Scottish Enterprise

The Role of Acquisitions in Company Growth

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A report for Scottish Enterprise

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EXECUTIVE SUMMARY

This report presents an overview of the structure of the acquisitions market in Scotland from 2003-12, before putting this into international context. It then begins to explore the underlying motivations behind the activity of Scottish companies through a randomly selected small group of case studies of Scottish Enterprise Account Managed companies. Both sales and acquisitions have been seen by companies as an avenue to achieve their growth objectives. Whether part of a deliberate strategy or arising out of spotting and seizing an opportunity, both avenues have been beneficial for Scottish companies and the wider economy. However, they still remain an under-utilised avenue for companies to grow.

The Account Managed companies interviewed felt a range of barriers prevented their organic growth including being unable to secure the necessary funds for investment, being unable to attract and retain the skilled staff required and in particular, being unable to offer a greater range of products and services in order to secure larger contracts alongside gaining access to new markets. Ultimately, these triggers have led to sales and acquisitions.

Account Managed companies saw a sale or acquisition as the most desirable avenue through which to achieve their objectives. They offered the safest and most efficient way in which to achieve growth, often bypassing the time and risk involved in organic growth. They have secured greater access to financial resources, a larger suite of products and services, expertise and skills of trained staff, as well as instant access to markets and clients previously inaccessible.

Both sales and acquisition fit within our existing understanding around company growth, with both potentially acting as a trigger point through which to initiate a period of growth, or sustain an existing period. From the experiences of those Scottish companies interviewed as part of this research, a range of factors were identified as being central to ensuring a successful trade sale or acquisition, central to which was strong company management with a clear plan, combined with an ability to recognise and seize upon opportunities. A lack of strong management and an inability to consider all potential alternatives heightens the risk of failure.

Activity involving Scottish companies shows a heavy reliance on the UK market, a stronger reliance than that of any comparable nation. Scottish companies are engaged in sales and acquisitions at an earlier age than their European counterparts, but median deal sizes suggest that whilst younger, the companies are of a size similar to older European firms. Meanwhile, Scottish firms who are acquired by another company (within Scotland or from elsewhere) have one of the highest post-deal active rates in Europe, suggesting that approaches to embed companies within Scotland are proving to be successful.

This aside, activity involving Scottish companies is broadly similar to that seen by firms of other European nations. A key difference is that Scottish companies are less active in acquisitions than nearly all comparable nations and experience fewer international trade sales as a percentage of its business base than several nations.

This initial work on the scale and activity of the trade sale and acquisitions market in Scotland provides a framework for further research in this area, in particular around the scale, range and impact of ‘recycling’ as a result of sales and acquisitions, to help shape understanding on the issue and how policy-makers can support companies to achieve their objectives. It has highlighted what can trigger and drive companies towards sales and acquisitions, and therefore what needs to be considered to provide support to these companies both before and during the process.

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INTRODUCTION

Preamble

Mergers and acquisitions (M&A[1]) have long been a prominent feature of business and its increasing frequency in recent years has led to it becoming an area of great interest, with domestic and cross-border deals focusing the minds of academics, policy-makers and governments alike.

In recent years, the number of cross-border and domestic M&A's has grown rapidly in many OECD economies. This growth has been very much in evidence in Scotland with observers noting the trend of inward acquisitions of major, well established Scottish companies[2] but also a string of outward acquisitions made by Scottish firms such as The John Wood Group and The Weir Group[3].

Whilst growth by acquisition is traditionally associated with companies who enjoy substantial financial resources, there are increasing signs that younger and smaller firms are starting to recognise their potential as part of a deliberate growth strategy.

Existing research identifies a range of reasons why businesses acquire or are acquired, including:

- In order to grow more rapidly, enter new markets, access new resources and funding, broaden their customer base and internationalise their operations. In short, create value by bringing two firms together which would not be realised by either company continuing to stand alone[4].
- To obtain new technology more quickly[5]. An increasing number of larger businesses are now based on a 'buy to build' strategy[6], since acquisitions allows existing internal resource constraints to be overcome.
- To achieve greater economies of scale by acquiring a firm within the same sector, eliminating competition and/or excess capacity in the sector. Greater efficiencies then lead to greater profits as well as allowing resources to be redeployed elsewhere in the business[7]. The same rationale can also instigate acquisitions out with the same sector, in order to secure control of a supply chain, often at a lower cost.
- To reduce the need and time to 'learn' by acquiring an established player in a particular industry to take advantage of their knowledge[8].
- Some businesses are established and developed by entrepreneurs with the explicit intention from the outset of achieving a sale and a return on their investment and that of others. For example, investors in businesses often view a trade sale as the main exit route to harvest their original investment[9].
- Establishing 'greenfield' operations in a new overseas market can be a slow process with firms encountering significant transactions costs such as regulatory approval and

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[1] M&As refer to the *'change in ownership in existing enterprises to achieve strategic and financial objectives'* (Measuring Globalisation: OECD Economic Globalisation Indicators 2010, Aug 2010, p. 102). In the overwhelming majority of cases acquisition rather than merger dominate flows in advanced economies.
[2] Ashcroft & Love (1993).
[3] Source; ZEPHYR
[4] Ahuja & Katila (2001), Haleblian, Devers, McNamara, Carpenter, & Davison (2009), Steger & Kummer (2007)
[5] Graebner (2004), Ahuja & Katila (2001)
[6] This is best exemplified by firms such as Cisco who have undertaken some 150 acquisitions over 30 years
[7] Haleblian, Devers, McNamara, Carpenter, & Davison, (2009)
[8] Hitt, Ireland, & Hoskisson (2001)
[9] Mason and Harrison (2011)

planning permission. Overseas acquisitions can enable firms to leapfrog these challenges.

There is little to no understanding of the shape and scale of the acquisitions market in Scotland, and within that how companies are using these in order to grow. This has led to speculation and assumptions over the role of acquisitions, fuelled by anecdotal evidence.

This report uses a randomly selected small group of Scottish Enterprise Account Managed companies who have been through trade sales or acquisitions to begin to explore their motivations and the factors that influenced their activity. It is important to highlight from the outset that these firms are account managed as a result of their potential for high-growth. Therefore, their considerations of the role of sales and acquisition may differ slightly from the majority of companies in the Scottish economy.

This study is also of policy interest for a number of reasons:

- To understand the prevalence of activity and the impacts on Scottish businesses of acquiring (and being acquired) allows us to begin to assess the overall importance of sales and acquisition in Scotland
- understanding the reasons for (and challenges of) adopting acquisition as a growth model or as part of a model for growth (versus organic growth) can help inform the role that Scottish Enterprise could play in assisting firms to adopt and follow this approach where appropriate
- understanding what options companies consider, which lead to a sale or acquisition and which factors are the most important in their decision-making.

At the outset of this work in autumn 2012, Scottish Enterprise acquired the ZEPHYR database that records acquisitions dating back to 2003[10]. ZEPHYR is considered to be one of the most comprehensive and authoritative sources of data on acquisitions in the UK. While such a database will never provide the complete picture of acquisition activity, it has proved to be a robust source of evidence into the acquisition flows within the Scottish economy.

As a result of initial evidence gathered from ZEPHYR, this work focuses only on acquisitions, excluding mergers as an area of study. The rationale for this is that the sample of mergers involved is simply too small to merit its inclusion. Over the period 2003-2012, just 2,960 completed mergers were recorded by ZEPHYR globally in contrast to 442,935 acquisition deals over the same period. Only 15 completed mergers involved a Scottish company being proactive and making the merger proposal, with a further 9 involving a Scottish company where they agreed to a proposal made by another party.

[10] Owned and managed by the Bureau Van Dijk, the owners of the FAME business database

LITERATURE REVIEW

Do acquisitions create value?

Existing literature centres on determining whether acquisitions create value. Evidence is somewhat inconclusive on the benefits to the acquiring firm and the wider economy, but this relates mainly to large scale acquisitions rather than those by SMEs. There is a notable trend that existing literature focuses the nature of acquisitions amongst large businesses rather than the SME business population. This has ultimately led to a gap in our understanding of the role acquisitions amongst SMEs can play in the economy.

One academic review reported that there was *"no evidence that acquisitions, on average, improve the financial performance (e.g. abnormal returns or accounting performance) of acquiring firms"*[11]. Subsequent studies concur, reporting that the majority of acquisitions create no or little value[12].

Whilst a major study by the M&A Research Centre[13] (MARC) into the economic impact of acquisitions on the UK economy found that acquisitions generate economic benefits in the short-term, a more in-depth analysis concluded that the majority of UK companies were unsuccessful in adding value through acquisitions and the long-term benefits to the UK economy are at best, ambiguous[14]. Further work by MARC has demonstrated how corporate takeovers stimulate growth in revenues and employment over the long-term, but this is as a consequence of the small minority that are successful, who add more value than the majority who fail to do so. Again however it needs to be emphasised these studies are based on analysis of publicly traded companies.

Evidence of the impact of acquisition on employment suggests that while there are examples of increases in employment at corporate level, most acquisitions are generally followed by a reduction in employment within the acquired firm[15]. Previous research by Scottish Enterprise on Scottish corporate headquarters found acquisition of a company has the potential to lead to a loss of autonomy and functions in the acquired company's HQ; that acquired companies are more vulnerable to closure; and that within about a decade of acquisition, employment in the acquired company had more or less halved[16]. Similarly, there have been numerous studies showing acquisition leads to turnover within top management teams within the acquired firms[17] but if the company survives then higher value jobs are often introduced to the acquired company[18]. This complex picture suggests the impact of each deal rests on unique elements specific to that deal.

