considered and taken into account when making strategic decisions and conducting financial and economic analysis as managers focus their efforts on maintaining and maximizing revenues from high-appraised value and active demand.

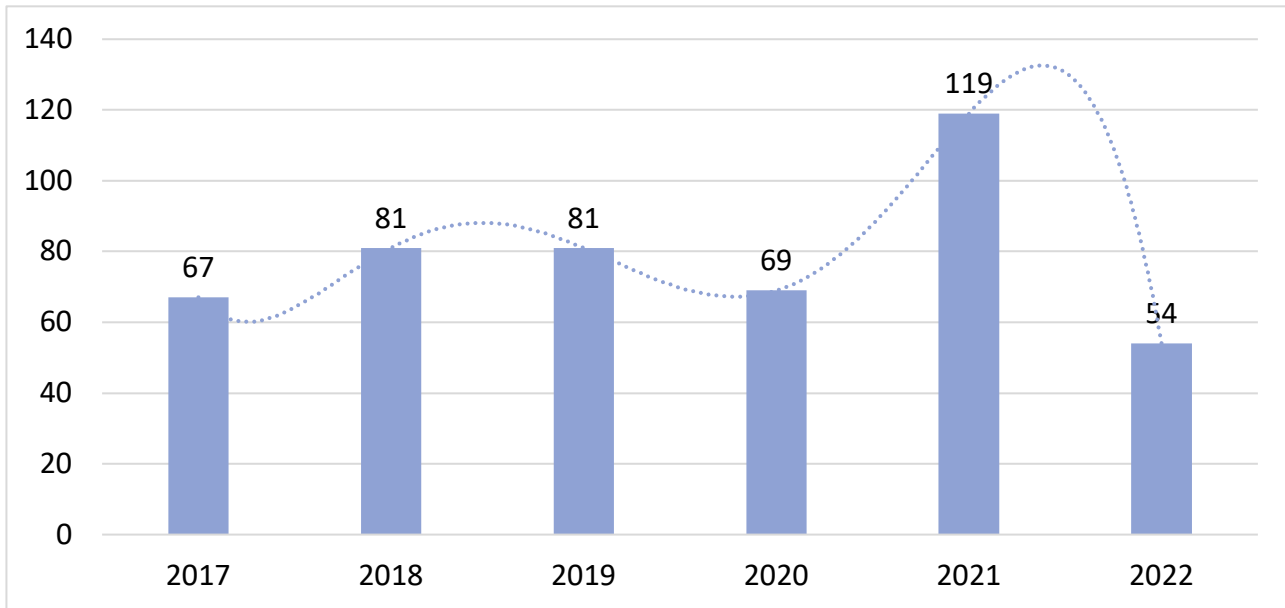
### Problems of the M&A market in Ukraine: ways to solve them



For Ukrainian companies, participation in mergers and acquisitions is an opportunity to expand the scope of activities, increase profitability, penetrate new markets, and reach a "qualitatively new level of development" (Gonchar et al., 2022). However, the dynamics of these processes in the domestic market is low, which is due to the presence of a number of problems that need to be solved.

At the present stage of development of the national economy, mergers and acquisitions (M&A), which are tools for expanding the activities of companies, strengthening their positions in the market, and developing new markets, are gradually developing in Ukraine.

In Ukraine, there is a gradual development of the M&A market, despite the difficult political and economic situation in the country (Figure 4).



**Figure 4.** Number of deals in the Ukrainian M&A market for the period 2017–2021, units (KPMG «M&A Radar 2021: Ukraine, 2021).

In 2021, 119 M&A deals were concluded, which is 45% more than in 2020, and compared to 2017, the number of deals increased by 77.6%, and the total volume in 2021 amounted to 2.7 billion. This is 2.3 times higher than the value of this indicator in 2020 (KPMG «M&A Radar 2021: Ukraine, 2021).

In the structure of the market, Ukrainian M&A deals account for 55% of the value and 62% of the volume of deals (KPMG «M&A Radar 2021: Ukraine, 2021). For example, the largest deal in 2020 (\$110 million) was the acquisition of Eurozhytlogroup LLC by Dragon. The value of the largest transaction in 2021 (USD 400 million) is the amount of acquisition of shares in Ivanofrankivsktsement PJSC by the Azerbaijani company NEQSOL Holding.

The distribution of M&A deals by industry in 2021 is shown in Table 3. (KPMG «M&A Radar 2021: Ukraine, 2021).

