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Dynamic Assessment of Mergers and Acquisitions Risks in Botswana

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ABSTRACT

The aim of the paper is to address the issue of local enterprises that fall prey to international companies in terms of mergers as they fail to address risks that collapse their institutions. In this research paper, the study is based on literature. The researcher looked at similar cases of mergers and acquisitions in Botswana and overseas in diverse sectors of the economy. The core assessment of risk identification which is portfolio risk helped in identifying risks that affect consolidations, mergers, and acquisitions in Botswana. The researcher intends to help the companies taking over others to be able to manage risks, contain their risk appetite in order to avoid financial losses as well as legal litigations from either parties that will be affected. Local enterprises fail because of lack of experience and capacity to handle risks. It is also coupled with failure to measure their risk appetite as well as test the role of leadership in managing risks. The methodology used is direct interview and consultations for the information.

1. Introduction

For a country like Botswana, the economy is much more dependent on government sector as the government dominates the industries and it is the largest consumer of products and services. Usually, when the government itself is not doing well, businesses do suffer a lot, leading to retrenchments and closure to some. In this scenario, that is when companies come with strategies to survive, that include consolidating with others, acquiring as well as merging. The organizations strive to make a profit, multiply in branches which account for growth, branding, provide for social responsibilities in the communities they serve.

In consolidations, mergers, and acquisitions, a risk capacity of the major company must also be considered. That is the implication that exists of risk taking and tolerance of the taking over process. The major company might lose reputation, people, knowledge, internal strive as infrastructure. Companies in Botswana are facing stiff competition from outside world due to globalization. Hence, organizations face competitive pressure for product markets and service providers. Even in case of normal distribution of goods and services, more risks are directed to small corporations (He Bin 2013, p.1013). In terms of acquisitions, normally for a bigger company to be in a position to take another one, it has to be a high-performance company. It is always alert to changes, with a capability of managing risks. It is of paramount importance to understand how success and failures of businesses are driven when a company take over. Effective strategic management will need to be put in place so that the business mergers may not be a failure.

2. The Statement of Mergers and Acquisitions in Botswana.

When two companies combine, it is called a merger. Whereas, when one is completely absorbed by another corporation it is known as an acquisition. The identity of the target company is lost and it is incorporated into the bidder company, which retains its identity. All the privileges, rights, and liabilities of the merged corporation are assumed by the target company (Lee 2003). On the other hand, in a consolidation, two corporations with diverse identities forge them to form a completely new corporation. In this case, there is no bidder company and target company. It can happen when there is the dissolution of two companies after which a new one is born. A typical example is when Botswana Technology Centre (BOTEC) and Rural Industries Innovation Centre (RIIC) were dissolved and Botswana Institute for Technology Research and Innovation (BITRI) was found. In an acquisition, what is normally involved a public tendering offer, typically of a prescribed price, at a substantive amount over the existing market price, best for a short time frame, and suitable for target firm's stock's substantial percentage. Acquisition itself may in the end kill other competitors in same market, hence making the business to survive. Normally same line of product is involved (Rosset 1990). Acquisitions are what actual transpires when the business is failing or when its being taken over. As a bidder company, taking over a target company the bidder becomes involved, therefore develops in response the value generated by business operations (Lee 2003). Horizontal mergers can solve some issues like elimination of competition between companies or organizations, creation of enough and sustainable market. Finally, concentration in the relevant market. Normally there is no relationship between a transaction of a conglomerate and competition. Smaller independent companies will be sidelined and making a conglomerate more powerful and may impair independent decision making of small scale operators. In Botswana, mergers and acquisitions are governed and controlled by the Competition Authority. Competition Authority is constituted in terms of section 4 of the Competition Act Cap 46:09.