Whilst some evidence points to improved innovation performance following an acquisition[19], other showed how acquisition in high-tech industries only contributed to improved innovation performance during the first couple of years post-acquisition before going into decline[20]. Studies have also found prior acquisition experience to have a positive influence on the

[11] King, Dalton, Daily & Covin (2004)
[12] Cardinali & Wikren (2012), Craninckx & Huyghebaert (2011), Graebner (2004), Hitt, King, Krishnan, Makri, Schijven, & Shimizu (2012) and MARC (2011)
[13] The Mergers and Acquisitions Research Centre is based in the Cass Business School, based at City University, London
[14] From studying the performance of publicly traded companies it should be noted.
[15] Harris, (2009)
[16] Botham, & Clelland (2005)
[17] Krug, & Hegarty (1997)
[18] Harris (2009) and Girma & Gorg (2007)
[19] Gautam & Riitta (2001)
[20] Cloodt, Hagedoorn & Kranenburg van. (2006)

successful assimilation of new acquisitions[21]. This would perhaps explain why some firms become 'serial acquirers', continually building on a 'tried and tested' model of success with further acquisitions.

Consideration of the economic benefits of acquisitions reflects on the location of the acquired firm and the actions of the acquiring firm. The acquiring firm may choose to keep the activity (for example employment and output) at the acquired firm's current location. In this case, the economic benefits are likely to be restricted and employment and GVA benefits are likely to be small, although there may be some wider spill over benefits from the wider global network both firms have access to. There may be cases where some employment such as higher value functions may shift from the acquired firm to the acquiring firm's location. Depending on whether the Scottish firm is the acquirer or the acquired firm will have a bearing on the benefits or otherwise of the acquisition.

If activity remains in Scotland, the economic impacts are likely to be restricted to the potential 'loss' of profits should the acquirer choose to repatriate them back to their home nation. Any shift in the high value aspects of the company away from Scotland would similarly result in a potential loss to the economy. However, if profits are recycled within Scotland it can stimulate further economic benefits.

The majority of evidence suggests that acquisition does not create value – although it needs to be emphasised that this is by no means universal. There are cases which show both acquisitions to be successful and unsuccessful, be that in terms of jobs or innovation or any other barometer of success.

Given that the balance of evidence suggests that the economic value of acquisitions is at best limited and at worst negative, research has concentrated on the elements of acquisitions that can create and destroy value. These factors can offer insight into how acquisition can be used as a model for growth and for policy-makers, it can highlight approaches and interventions which can ensure that companies are equipped with the skills and support to make the most of the potential that acquisitions present if and when the opportunity arises.

What factors are seen to create and destroy value?

Competing for market advantage

Taking two distinct companies and blending the strongest assets of both into a single company a significant challenge. Making acquisitions to realise synergies between the acquirer and target is the result of believing the value of the combined entities would be greater than if the two firms remained separate[22]. Research identifies two established methods through which synergies are sought; 'cherry picking' and 'buying lemons'[23].

Cherry picking is acquiring the best performing companies in order to secure their best assets, and bring them into the acquirer to yield greater overall profits[24]. In contrast, buying lemons can be either instigated by the acquirer or the target firm. The acquirer seeks to take advantage of an underperforming company to obtain a particular asset or knowledge to improve their performance. But when the target firm (or 'lemon') instigates its own acquisition, it is to seek a 'match' with a more effective performer in order to bring about greater performance.

[21] Bruton, Oviatt, & White (1994)
[22] Cardinali, A., Wikren, B. (2012) Raj, M. & Forsyth, M. (2004) and Berkovitch & Narayanan (1993)
[23] Department for Business, Innovation and Skills (BIS) (2011)
[24] Harris, R. (2009)

Jensen & Ruback (1983) and Healey et al (1992) found that where opportunities to realise synergies exist, bringing two firms together will and can deliver greater effectiveness, efficiency and profitability. Gugler et al (2003) found that the average profitable merger in their sample has increased company's' market power. A study by Clare and Faelten (2013) into the UK market (albeit looking at shareholder wealth as a measure of performance) found that acquirers have outperformed peers for three years after a transaction, adding approximately 10% of revenue and 9% in employment levels post-acquisition. Whilst both of these studies highlight how growth can be achieved through acquisitions, again they focus on the acquisitions of publicly traded companies.

As stated previously, an additional dimension is introduced when considering cross-border acquisitions. Harris (2009) finds that foreign (inward) acquisitions have not automatically led to improvements in efficiency and productivity in the target. Labour productivity has increased with a decrease in labour intensity through introducing the assets of the acquirer to increase productivity whilst there is also a drop in employment. This is not only to achieve the desired profitability gains but to bring the acquired company's operations in line with the new owners' requirements.

Impact of company management

The literature indicates strongly that the actions and decisions of management are the most influential factor on the success of acquisitions[25]. The recent Kay Review lamented many cases in the UK where poor decision-making had damaged the long-term success of companies[26] and continued following the recession[27], reinforcing the perspective that managerial hubris drives activity, as managers and CEOs compete through companies in order to fulfil their own personal objectives. This is seen as highly damaging, resulting in losses to the acquirer over the long-term.

Bouwman, Fuller and Nain (2009) and Scharfstein and Stein (1990) have also observed this pattern over time. Managers begin to mimic their peers' investment decisions and as a result, acquisitions gradually become more about keeping up with peers (via status and benefits) than realising synergies. Over time this behaviour is increasingly more damaging because 'late movers', who are simply mimicking other managers, are significantly more likely to make unprofitable acquisitions[28].

This is because the more attractive and suitable companies have already been purchased by the early mover managers (who were motivated by achieving profitability and synergy goals). This leaves firms for the late movers who are likely to be of poorer quality and less appropriate for integrating into the acquiring company.

Furthermore, since the early activity leads to an increase in market prices due to fewer available companies, prices are likely to peak at the time the 'late mover' makes their acquisition. This means they are not only more likely to be unsuitable for a successful acquisition but also overvalued, which makes them even more unsuitable. However, as Scharfstein and Stein (1990) point out, this is lost on management in these cases since their motivation is not to realise value; it is about protecting and enhancing their reputation, status and benefits.

Enhancing personal benefits is recognised as the principal motivation behind many acquisitions because acquisitions lead to an increase in the personal benefits to the acquiring manager, regardless of its success[29]. Agrawal and Walkling (1994) note that

[25] Lloyd Greif Center for Entrepreneurial Studies (2004)
[26] For example ICI and GEC, as set out in Kay, J. (2012)
[27] p.14, 2012
[28] Bouwman et al (2007) p.637
[29] Grinstein & Hribar (2004), Haleblian et al (2009), Harford & Li (2007), Jensen (1986),

acquisition attempts are more frequent in industries where CEOs have the greatest levels of compensation, cementing a clear and direct link between the level of acquisitions and managerial benefits, again from a publicly traded company perspective.

This managerial behaviour is not just about maximising personal benefits but also protecting personal status. Evidence shows that if acquired, managers are often replaced and because of this fear a series of defensive acquisitions begins (Gotton, Kahl and Rosen (2005)). An initial acquisition (or a small number of acquisitions) is made by one company, driven by realising a profitable opportunity. This sparks fears in other firms' management that they may become an acquisition target and therefore they seek to acquire to deter potential takeovers. This spreads throughout the particular sector (the authors note a sectoral structure exists which is more conducive to this type of behaviour – where a more evenly spread size of company leads to the increase in competition) as a defensive wave of acquisitions develops, principally to protect firms and managers rather than to create growth and realise synergies. It is as the authors say, a 'race for firm size'.

Turnover in management

Acquisition brings significant change, none more so than for the management of the acquired firm. As a result, Angwin and Meadows (2009) observe competing arguments over whether senior executives should be retained or replaced post-acquisition.

Whilst retaining the incumbent management keeps their firm-specific expertise and knowledge and provides continuity in leadership (recognised as an important factor in reducing employee uncertainty and negative reactions amongst the acquired firm's staff)[30], a study by Graebner found the acquired management can play a critical role in delivering the success of the acquisition through assuming a leading role, focusing staff in the acquired company and using their knowledge to deliver the new goals[31].

They can also play an additional role in realising the unforeseen benefits of the acquisition – the 'serendipitous' value. This is where the more effective acquired manager brings their unique skills and experience to exploit opportunities that arise which may not be obvious to incoming management[32].

However, an incumbent manager can also be an obstacle to change, with inflexibility in their methods and a commitment to old and rigid approaches. Angwin and Meadows (2009) note incumbent managers (who are often the founders of the company) can be seen as a barrier to the success of the acquisition, hence why they often find themselves replaced or demoted.

Changing management can inject fresh perspective, can focus on the objectives of the new owners and can enable the implementation of new ideas. They may import systems to deliver short-term performance objectives (assuming the company has underperformed in recent times). But, whilst new management can bring new ideas and methods, they will equally lack specialist skills and knowledge relevant to the new company, which can lead to cultural differences and clashes which prevent the realisation of goals for the company.

Regardless of the respective pros and cons, it is apparent most acquirers prefer a change in management. Angwin and Meadows (2009) as well as Krug and Aguilera (2005) find in the UK less than half of the acquired companies CEOs remain two years after the deal is completed and two-thirds of those leaving the company following an acquisition would not have done so had the acquisition not taken place. Half of these were involuntary terminated

[30] Angwin & Meadows (2009)
[31] Graebner, (2004) pp.759-768.
[32] pp. 768-772.

whereas the other half, whilst formally recorded as leaving voluntarily, would not have done so if not for the takeover[33].