**Table 3.** M&A deals in Ukraine in 2021 by industry.

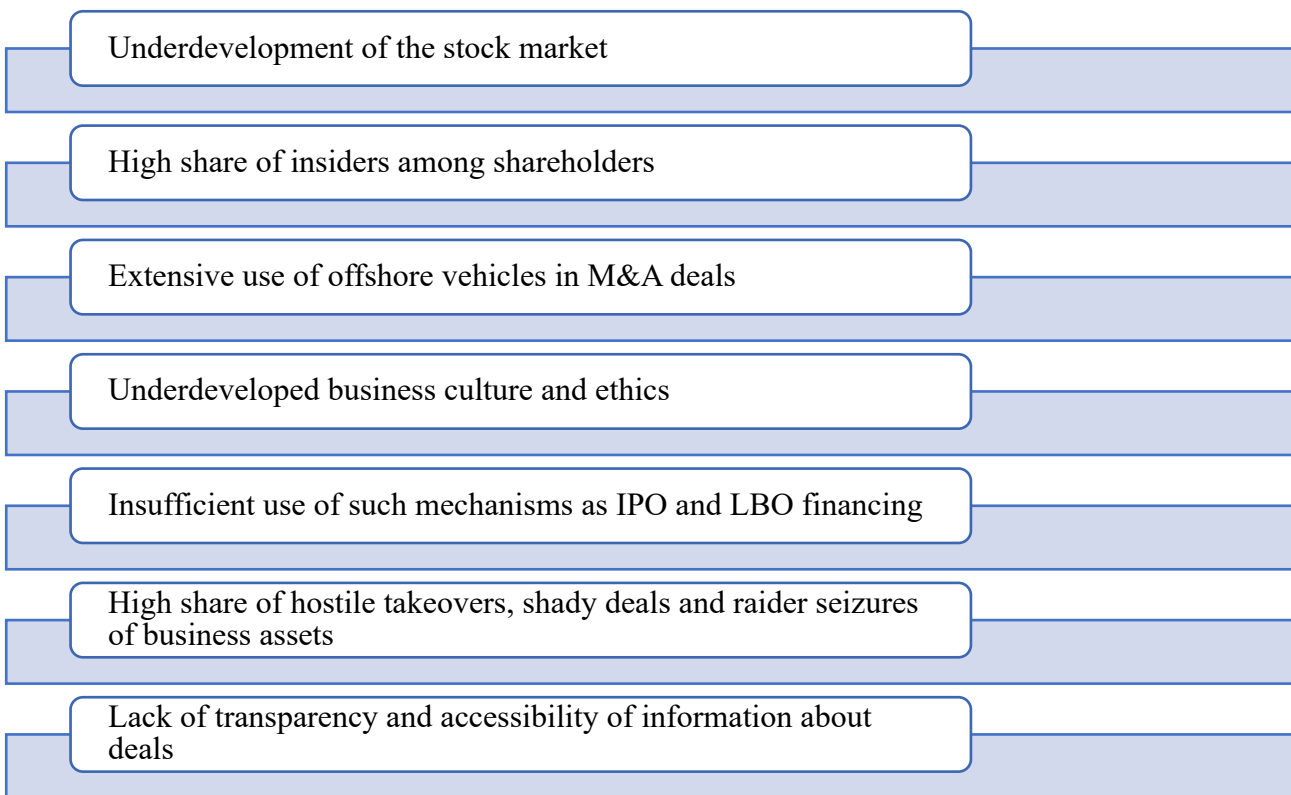
Industry	Number of deals, units	Amount, mln. \$
IT & Telecommunications	36	813
Construction & Real Estate	6	650
Metallurgy	1	340
Agriculture	19	234
Financial activities	8	109
Extractive industry	10	124
Food industry	14	58

Transport & Warehousing	8	34
Other	17	384
Total	119	2746

Thus, in 2021, the most attractive areas in terms of M&A were IT and telecommunications, agriculture, food and mining.

Foreign investors prefer such sectors of the Ukrainian economy as innovation and technology, agriculture, transport and infrastructure. The most active participants in the Ukrainian M&A market are investors from Europe, the Middle East and North America. In particular, in 2020, "Europe (USD 135 million), the Middle East (USD 130 million, one transaction) and North America (USD 70 million, eight transactions) accounted for 83% of the value of all acquisitions of Ukrainian assets by foreign investors and 92% of the volume of all such transactions" (Lunova, 2022).

The development of the Ukrainian M&A market is characterized by a number of problems (Figure 5).