Table 1: Summary of merger activities in Botswana

Sector	2012/ 2013	2013/ 2014	2014/ 2015	2015/ 2016	Total
Agriculture	2	4	0	0	6
Construction	2	1	1	1	5
Advertising	0	0	1	0	1
Education	0	0	2	0	2
Finance and Banking	0	1	2	0	3
Health	3	0	0	0	3
Hospitality	2	3	2	1	8
ICT	2	1	1	2	6
Insurance	4	0	1	2	7
Manufacturing	0	2	2	5	9
Mining	5	5	6	2	18
Motor Industry	0	0	1	0	1
Pharmaceuticals	0	0	1	0	1
Property	0	1	1	3	5
Retail	4	5	6	12	27
Security	0	0	2	1	3
Telecommunica tions	0	0	1	0	1
Transportation	1	7	2	0	10
Other	5	2	0	4	11
Total	30	32	32	33	127

Source: Competition authority annual report 2015/16

3. Previous Cases of Mergers and Acquisitions Abroad

In the past, talking about risk was only confined to safety and insurance, but evolved overtime to being that of a significant natural phenomenon. Risk only focused on threats and negative aspects of businesses and was separate from the business concept. Companies are now aware of business risks and seek the help of risk managers, consultants, and facilitators where necessary. Acquisitions have been there in the global business as early as the seventies. Back in the past, companies focused much on hazard risk management, finance or insurance. Today, every activity in business is passed through out the risk assessment procedures to ensure its effectiveness. According to Slater (2013, p.18), it is proven that the whole purpose of acquisitions, whether friendly or aggressive, is to sustain continuity of businesses in the state of economies. It is due to the reason that companies are given an opportunity to keep up with their operations. As evidenced in the past decades, it is seen that two-thirds of all newly created jobs in the United States came about because of acquisitions. This is because mergers and acquisitions enabled larger corporations to exist, enjoying economies of scale, fresh leadership, and to a certain point less administrative pool (Slater 2013). Looking at the context of America, critics believe that smaller companies are the ones who are most successful, companies such as Apple computer, Genentech and New York Air. As far as 1953 it is believed that close to 50 000 acquisitions of companies took place in the America alone. When this happens, small companies being taken by the giants weakened or phased out from their operations (Slater 2013). However, in the United Kingdom, studies show that acquisitions by public companies only is controlled by the city code. The city code is an instrument that is supposed to be binding and followed and came to effect in 2006. In fact, corporate take overs are everywhere in the world, Spain, Canada, United Kingdom, Africa as well. In a country where most companies are owned by the state, it is also on minimal occurrences that there can be acquisitions. In Botswana, bigger companies are killing businesses of smaller companies either by these acquisitions or keep them out due to competition.

4. Risk Management of Mergers and Acquisitions in Botswana.

To understand further on this subject, definitions of risk management have to be looked at for simplicity of the stated topic of the research. According to Fraser and Simkins (2010), Enterprise Risk Management (ERM) as a concept is the responsibility of leaders, management, directors, and other officials. It should be included in strategy setting in the entire enterprise. It should also be crafted to be proactive in order to detect unforeseen circumstances which can harm the enterprise, and manage risk to be within its appetite, to provide reasonable assurance regarding the achievement of entity objectives (Wright 2000). ERM will help companies to meet their strategies and objectives (Brady 2006, p. 33). According to Pons and Raine (2003, p.3), uncertainties in a risk have got different levels of dimensions or a degree of occurrence. The whole purpose of risk management is to make sure that organization's reputation, assets, and interests by managing threats in business (The Financial Services Skills Council: 2008). Risk analysis involves risk identification, estimation, analysis, as well as evaluation and control (Rahman, Youtang, Azim, and Mahfuz (2016, p.1053).

The risk identification process is used to discuss the ongoing threats that the organization may face and help the organisation to mitigate the risk (Brady 2006, p.33).

Risk Assessment will then be used for:
- Identifying hazards
- Deciding on casualties
- Evaluating risks and deciding safety measures.
- Recording findings
- Review on assessment and update

Risk avoidance would then lead to not doing anything that could carry a threat to any business. Bidder companies can, therefore, avoid buying target companies in order not take on the legal liability that comes with it. Risk avoidance may solve some problems or prevent rushing into making losses. But there is also an opportunity that can be lost if not taking chances. All levels in the organization, therefore, would be responsible for the safety of risks in the company and help with avoidance of such risks (Tasmin and Salehudin, 2016).