Krishnan, Miller and Judge (1997) find a higher incidence of managerial departure in acquired firms when their backgrounds are similar to the acquiring manager, due to a lack of any compelling reason for retention. King and Hegarty (1997) observe a higher rate of turnover in cross-border deals than purely domestic ones, with the rate rising even further when the acquirer has prior experience in that country, again suggesting that acquirers need a compelling unique reason to retain incumbent managers[34]. This is not unanimous since there are cases where acquirers give local knowledge a higher value over standardisation.

Krug and Aguilera identify an interesting trend that it is in the immediate aftermath of deals is when incumbent CEOs depart, but after three years the departure rate for management installed following acquisition begins to increase significantly[35]. They offer two potential explanations for this pattern:

1. That the acquisition has been unsuccessful and not achieved its objectives, therefore someone must be held responsible.
2. The companies have been integrated post-acquisition and a new phase for the company is about to begin, which requires a different skill set amongst leadership.

Whilst much of the literature contemplates the rationale and consequences of replacing management, there is little consideration of what departing management goes onto do once they leave their position (often from a company they founded). Similarly, there is little understanding of the fate and futures of other Executive team members, as well as key and up and coming personnel which in turn limits the understanding of the scale of recycling as a consequence of acquisitions.

We know from Scottish Enterprise's research into High Growth and High Technology Firms[36] and prior work by Mason and Harrison (2006) that acquisition can trigger a process of 'entrepreneurial recycling'. This is where entrepreneurs use their newly acquired wealth, along with their experience of starting, developing and then selling a business, to engage in other entrepreneurial activities, notably (but not restricted to) starting new business ventures and investing in other businesses as business angels or venture capitalists.

Mason and Brown (2012) believe the key issue for economies like Scotland if they are to benefit from 'new' capital via inward acquisition is the size of the company before (and after) they are sold[37]. They argue that if acquisitions are typically of small businesses then the scope for reinvestment by the entrepreneur (be that through starting a new business, becoming a business angel, a mentor etc) is limited.

However, this simply addresses management who owned the business and thus received a return on the sale. It omits other members of management who may leave after being taken over. These individuals may not have received a return on investment to potentially re-invest, but they will have gained useful knowledge and experience to be applied in future. At present, this more rounded analysis of recycling remains a gap in our understanding.

[33] 2005, p.127-128
[34] As well as Krug and Aguilera (2005, p.130)
[35] 2005, p.127
[36] Mason & Brown (2012)
[37] 2012, p.69-70.

Ownership

Studies have shown the importance of ownership in determining acquisition activity, particularly amongst private firms. Bena & Li (2014) conclude that the location of the company's owner is a determinant of company activity since an overseas based owner increases the likelihood of a cross-border deal (compared to domestic, individual or family owner). In particular, a foreign owner is associated with 'genuine' international deals where the acquirer, target and owner of the target are from different countries. They find that those firms with a controlling shareholder are also less likely to be subject to a takeover bid from overseas. Larger firms and firms with a global financial advisor are also more likely to be targeted from overseas in contrast to older firms.

Ferrera, Massa and Matos (2010) observe that foreign institutional ownership increases the probability of a cross-border deal regardless of whether they are the acquirer or the target. In addition to that, they state that this brings a greater chance that the deal will be successful. Humphrey-Jenner, Satuner and Suchard (2013) take this further, noting that firms backed by private equity are more likely to be targeted in cross-border deals since financial owners have specialised knowledge which gives them an advantage. Given the prevalence for financial owners to be multi-national companies, they are better able to identify foreign acquirers who can help identify and then realise opportunities.

Firm Characteristics

In seeking to understand acquisition activity and patterns, existing research has considered a range of factors reflective of the firms involved. One of these is the size of the firm making the acquisition.

Whilst there are differing opinions regarding the overall benefit of larger takeovers, there is a prevailing view that smaller acquisitions have a greater chance of seeing their potential benefits realised[38]. MARC note that the gains of a minority of successful global firms[39] present the overall view that acquisition activity is a positive contributor to the UK economy when the overall picture is more unclear[40]. There is little empirical evidence however, which shows the effect of being a private firm in the acquisition process, and what this means for their growth. Of what is known, Craininckx and Huyghebaert (2011) find that when targets are private, returns are slightly better and failure rates are lower.

Whilst companies with a strong degree of relatedness achieve greater benefits from acquisitions than those seeking to diversify[41], evidence also shows there is a point when the two companies are too similar and there is a lack of unique elements being brought together. This increases the likelihood that the acquisition is likely to prove unsuccessful.

Often firms only look at diversification when their particular industry enters a downturn. Yet Lamont and Polk (2002) find firms diversifying to mitigate a shock in their current industry see their value decrease. Kaplan and Weisbach's longitudinal study (1992) of large acquisitions found that these acquisitions are four times more likely to be divested than acquisitions of related firms.

Cross-border acquisitions

Cross-border acquisitions not only present a greater set of opportunities, but an additional set of challenges[42]. Their increased complexity leads to cross-border acquisitions often

[38] Cardinali & Wikren (2012), Gotton, Kahl & Rosen (2005) and KPMG (2007)
[39] Such as BP, AstraZeneca and Reckitt Benckiser
[40] 2011, p.5
[41] Ahuja & Katila (2001, p.217), Cardinali & Wikren (2012), Cloodt, Hagedoorn, & Kranenburg (2006, p.650), Hitt, King, Krishnan, Makri, Schijven, & Shimizu (2012) in Faulkner et al (eds)
[42] Hitt et al (2012)

having less success due to the increased need for local knowledge, cultural understanding and expertise of regulation in the host nation[43].

Firms engaging in cross-border acquisitions experience significantly lower announcement effects (from analysis of stock performance) than those acquiring domestically[44]. However Scherer and Ross (1990) show that when the acquiring nation has superior management techniques, systems or processes then it is often easier for the cross-border acquisition to deliver the value required.

Inward acquisitions also present challenges for policy-makers and Governments in the target nation through the increased possibility that plants will close as part of a restructuring[45] since whilst Harris finds foreign acquisitions generally increase labour productivity they also bring a decrease in labour intensity as investment and new practices are used to achieve the required profitability gains. This represents a challenge for smaller nations experiencing significant levels of inward acquisition to retain the economic value within the nation and not see benefits repatriated back to the nation of the acquiring firm since evidence from Germany noted that plants who are not exporting when acquired are far more likely to be closed[46].

Learning from experience

One aspect universally regarded as having a positive influence on acquisitions is prior experience. Harding and Rovit (2004) find that top deal makers prefer a succession of small deals as opposed to 'mega-mergers' in order to implement their own success formula. Denison et al (2011) notes how prior experience and knowledge of acquiring within a particular country prepares firms for the challenges involved, including legal and regulatory frameworks thus making the deal more likely to prove successful[47]. However, evidence also shows that future acquisitions may not always yield the same benefit due to *"inappropriate application of prior experience"* (be that same location, sector or simply using similar approaches)[48].

Graebner takes this further by explaining how serendipity (principally in earlier acquisitions) can bring unplanned value through how acquired management is utilised[49]. He believes that earlier in its growth strategy companies are likelier to have vacant positions the acquired manager can fill, and take on cross-organisation responsibilities to help to harness the value of the acquired company. They are particularly suited for such roles as they know the acquired company, its staff and its strengths greater than anyone. But as future acquisitions are made, due to a lack of available similar positions for management from acquired companies, Graebner believes the opportunity for serendipitous value to arise diminishes, which could in part explain the declining performance of subsequent acquisitions over time.

Payment

Evidence highlights that cash offers are more successful than deals including stock[50]. Loughran and Vijh (1997) found that on average, those companies including stock earn significantly negative returns of -25% compared to those using cash, who offer excess returns of 61.7%. Sudarsanam and Mahale (2003) distinguish between 'value acquirers'

[43] Cardinali and Wikren (2012), Ravenscroft and Sherer (1987)
[44] Goergen & Renneboog (2004), Martynova & Renneboog (2006)
[45] Harris (2009)
[46] Andrews, Bellmann, Schank & Upward (2007)
[47] This is cultural familiarity theory.
[48] Finkelstein & Haleblian (2002), Graebner (2004), Haleblian, & Finkelstein (1999) and Zollo & Singh (2004).
[49] 2004, p.773
[50] Including Cardinali & Wikren (2012), MARC (2011), KPMG (2007) and Goergen & Renneboog (2004)

motivated by securing growth opportunities and using cash to finance deals; and 'glamour acquirers' using overvalued equity to supplement cash offers[51].

Over the three year post-deal period, they find value acquirers outperform the glamour acquirers and using cash generates a higher return, regardless of the company's status as either glamour or value acquirers. Travlos (1987) observed that the use of stock conveys a message to the market that the bidding firm is overvalued and the acquisition is highly unlikely to realise any value.

Overpayment can occur when a high price is put on the target by management, and driven by a manager motivated primarily by personal benefits and not the realisation of value; the acquiring company agrees to meet this price. It can also occur when as described earlier, a wave of acquisitions develops, sparked competition amongst managers, leading to higher premiums brought about by fewer companies being available[52].

Friendly vs Hostile

A further factor, which again reflects the predominant focus in the literature on publicly trading companies, is whether the deal is a hostile or a friendly takeover. Raj and Forsyth (2004) find that hostile takeovers are more effective, hypothesising this is because the bidder extracting its planned value ruthlessly. In a hostile takeover, firms are less concerned and have less need to portray a consensual approach. Therefore, it is not surprising that Cash and Guest find that hostile takeovers improve performance in underperforming businesses, but note that there is little evidence suggesting they can act as a disciplinary function and completely stop the non-value maximising behaviour of target companies[53].