**Figure 5.** Problems of the Ukrainian M&A market (Vergeles, Baiura, 2023).

Among the above, a particular problem in the market is the high share of hostile takeovers, including the following typical hostile takeover methods in Ukraine:

- deliberate bankruptcy of unprofitable enterprises, in the assets of which the acquiring company is interested. A popular variation of this method is the purchase of debts;
- purchase of shares;
- contestation of property rights by a qualified raider who takes advantage of the mistakes of unqualified management of companies. The effectiveness of this method is ensured by a "friendly" court (Sereda, 2023).

An analysis of scientific sources devoted to studying sources of financing of M&A transactions shows that in Ukraine such a mechanism for financing mergers of companies as an initial public offering (IPO) of shares is not sufficiently used, although in the agricultural sector of the country's economy this mechanism has brought certain results. Thus, at the end of 2011, 12 Ukrainian

agricultural companies entered the international stock market, while they attracted USD 980.6 mln through the sale of a share of assets, and their total market value reached USD 4884 million (Lunova, 2022).

According to experts, the main problems and weaknesses of Ukrainian companies that hinder effective IPOs are the following:

- a requirement on the part of domestic legislation to issue shares of companies in the national currency;
- prohibition by Ukrainian legislation to issue more than 25% of shares abroad;
- the need for the company to comply with all the requirements of a public company;
- the need to demonstrate stable and long-term dynamics of financial indicators and other components of financial statements;
- availability of financial resources to go through all stages of preparation and conduct of the IPO (5-20% of the placement amount);
- inconsistency of the provisions of national legislation with the requirements of foreign stock exchanges;
- differences in accounting and tax reporting with foreign companies.

In order to intensify M&A processes in the Ukrainian market, among other measures, it is also necessary to eliminate shortcomings and problems of the processes of preparing and entering domestic companies for IPOs, since at this stage of development, the Ukrainian M&A market does not yet sufficiently use the mechanisms of debt financing of LBO deals. Leveraged Buy-Out (LBO) deals are buyouts of a target company using a debt financing scheme. In such a transaction, the buyer uses external financing (bank loans, bond issues, third-party investments) to finance the purchase of the company. At the same time, the share of external financing can reach 90% of the price of the acquired company. The peculiarity of such a transaction is that the assets of the acquired company, together with its cash flow, on the one hand, act as collateral, and on the other hand, are a source of payment for debts incurred by the buyer as a result of the transaction.

Scholars highlight the following advantages of LBO financing for the current Ukrainian situation:

- no need to divert additional funds from the company's operating activities;
- diversification of risks;
- possibility of rapid business development with an adequate risk assessment;
- tax advantages related to debt financing (the cost of paying interest on the loan reduces the tax base of the company);
- lack of disclosure of information (in comparison with raising share capital by going public or debt capital by placing a bonded loan);

"A fixed interest rate for the use of the loan ensures high profitability of transactions" (Borio et al., 2015).

A significant problem in the development of the Ukrainian M&A market is the underdevelopment of the stock market and the low share of public companies circulating in it, which has been noted by experts and analysts for a long time. In Ukraine, there is practically no effective system for protecting the rights of corporate investors, and the market for trading in corporate securities is actually underdeveloped. The over-the-counter market is much larger in volume than the exchange market, which indicates the presence of disproportionality of sectors. The presence of these problems necessitates an active reform of the system of state regulation of the stock market and stimulation of its development, which will make it possible to intensify M&A processes.

## Conclusions

Mergers and acquisitions are a current, widespread in the world practice trend of consolidation of assets and concentration of production activities of companies. Such consolidation takes place on various grounds: either on a voluntary basis, taking into account the interests of the parties interested in the association, or in a hostile form, which is due to the rigidity of the competition mode. The type

of mergers and acquisitions depends on the market situation, the strategy of companies and their resource potential, as well as on the targets of such transformations. The number of transactions directly depends on the economic situation: interest rates, investment activity, applicable legislation, etc.

Mergers and acquisitions of companies are an effective tool for ensuring their effective economic activity, a means of increasing investment attractiveness and increasing the total value of assets through synergy. The main directions of intensification of M&A processes in the Ukrainian market are the following: improvement of legislation regulating mergers and acquisitions of joint-stock companies in accordance with current international practice; implementation of measures for further development of the stock market, increasing its capitalization and transparency; more active stimulation of the development of the IPO market, which will contribute to the integration of the country's economy into the system of world economic relations, and stimulate economic growth through investment attraction.

### Conflicts of interest

The authors declare no conflict of interest.

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### Authors contribution

Conceptualization, H. P. and I. A.; methodology, I. M.; analysis data, O. P.; project administration, V. K. All authors have read and agreed to the published version of the manuscript.

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