When a company takes over another there must be principles for assessing risk which will help with the control of acquisitions. So Competition Authority helps to protect companies from some of the risks from larger multi-national companies and from unfair competition.

5. Assessing Risks Faced by Companies in Botswana

The portfolio of risks is a simple summary of possible risks that can be found either in an industry or inside governmental organizations. During consolidations, mergers, and acquisitions, this portfolio of risks will become handy because a target company will refer to them. It would take stock and prepare for activities that will help mitigate the risks. The portfolio will also enable the company in deciding whether to go ahead with the risks or not. Risks generated from the portfolio must be tangible and focused on objectives which the companies need to fulfil. Political, Environmental, Economic and Technological (PEST) factors can help in risk identification (Deng & Deng, 2016).

Financial Risks – credit default, debt and credit rating, interest rate fluctuations, transaction processing errors, revenue management, tax law changes, instability in financial markets, recession in economy, asset valuation, acquisitions, fluctuations in interest rate, fluctuations in foreign exchange as well as currency, health care and pension costs (Debra, 2006).

Strategic Risks – Decision makers in strategic risks must align their understanding of risks and objectives. Moreover, they have to assess and mitigate risks. (Qianfen & Junwu 2016, p. 1134).

Operational Risks – Skills shortage, distribution failures, loss of key equipment, management oversight, recall campaigns, accounting or internal control failures, utility failures, vandalisms, service provider failures, health and safety violations as well as supply chain (Chen, 2009).

Hazard Risks – sabotage/terrorism, worker's compensation, geopolitical risks, diseases, severe cold/hot weather, boiler or machinery exposure, property damage, outbreaks, natural disasters.

Political influences can have an effect on monetary policies. At times technical refinement or minor reforms might be needed in order to help enterprises. Competing currencies can lead to financial risks of businesses and kill the entire economy. Financial crisis can be because of economic circumstances, making it extremely difficult for business to operate. It will extend to difficulties in acquisitions. Hazard risks maybe as a result of human activity that can cause geological environment which can lead to destruction in businesses (Liu, Jing, & Zhao, 2008 p. 82-85). Management of both target and bidder company must have a brainstorming session whereby participants should be in a position to understand objectives which are explicitly stated clearly and understood by the participants. This will allow participants to be creative hence draw a pattern of risks. According to Biasotto & Rouhan (2004), risks are identified and classified on the basis of the likelihood. A useful session of brainstorming for participants will show their originality and come up with a team that will cooperate to come up with common risks encountered before. Risk perception approach of an entrepreneurial team can impact on the personality of the team. (Qing 2013, p.1213). Another way of identifying risks is by use of a questionnaire with a number of questions concerning events to find out uncertainties, and there will be a possibility of risk assessment (Guldenmund, 2000). Organizations can engage employees when coming up with ideas for identifying threats. Possible portfolio of risks will help in risk criteria. Risk criteria must be defined for every environmental risk factor to help in brainstorming and after benchmarking with other enterprises on which risk to tolerate, treat, accept or reject.

6. Problems Faced in Mergers and Acquisitions.

Most of the target companies have financial problems but with potential for further business expansion. Acquisitions by target companies help smaller companies to be able to increase their risk appetite. The following are problems that may be brought about by mergers and need to be addressed.

• There is going to be retrenchments because staff members of two companies will be merging, so some services by employees will be rendered obsolete. Talented employees must be retained.

• Target company employees may not like the new structures and new management hence may start with low morale

• Loss of capital when a bidder company purchases a target company

• Legal tussles over employment contract and compensations which will cost the target company more money or derail processes of a takeover.

• Target companies may not reveal all information about itself and hence in the aftermath of a takeover, a bidder company will have problems.

• Cultural and ego conflicts between the target company and bidder company employees, while the integration is still new.

One of the main reasons why control is needed in any form of mergers is so that the target company will be audited in order to give light to the company whether risks can be cleared or not.