Whilst there are immediate benefits brought about by the restructuring of the acquired company, Cardinali and Wikren note that hostile takeovers do not destroy value in the long-term[54]. This again highlights the prevalence amongst existing research to focus on acquisitions involving public companies. Being able to track share performance over time allows research to identify if an acquisition has created value. Yet in doing so this only focuses solely on share prices, missing other aspects within the two companies which can explain what can create or destroy value.

Despite the level of media and political attention given to 'hostile' takeovers, the number of hostile acquisitions is negligible. This may explain why they are deemed more successful, but in terms of the objectives of this research, 'hostile' vs 'friendly' acquisitions remains firmly in the background, simply due to its scarcity in the sample from across Scotland.

<u>Environmental Factors</u>

Timing

It is unsurprising research has noted the importance of timing since companies stock performance, lead-in time as well as post-acquisition share price can be analysed. The M&A Research Centre (MARC) emphasise that those who 'time' it right, i.e. announce an acquisition when their own share price is at a peak compared to the equity index, can suffer if they buy over-valued targets as a consequence of over-confidence in management as well as a tendency to include stock to finance the move. However, in the short-term there are significant short-term benefits which MARC say is worth £178m per deal (the cumulative average abnormal returns 40 days post-acquisition)[55].

[51] Also noted by Fun, Lin & Officer (2013)
[52] MARC (2011) p.5, Bouwman, Fuller & Nain (2009), p.635
[53] 2001, p.5-6
[54] 2012, p.12
[55] 2011, p.10

So their conclusion and that of others[56] from high-value markets is that this is not a good time to acquire, pointing to the negative long-term performance, despite the initial peaks and even a lower long-term performance than low-value market acquisitions (which still underperform). Low-value market acquisitions are believed to be more beneficial due to low prices, which give an increased chance for achieving growth following the deal.

In a downturn, acquisitions can be more attractive due to the lower prices of firms which offer the potential to secure a value price for a company. The pressure to complete the deal is also lower; acquirers can take their time and find firms best aligned with their long-term objectives. This can allow acquirers to find firms that are financially solid but due to the economic climate have weak levels of profitability.

National culture

The literature proposes two explanations for why culture matters. The first is known as economic nationalism[57]. Dinc & Erel's study (2013) demonstrates protectionist, nationalistic tendencies against inward acquisitions increased with more right leaning governments as well as governments with smaller majorities. This has a direct economic impact with 70% of bids resisted by national Governments ultimately failing, compared to a 27% failure rate when 'support' (or at least no objection) is expressed by the Government[58]. Interventions can also deter future acquisitions in these countries as companies choose to invest elsewhere without this hostility.

Their study found the most outspoken governments were the French, Spanish, Italian and Portugese. The authors report no instances of negativity from the UK Government, reflecting their long-standing perspective that country of origin matters less than the quality of the bidder and the proposal made[59].

Dinc and Erel demonstrate that economic nationalism is neither ideologically nor economically driven. Factors like unemployment and GDP have no bearing on its frequency. Instead sociological reasons drive political factors via the electoral cycle. For example, they note Government have a more hostile approach to proposed acquisitions when immigration (not specifically from the country of the bidder) is perceived to be a problem by the electorate.

Bena and Li (2014) as well as Ahern, Daminelli and Fracassi (2012) go further, introducing cultural familiarity as the second explanation why national culture matters. They demonstrate the number of cross-border acquisitions increasing when key elements of 'trust' between nations are stronger. Leuz, Lins and Warnock (2009) find outsiders invest less in countries with poor outsider protection, poor disclosure rules and national governance issues. Denison et al (2011) show firms are less likely to acquire in culturally distant countries and when they do, have poorer post-integration performance[60]. The larger the cultural and/or

[56] Bouwman et al (2007), p.635
[57] Feiler (1935) and Seers (1983) are seen as the founding observers of economic nationalism theory
[58] The limits to which national Governments can prevent takeovers are limited. Dinc and Erel authors chose the EU for their study into the prevalence of economic nationalism because of the primacy of the European Commission as the anti-competition authority, which meant a nationalistic approach cannot be described as pro-competition. The arbiter of competition matters falls back to the domestic government and their respective Competition Authority when more than two-thirds of the turnovers of both companies take place in that country, thereby making it less likely that the bidder is seen as a 'foreign' company. The role of the Commission also largely reduces national government's actual power in regards to blocking acquisitions to little more than as an interested party.
[59] Repeated at a BIS Select Committee (26 March 2013) by the Sec. of State for BIS and in the Government's response to one of Lord Heseltine's recommendation for managing the acquisitions market to a greater extent, a recommendation widely seen as based in economic nationalism.
http://www.parliamentlive.tv/main/Player.aspx?meetingId=12925
[60] Datta and Puia (1995), Lee, Shenkar, & Li (2008), Li & Guisinger (1991), Shenkar (2001)

trust gap between the two nations the lower the volume of acquisition and the less successful those acquisitions that do take place are.

Whilst the majority of evidence points to cultural familiarity discouraging acquisitions between diverse nations, Chakrabarti, Mukherjee and Jayaraman (2009) show the opposite; showing how acquisitions in culturally diverse nations can prove more successful because of the greater differences allowing for the development of larger synergies than between two broadly similar cultures. Whilst this does not disprove the majority of the research it serves as a reminder that each acquisition is different, bringing together a unique set of factors produce unique outcomes.

Conclusions

Research casts doubt on whether acquisitions can create value for companies. However, this is predominantly based upon analysis of publicly traded companies. There is an evidence gap at the SME level in understanding acquisitions and in particular how acquisition is being used as part of a growth strategy. Whilst existing literature is limited given its focus, it has still identified factors which may apply at the SME level.

It is clear companies acquire for many reasons; predominantly around creating value. It is also apparent other self-interested factors play a role in acquisitions, so much so that the UK Government has considered this aspect and its effects through the Kay Review. These serve to highlight the importance of company leadership and management and understanding the motivations and decision-making processes will provide insight into the role of acquisitions in growth strategies.

This is because as Denison et al note there is little existing evidence which looks at the *"role of M&A in a corporate growth strategy"*[61] as organic growth and growth via acquisition are presented as alternative strategies when the reality is they can complement each other as part of an overall business strategy. Prior research by SE (2012) demonstrated company growth is rarely linear and occurs periodically through a series of 'trigger points'. This suggests organic growth can be complemented by acquisitions in order to trigger or accelerate a period of growth. Work by Nesta (2014) highlights acquisition activity as a feature of high-growth firms, developing further the link between acquisition and growth.

What is apparent as well as obvious is that acquisitions are complex and unique, especially when they are made across borders. Cross-border acquisitions face greater scrutiny and are seen as more contentious because of the perception that inward acquisitions lead to negative economic consequences for the wider domestic economy. Existing research highlights both positives and negatives from the foreign acquisition of an indigenous firm.

It could be argued that existing consideration of the consequences of the deal is narrow, restricted simply to entrepreneurial recycling based on the size of the company at the time of sale and the futures of ownership, management and financial backers. This excludes the benefits over time for all those involved in the company (such as salaries, training, skills) as well as those linked to the company through the supply chain, the payment of taxes as well as reputational benefits to places, sectors and individuals. Acquisition is simply one stage of a series of constantly evolving processes and circumstances. These gaps and further questions in existing research provide further specific areas for this research to consider in pursuit of its objectives.

The next chapter briefly outlines the methods used in this study before exploring the make-up of the Scottish acquisitions market between 2003 and 2012 and comparing the Scottish market with that of neighbouring nations.

[61] 2011, p.112-113

METHODOLOGY

Aims and Objectives

The aim of the research was to understand the role that acquisition can play in the growth of Scottish companies. The research had the following objectives:

1. To provide a comprehensive overview of the acquisitions market within Scotland over the past decade;
2. To consider the role and impact of acquisitions on company growth;
3. To highlight the impact of acquisitions on the Scottish economy;
4. To provide insights into the acquisitions market to help inform Scottish Enterprise's policies and practices (as well as that of others).

This research was carried out in two stages, combining quantitative analysis of data with qualitative research in the form of interviews.

Quantitative Analysis

As previously referenced the ZEPHYR database was acquired to provide an overview of the Scottish sales and acquisitions market. ZEPHYR, part of the Bureau van Dijk network of business information, is regarded as the leading database for Mergers and Acquisition activity globally and is updated hourly. It contains information on M&A, IPO, private equity and venture capital deals and rumours, and its link to the FAME database provided the opportunity for further analysis should that have been necessary.

ZEPHYR mainly includes information on acquisitions above £500,000; therefore acquisitions of small companies may be underrepresented. In addition to this, clearly it depends on information on deals being publicly available and in turn the submission of information from their various teams around the globe. Therefore, it is important to emphasise that whilst ZEPHYR has provided an excellent insight into the acquisitions market not just in Scotland, but across similar European nations, it does not cover every deal.

A search strategy was established to look at completed deals within Scotland across a ten year period spanning 2003 through 2012. Initial analysis of the Scottish acquisitions market was carried out, to present a range of data discussed in forthcoming chapters. The analysis was broken down into three main categories of acquisition, namely:

- Inward acquisitions – where a non-Scottish company acquires a Scottish company
- Outward acquisitions – where a Scottish company acquires a non-Scottish company
- Intra-acquisitions – the acquisition of a Scottish company by another Scottish company

From here, a cross-analysis exercise was carried out with a database developed to assist and inform an Evaluation of Scottish Enterprise's Engagement with Account Managed Companies[62]. This identified a range of companies who had been account managed by Scottish Enterprise over the period 2003 through to the end of 2012 (NB. Many of these companies may not have been account managed at the time of their acquisition).

[62] Available at http://www.evaluationsonline.org.uk/evaluations/Search.do?ui=basic&action=show&id=530

This analysis found:

- 89 present or former Account Managed companies had been acquired from outside Scotland (inward acquisition);
- 79 present or former Account Managed companies had made acquisitions outside Scotland (outward acquisition);
- 44 present or former Account Managed companies had made acquisitions within Scotland (intra acquisition); and
- 25 present or former Account Managed companies had been acquired from within Scotland (intra acquisition).

Concurrently, the ZEPHYR database was analysed further in order to provide international data for a range of similar nations, adopting the same approach and methods as that used for the data for Scotland, in order to enable comparison with Scotland's performance on a range of key measures. An analysis of this is presented in Chapter 4.

Qualitative interviews

A randomly selected group of past or present Account Managed companies from across each criterion was selected, to approach with regard to conducting an interview addressing their experiences of acquisition. The selection criteria was simply to construct a shortlist which not only spanned across each of the three types of acquisition[63] (inward, outward, intra) but which broadly reflected a range of company sizes, sectors and location.

This would provide a qualitative aspect to complement the data findings of ZEPHYR, but was never intended to be fully comprehensive and cover all aspects. Its aim instead, was to provide case studies which met the objectives of the research – to consider how Scottish companies have used acquisitions as part of company growth.

Account Managers from Scottish Enterprise were approached to facilitate the approach to the company, and in some cases they made the approach themselves as part of their regular contact with the company. This ensured that they were part of the process and supported access to senior management within each company.

An outline of the research objectives was provided, and as a result the issue of confidentiality and anonymity was raised. At this time, given the objectives of the research it was believed that it would not negatively impact the work to grant this confidentiality to companies.

In total, twelve interviews were conducted between November 2013 and January 2014 with a diverse range of companies, from across multiple sectors and all with different experiences of acquisition. A summary of these companies is presented at Figure 1. Interviews were conducted face to face at the offices of each company with a range of senior figures in each firm, including Chief Executives, Managing Directors and Finance Directors, and lasted approximately one hour. Interviews followed a semi-structured approach with a core set of key questions applicable to all (regardless of the type and number of acquisitions the company had gone through) supplemented by further questions depending on the issues raised by the interviewee.

It was felt that a more general discussion rather than a structured and rigid approach to interviews would allow the individual experience of each company to emerge, providing much more valuable and insightful information, which may not have emerged with a single format being applied to all interviews.

[63] As interviews proceeded, it became apparent that several companies being interviewed had participated in multiple acquisitions, which often were of multiple types e.g. inward and intra.

Figure 1: Profiles of companies interviewed

Company Sector	Inward Acquisition (Trade sale)	Outward Acquisition	Intra-Acquisition
Food & Drink	X		X
Technologies and Advanced Engineering	X		XX
Technologies and Advanced Engineering		X	X
Financial Services		XX	
Life Sciences	X		
Food & Drink			X
Energy	X		
Energy	X		X
Non-Sector	X		
Food & Drink		X	
Energy		X	
Non-Sector	X	X	

Granting anonymity in the interview process allowed interviews to really explore details of each acquisition, understanding the journey that companies have been on and why they made the decisions they did. The confidentiality has allowed senior management to confidently reflect on their experiences of acquisition, and what had worked well but also what had not worked and how they would have done things differently, if at all.

The detail from interviews was analysed using coding based on the core interview questions, which allowed a series of themes to emerge organically. These themes are also outlined and debated in forthcoming chapters of the report.

SCOTLAND'S ACQUISITION MARKET: A STATISTICAL BREAKDOWN

Between 2003 and the end of 2012, ZEPHYR recorded the following number of deals involving Scottish companies:

- 664 inward acquisitions, where a non-Scottish company acquired a Scottish company
- 458 outward acquisitions, where a Scottish company acquired a non-Scottish company
- 284 intra-acquisitions, the acquisition of a Scottish company by another Scottish company

Before detailing how the acquisitions market in Scotland is structured, in order to provide some context, the following short section briefly summarises the global acquisitions market and some significant shifts which have occurred within the past decade.

The global environment

In recent years, the global sales and acquisitions market has been subdued as the international economy continues to recover from the financial crisis. Over this time Ernst & Young's (E&Y) analysis of global M&A indicates a shift from West to East and from traditional powerhouse nations of the US and the UK (who still remain highly relevant) to new and emerging markets in Brazil, Russia, India, China and South Africa (BRICS).

Whilst their rapid rise from 2007 slowed during 2012 and 2013, the BRIC countries' share of value in the market increased from 7% to 15% in the five years from 2007. The Eurozone's share declined from 21% to 11% whilst the US market halved in value at a time China's M&A market doubled[64]. E&Y's Maturity Index also reflects the level of competition from the East with Singapore, Hong Kong, South Korea, China and Japan moving into and up the top ten. Nations such as Thailand, Malaysia, UAE also rose up the rankings alongside other emerging markets in Czech Republic, Poland, Chile and Turkey.

The United Nations Conference on Trade and Development's (UNCTAD) latest trend monitors shows that BRICS nations continue to grow both as recipients of foreign direct investment (FDI) and as major players in investment[65]. Their global share of FDI inflows trebled to an estimated $263bn in 2012, some 20% of global flows, up from 6% in 2000. Outflows increased from $7bn in 2000 to $126bn in 2012, with 34% of this being invested in the EU. 2013 saw this pattern continue as flows (mainly driven by acquisition activity) to developed countries, continued to decline at the expense of flows into developing and transitional economies. These nations have also showed greater resilience to the economic crisis, with outflows only dropping 26% in 2009, compared to a global decline of 41%.

[64] http://www.ey.com/GL/en/Newsroom/News-Releases/News_2012-Global-M-and-A-values-half-that-of-2007-book

[65] UNCTAD Global Investment Trends Monitor, No.11 (January 2013), No.12 (March 2013) and No.13 (October 2013).

The UK Market

The UK Government refer to the acquisitions market as a *'vital part of a vibrant market economy'*[66]. Despite recent proposals for Government to take a more active role in acquisitions, including a recommendation by Lord Heseltine for Government to more pro-actively use its powers in regards to M&A from outside the UK[67], the UK Government believe their role is appropriate and took the opportunity to reaffirm that *'the UK is open for business'*[68]. This debate has recently re-surfaced in relation to Pfizer's proposed takeover of AstraZeneca. Prior to this, even the Kay Review, weary of short-termism prevailing amongst managers looking to acquire for the sake of it, advocated a hands-off approach, believing it was not the role of Government to correct decisions freely made in the market[69].

Despite a decline in activity since the recession[70], the UK is the biggest sales and acquisitions market in Europe, well ahead of France and Germany[71]. Within this depressed market, the Confederation of British Industry (CBI) advocated reforms to de-regulate takeovers when the total turnover of both companies is under £5m. They believed this would stimulate growth in areas of the economy particularly affected by the crisis and the subsequent squeezing of credit conditions, therein unlocking the opportunity for more companies to grow[72]. Again, this indicates a perspective that acquisition can be an approach through which to achieve company growth.

Data from Experian for Scotland highlights the impact of the downturn on mid-sized companies. Whilst in 2012, their records showed a 21% increase in large value deals with Scottish involvement, mid-market deals saw a decrease of 19.3% in volume (23.5% in value) and small value deals saw a decline of 42.7% in volume (a 4.5% decline in value)[73].

Despite this evidence suggesting a lack of activity was constraining growth, the Government did not believe there was a strong enough case to deregulate this aspect of the economy, believing that such a move may result in acquisitions taking place without any scrutiny and therein proving detrimental to the economy[74]. Given that existing evidence points to smaller deals creating the most value for companies and growth companies being more successful when considering acquisitions as part of a company growth strategy[75], this is critical. The lack of activity in this part of the market could be hindering the opportunities for companies to grow.

Acquisition flows outwith and within Scotland

Current export flows for Scotland show a dominance of culturally similar markets. Scotland has significant levels of investment from the United States, France, Sweden and Norway, with less from more culturally diverse nations such as China and India[76] as well as other

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[66] Department for Business, Innovation and Skills (BIS) (2010). *A Long-Term Focus for Corporate Britain: A Call for Evidence.* BIS, London.
[67] Heseltine, '*In Pursuit of Growth'*. (2012) p.151-154.
[68] HMT/BIS (2013) p.21.
[69] The Kay Review (2012) p.59-60.
[70] Ernst & Young (December 2012) *'UK M&A Values Plummet over 65% in 2012 Compared to the Credit Boom of 2007'*
[71] Experian (2012) *Advisor League Tables 2012 – International – Deal Volume and Value*
[72] Confederation of British Industry (CBI) (March 2011). 'Competition Reform must unlock investment and make system more efficient'.
[73] Experian (2013) Advisor League Tables and M&A Activity Full Year 2012: UK and Republic of Ireland – Deal Volume and Value.
[74] BIS (2012) p.43-44
[75] Cardinali & Wikren (2012) p.13.
[76] Ernst & Young (2013). No Room for Complacency. 20013 UK Attractiveness Survey – Scotland http://www.ey.com/Publication/vwLUAssets/2013_Scotland_Attractiveness_Survey/$FILE/EY_2013_Scotland_Attractiveness_Survey.pdf

emerging BRICS nations who are becoming increasingly important in global foreign investment flows.

Data from ZEPHYR reinforces these export investment flows, with both inward and outward acquisitions reflecting export flows with nations culturally similar to Scotland than others.