7. Strategic Risk Management Mindset in Addressing Risks During M and A.

This is when focusing on how well a strategy of a business will operate under different circumstances, considering the fact that in merging, the restructuring will have to take effect. The Risk mindset help to guard against declining of shareholder value, or damaged company reputation. The risk in a company merger or acquisition can mean losing assets and control. The business after an acquisition must continue its operations without any distractions if the takeover was well controlled (Fraser and Simkins 2010:40). There are possible events and scenarios that are going to come out after acquisitions process is completed. All risks involved in all forms of acquisitions must be governed and control, including but not limited to the following (Fraser and Simkins 2010:40). Legal compliance, ethics, and risks must be proactively addressed, like all legal and regulatory requirements followed as well as risk factors. Appropriate indicators that will help with measures must be best endowed with management. Companies, especially state enterprises should be sensitive to issues of public concern. Compliance with regulations may even come from International bodies like World Health Organization (WHO), as evidenced in the case of Fukushima plant accident in Japan in 2011 (Yamashita, 2016).

7.1 Control of Risks after Mergers and Acquisitions

The Risk Matrix graph can, therefore, be used for all decisions made and everyday analysis to control business activities in the time of mergers. Laurence (2006), used a risk assessment matrix to allocate the likelihood of occurrence of a risk. An assessment of risks concerning their probability of occurrence and outcomes must be carried out. It will guide decisions by management. The process will address risk tolerance, the likelihood of failure and consequence of the event. Embedding a risk will accord the company to be able to demonstrate what is happening within. Management will then own and make decisive decisions which will be communicated and integrated in order to save the company from threats. The risk matrix is also used to measure the levels of potential hazards. Environmental hazards assessment must be included when identifying risks that are gauged by the risk matrix. Therefore, control of a company merger is of vital importance because the acquirer may suffer consequences which may collapse it. In cases of compensation to employees of the target company or retrenchments if necessary, proper procedures and retrenchment exercises must be followed. According to (Stankiewicz-Mroz, 2015), change in human resources will be expected, as well as re-evaluating the paradigms. Risks can be managed when in a process of an acquisition and there must be sufficient information on risks as well as experienced personnel. The management will then decide on action to be taken after the control of risk concerning the business. A decision then can be taken either to tolerate the risk, treat, transfer or even terminate. Monitoring and regulation is done looking at the fact that competition is taken out in firms that are merging. In Botswana for example, there is a governing body of competition among businesses and institutions called The Competition Authority.

8. Conclusion

The problems that are in companies in Botswana, a third world country to be precise, are a lack of need for cost synergies, compatibility of corporate cultures, size, time and nature of the deal. To make a merger to work after completion may become a problem. There is also a problem with limited due diligence, over estimate of potential synergies, lack of plan indecision. In some cases, stake holders are not even consulted on processes. A major challenge with acquisitions by the government is political appointments to key positions that require expertise and quality experience. The following suggestions can help with mergers and acquisitions in Botswana:

1. Transition after mergers and acquisitions – affirmative action policies if necessary must be put in place after merging. Localization must be considered so that the natives will benefit if merging involves foreign companies.
2. Supporting statutes from the government – Enactments and statutes must be availed by the law makers suitable for assessment indicators and strategies of company measures that should as well provide objectives. Strategic planning and objectives must address the risk appetite of the business.
3. A strategic approach for consolidations mergers and acquisitions – Transfer of skills should be the main purpose of allowing company consolidations, mergers, and acquisitions.
4. Put in place mechanisms and institutions for monitoring company activities – although there is already the competent authority in Botswana, it must be empowered to take serious actions against companies that do activities such as merging.
5. Implementation of policies and strategies for the investigation, prevention, redressing and removal of anti-competitive mergers and acquisitions. Also, monitoring compliance of merged entities with the decisions of the Authority, post authorization of the merger.
6. Appointments – Political appointments to key positions of state acquired companies must be made with skilled personnel, like Board members and CEO's of Competition Authority.

The intention and outcome of the study intend to sensitize companies about risk evaluation and control of mergers and acquisitions. Moreover, it is aimed to identify precise areas which lead to failure, in order to overcome risks and to strengthen these areas of concern. Alternatively, to identify those elements that have a negative impact on operations of the enterprise. Further quantitative studies on the subject are recommended in order to give more analysis on the subject.

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