Figure 2: Location of companies acquired by Scottish companies and acquiring Scottish companies (2003-12) and Scotland's top export markets (2012)

Location of companies acquired by Scottish firms (outward acquisitions)		**Location of firms acquiring Scottish companies (inward acquisitions)**		**Top 10 Scottish export trading partners (2012)**	
Rest of the UK	42%	Rest of the UK	44%	Rest of the UK	£47.6bn
Scotland	38%	Scotland	31%	United States	£3.6bn
United States	6%	United States	8%	Netherlands	£2.7bn
Ireland	2%	Norway	3%	France	£2.2bn
Australia	1%	France	2%	Germany	£1.5bn
Netherlands	1%	Ireland	1%	Norway	£920m
India	1%	Australia	1%	Switzerland	£870m
Norway	1%	Netherlands	1%	Spain	£830m
Canada	1%	Germany	1%	Ireland	£815m
France	1%	Canada	1%	Belgium	£735m

Source: ZEPHYR and The Scottish Government, Global Connections Survey (2013[77])

Whilst the similarities could be reflective of economic strengths; for example Norway for its oil and gas sector, it also reflects the predominance of the English language, a further signifier that cultural familiarity as a major factor in acquisition activity. Geographical proximity also appeals to be a strong determinant with only Australia and India requiring long-haul travel.

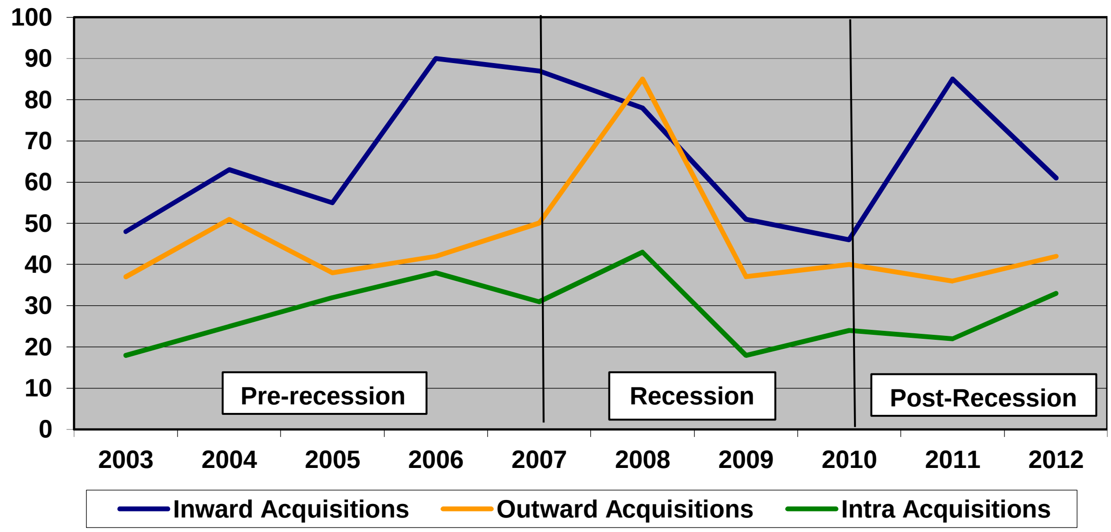
The lack of activity from the BRICs nations is striking as is the lack of any significant change in recent years despite the recent global trends showing their growing influence.

Volume and size of acquisition activity

Analysis of the number of deals over time (Figure 3) suggests the downturn did not act as a barrier to prevent those firms wishing to acquire or complete a trade sale from doing so.

[77] Data available from http://www.scotland.gov.uk/Topics/Statistics/Browse/Economy/Exports/GCSData

Figure 3: Time series data on Scottish acquisitions (2003-12)



Source: ZEPHYR

The trends can be broadly split into three stages – pre-recession (2003-2007), during the recession (2008-2009) and post-recession (2010 onwards).

***Pre-recession*:** A near 40% increase in inward acquisitions between 2005 and 2006 reflects conditions experienced at the time, buoyed by strong financial markets and easy access to finance for companies wishing to expand.

***Recession*:** Whilst the volume of inward acquisitions tumbled consistently from a peak in 2006 through to 2010, both outward acquisitions and intra-acquisitions rose sharply in 2008 before a sharp decline in 2009. The fall in inward acquisitions is unsurprising given the influence of Europe and America within the Scottish acquisition market. Difficult global conditions may have forced firms to focus on domestic markets and not expend additional time and resources on pursuing overseas acquisitions.

The increase in acquisitions made by Scottish companies could perhaps be seen in the context of the downturn in the UK not being as severe as within the Eurozone as well as Scottish companies taking advantage of the difficult conditions to make acquisitions at advantageous prices. This may have been to secure a supply chain or a company who may have been in difficulty because of the recession. The assumption is that making acquisitions at this time has a greater chance of achieving desired benefits due to lower prices and acquirers undertaking additional due diligence in a less pressured environment to ensure the success of the deal.

The reason for the sharp increase preceding a steeper decline for both types of deals in 2008 could be partially due to businesses believing an acquisition in a recession would be beneficial and even that the recession would be temporary; therein this activity created a mini-wave which failed to sustain itself in the face of the depth of the global recession, leading to a subsequent reduction in deals.

***Post-recession*:** Acquisition numbers post-2010 remains sluggish, reflecting ongoing global economic conditions. Given Scotland's heavy reliance on acquisitions with a small group of nations, continuing to feel the impact of the recession from 2007-08, this pattern is unsurprising.

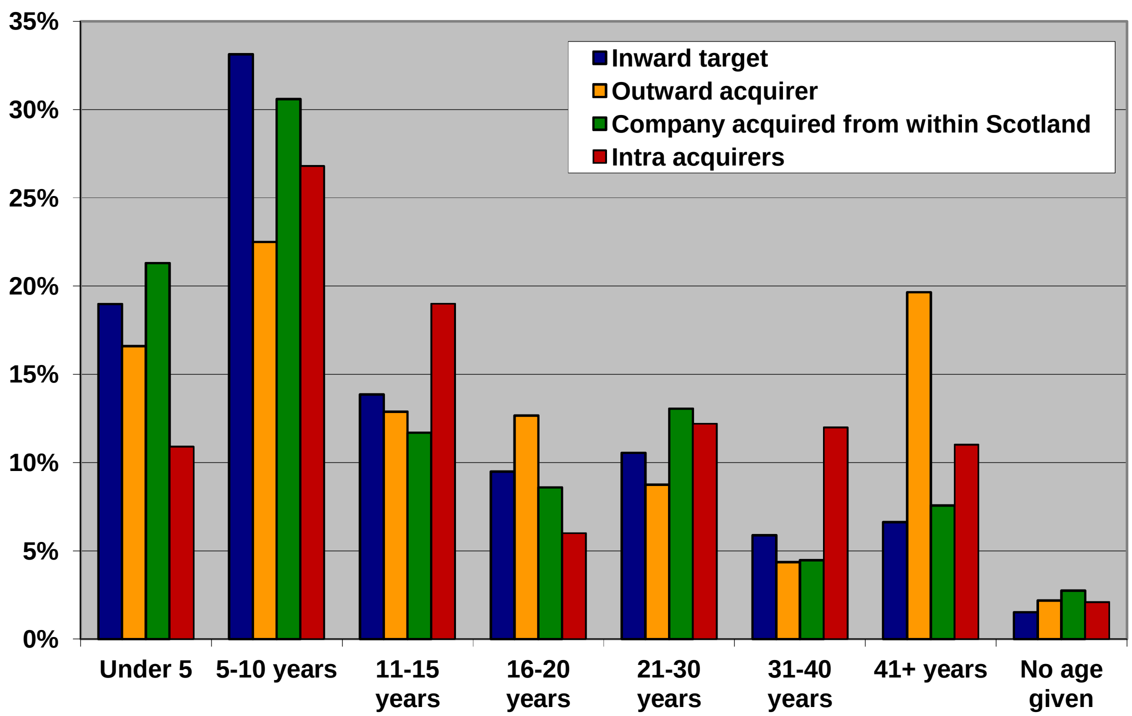
The one trend which is out of sync with this explanation is the sharp increase in inward acquisitions into Scotland during 2011, for which a few potential reasons could be proposed as an explanation:

1. As a result of clear Government support for inward investment into Scotland; mixed with strong support from the public sector through mechanisms such as Regional Selective Assistance for example;
2. Competitive business environment (low interest rates compared to other nations);
3. The poor economic performance combined with political turbulence in rival nations, particularly in the Eurozone. In contrast to nations such as Spain, Italy and Portugal, Scotland offered a stable environment in which to invest for those companies looking to do so.

Company maturity

One of the key issues highlighted by previous research by Scottish Enterprise (2012) is the age at which companies are acquired. Figure 4 demonstrates that, at over 50%, the greatest proportion of Scottish firms being acquired (be that from outside or within Scotland) occurs within the first ten years. The first decade is also the time at which companies are more likely to engage in both sales and acquisitions, in particular between 5 and 10 years[78].

Figure 4: Age of Scottish firms involved in acquisitions (%) (2003-12)



Source: ZEPHYR

Trading status

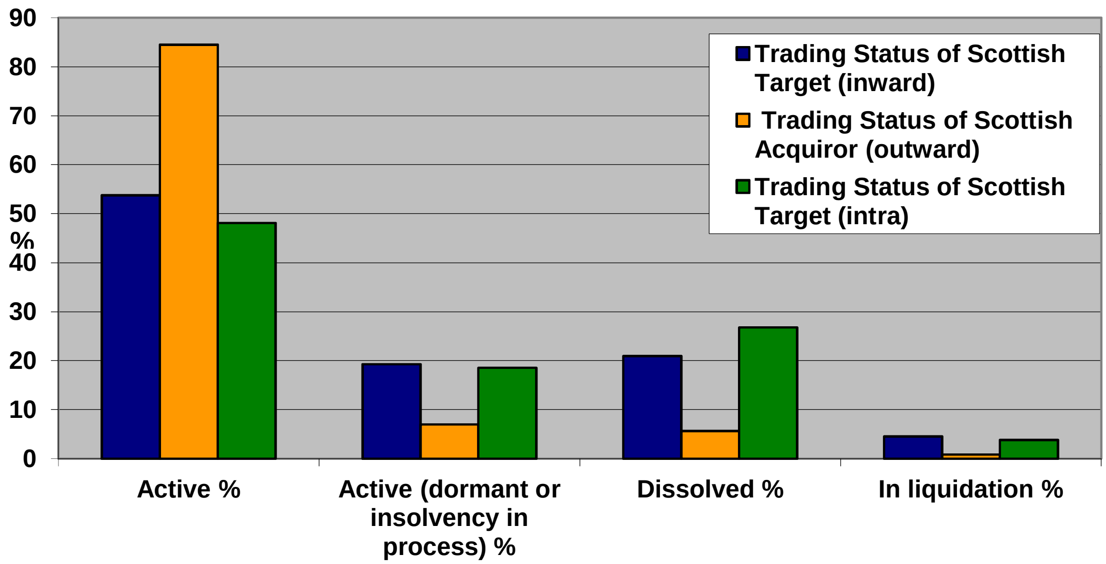
Analysis of the trading status of firms, as set out in Figure 5 shows as would be expected, Scottish companies making acquisitions overwhelmingly remain active with lower post-

[78] The spike in outwards acquisitions from the age of 21 and over is influenced by The John Wood Group PLC who made fifteen acquisition deals over the period thus abnormally inflating the data for this group.

acquisition active rates for acquired Scottish companies (54% for those acquired from overseas, and 42% for those acquired from within Scotland).

One in five Scottish firms (21%) acquired from outside Scotland were dissolved which is lower than companies bought within Scotland (27%). This suggests that more often than not companies are acquired from outside Scotland to enhance the buyer rather than to eliminate a competitor. It could also suggest Scottish firms are slightly more likely to be bought domestically in order to expand market share or eliminate competition for the acquirer.

Figure 5: Current Trading Status of Acquired Scottish Companies and Scottish Acquirers (2003-12)



NB: Figures reflect trading status at 31 December 2012 Source: ZEPHYR

It is worth highlighting the potential that the recession may have, as a result of a pressure to reduce costs, increased the rate of dissolution and even liquidation, but the dissolution or dormant status of the acquired company could equally reflect of a failure to achieve the desired outcome.

Deal Totals and Deal Size

Figure 6 shows the total value of acquisitions over time, and demonstrates how one large deal can overshadow all others in a particular year and drive up the annual average deal size.

Figure 6: Total value of acquisitions – by year

Completed Year	Inward Acquisitions	Outward Acquisitions	Intra Acquisitions
2003	£4,569m[79]	£3,732m[80]	£42.5m
2004	£1,032m	£5,095m[81]	£133.5m

[79] £3.2bn was a consortium's acquisition of Atlantic Water Inc, Northumbrian Water's holding company
[80] £1.5bn of which was The RBS Group acquiring Churchill Insurance
[81] £3.3bn of this was the acquisition by Lehman, Banca IMI, The RBS Group and Barclays of Fondo Inmobili Pubblici

2005	£3,086m	£1,334m	£773.9m
2006	£2,256m	£1,128m	£4,627m[82]
2007	£19,684m[83]	£3,847m	£405m
2008	£3,019m	£2,449m	£152.2m
2009	£15,013m[84]	£721m	£41.4m
2010	£1,409m	£905m	£31.0m
2011	£2,505m	£1,248m	£672.2m
2012	£1,249m	£1,925m	£197.4m

Source: ZEPHYR

The median deal sizes suggest the bulk of transactions are at the SME level. Unfortunately due to the number of deals without any deal value available the data is not sufficient to enable us to observe a time-series trend for the SME market.

There is a strong presence of 'mega deals' in both inward sales and outward acquisitions. The average inward sale of over £170m shows a huge amount of capital has flowed into Scotland from large inward acquirers such as Scottish Power, British Energy Group, the Whyte and MacKay Group and House of Fraser.

The average of nearly £96m for outward acquisitions is also inflated through major acquisitions made by the Royal Bank of Scotland, Scottish and Southern Energy, FirstGroup plc, Scottish and Newcastle as well as The Weir Group.

The median figures for both are around the £11m mark, suggesting no major difference in the size of companies targeted from outside Scotland and by Scottish companies in other countries. Since this suggests similar patterns between flows both in and out of Scotland, it becomes important to understand the motivations behind the different types of deal and the impact on the Scottish companies involved.

Figure 7: Average and Median size of deals including Scottish firms (2003-2012)

	Total number of deals	Average deal size	Median deal value
Inward acquisitions	664	£171.6m	£10.8m
Outward acquisitions	453	£95.9m	£11.1m
Intra acquisitions	284	£33.9m	£3.7m

Source: ZEPHYR

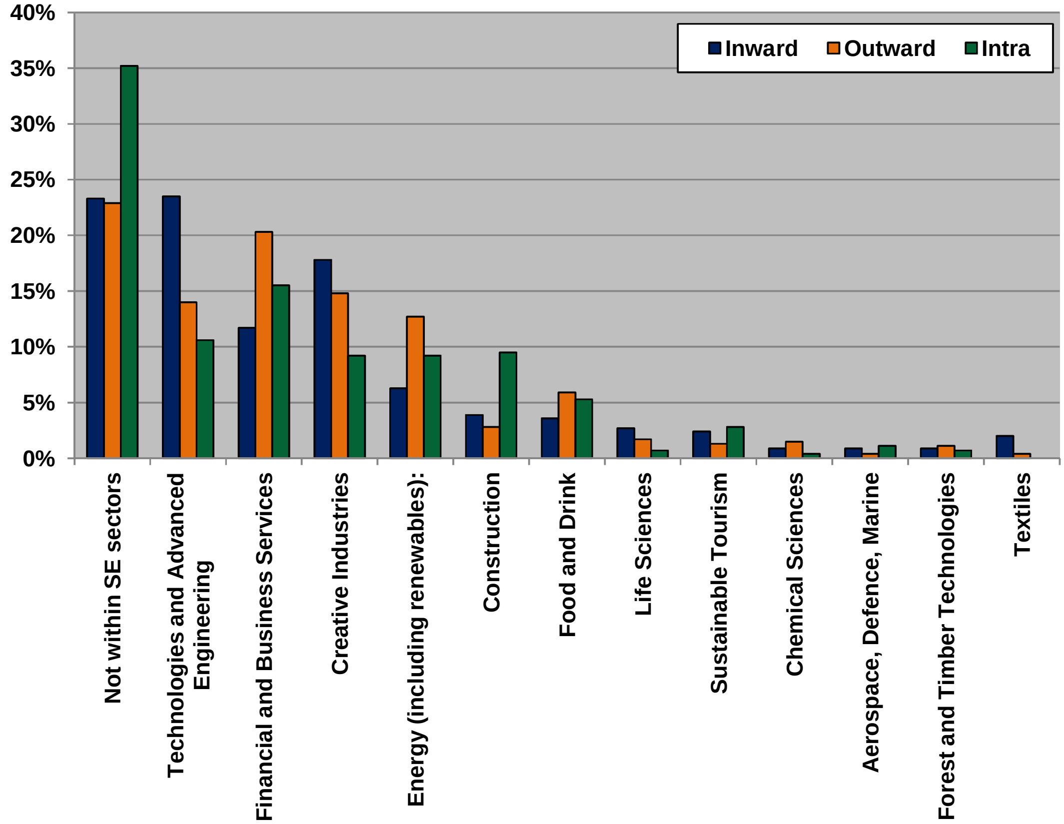
Sectoral Dimensions

Rather than use the 2007 version of the Standard Industrial Classification (SIC), which is how ZEPHYR classifies each acquisition, we have used a composition of SIC classifications constructed by Scottish Enterprise (SE) which groups together many SIC codes into the key

[82] £4.1bn of this total was Alliance Trust's acquisition of Second Alliance Trust
[83] £17.2bn was from Scottish Power PLC's delisting
[84] £13.8bn was from British Energy delisting

sectors in the Scottish economy[85]. The results for each type of acquisition are set out in Figure 8 below.

Figure 8: Acquisitions involving Scottish Companies. By Scottish Enterprise sectoral classification (2003-12)



Source: ZEPHYR

Most activity occurs in sectors outside SE's priority sectoral focus. Within priority sectors, the greatest number of deals are within technologies and advanced engineering, financial and business services, creative industries and energy (including renewables), and this is the case within each of the three deal types (inward, outward and intra).

Within the non-SE sectors no single sector dominated activity in any or each of the types, although within inward sales of Scottish companies, of the 155 acquisitions of this type, 30% were within wholesale trade (except of vehicles or motorcycles), with over 70% of these deals being sales to UK companies.

Account Managed Companies

At the same time of this research, a separate commission was looking at the impact of Scottish Enterprise on companies who are part of the Account Management programme. One aspect of this was a database that provided a comprehensive record of all companies – past and present, which have been and remain part of the process.

85 A description of this is available at Appendix 1

This provided an opportunity to cross-reference Scottish companies engaging in both sales and acquisitions with all those companies who have been and remain part of the Account Management process. The results for each type are set out below.

Figure 9: Scottish Acquisitions: Level of previous or current Account Managed Companies engaged in Activity (2003-12)

	Total	Percentage of total type of acquisition
Inward Acquisition	89	13.4%
Outward Acquisition	79	17.2%
Intra Acquirer	42	14.8%
Intra Acquired	25	8.8%

Source: ZEPHYR

This shows companies who are and have been account managed by Scottish Enterprise are more likely to make acquisitions than be acquired. They are also more likely to be acquired from outside Scotland than within, perhaps reflecting the greater levels of internationalisation that stems from being part of the Account Management programme. This again highlights that the experiences of the case studies within this work may not be wholly representative of the wider Scottish business base.

Summary

- Scottish acquisition flows are strongly linked to export activity, with the Rest of the UK, the United States and Western Europe dominating.
- The recession led to an initial spike in acquisitions made by Scottish companies, and a fall in inward acquisitions from outside Scotland.
- Most activity occur within the first ten years of the company's lifespan.
- Around one in two Scottish companies that are acquired remain active post-acquisition.
- 1 in 5 inward acquired and 1 in 4 intra acquired companies are dissolved post-transaction.
- The median deal size involving Scottish companies is around £11m, and is similar for both inward and outward acquisitions made across borders.
- Activity is concentrated in 6 priority SE sectors: Technologies and Advanced Engineering, Financial and Business Services, Creative Industries, Energy (including renewable), Construction and Food and Drink.
- Around 1 in 4 cross border deals and 1 in 3 intra-Scotland deals were outside SE priority sectors.
- Companies who are and have been account managed are more likely to make acquisitions than be acquired.
- Companies who are and have been account managed are more likely to be acquired by a company from outside Scotland.

Conclusions

This section has provided a detailed overview and initial brief consideration of the landscape of the Scottish sales and acquisitions market over the past decade. To give some further insight into the implications of this, similar data has also been analysed for a basket of similar European nations (as well as the largest markets in Western Europe). This will put Scotland's performance into context.

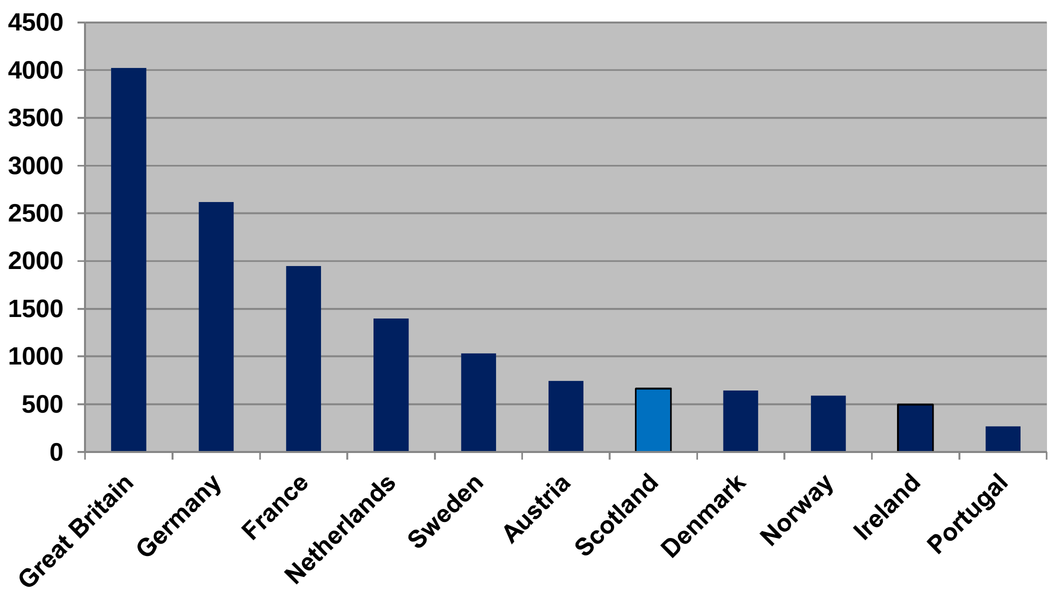
SCOTLAND'S ACQUISITIONS MARKET IN AN INTERNATIONAL CONTEXT

This section seeks to contextualise many of the features of the Scottish sales and acquisitions market between 2003 and 2012 by comparing it with a basket of European nations – both of similar scale to Scotland, but also major European markets.

Frequency of acquisitions

Figure 10 shows that Scottish companies are broadly acquired in similar numbers to firms from nations with similarly sized economies such as Austria, Denmark and Norway, albeit slightly behind Sweden. The figures also show the prominent role of the United Kingdom with 4023 acquisitions made of British firms between 2003 and 2012. This exceeds substantially the second largest inward market in Germany and more than double the numbers seen in nations such as France, and in some cases more than four times the total number seen in some nations.

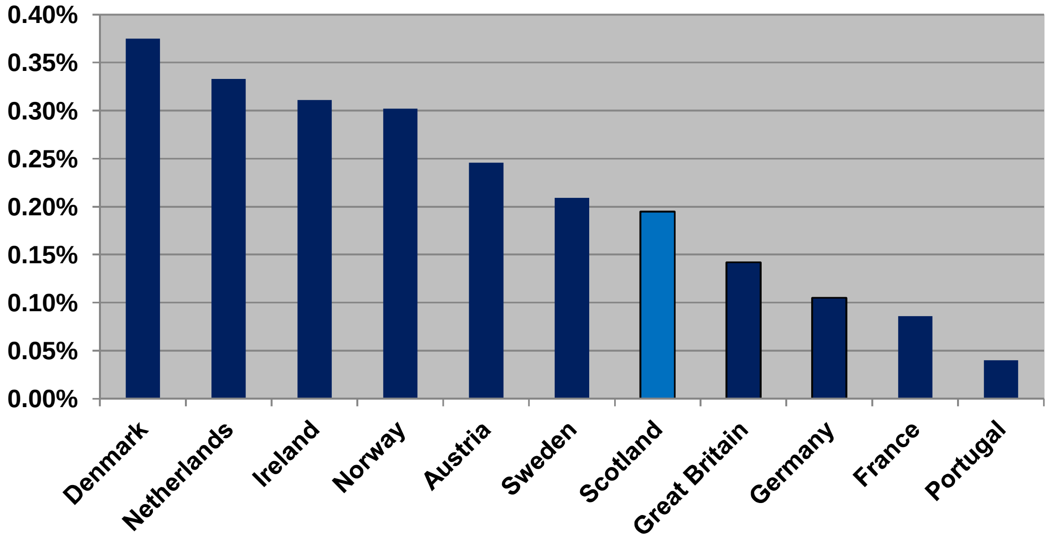
Figure 10: Total Inward Acquisitions By Nation (2003-12)



Source: ZEPHYR. NB: Great Britain excludes Scotland's figures

However, the total numbers of trade sales presents a rather simplistic picture which needs to be contextualised. To this end, Figure 11 shows the frequency with which companies are acquired from each nation using the overall business base in each nation.

Figure 11: Inward Acquisitions as a percentage of overall business base (2003-12)



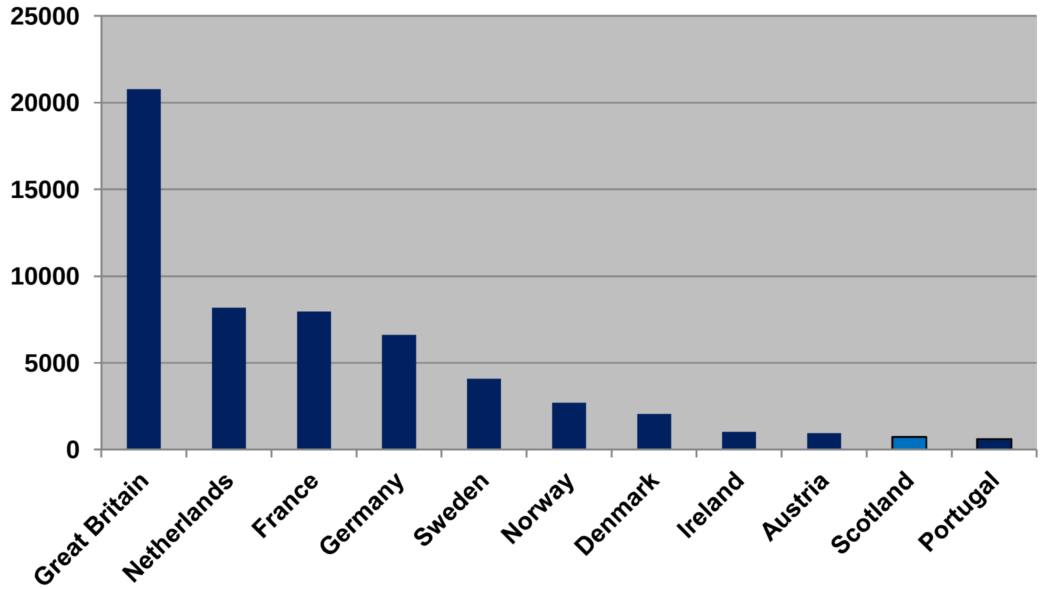
Source: ZEPHYR and Eurostat

This shows Scottish companies are sold at a lower rate than in most other nations. So whilst Denmark sees slightly fewer total inward acquisitions of its own companies than Scotland it has the highest percentage of inward acquisitions as a percentage of its business base. It demonstrates that acquisitions remain a relatively rare occurrence amongst businesses in Scotland.

Great Britain, Germany and France, who have the largest overall totals of inward acquisitions, have the lowest rate of inward acquisition/sale as a percentage of its business base (with the exception of Portugal). This perhaps reflects strength in their economies, meaning there are fewer reasons to seek out deals or accept any offer. This could include being within a larger, stronger and more resilient (during the recession) economy. It may be reflective of economic nationalism as the literature noted nations such as France have a more hostile approach to acquisitions by foreign firms. It may also be a result of policies which encourage organic company growth embedded within a nation, as seen in the Mittelstand within Germany.

Figure 12 shows the total number of acquisitions made by nations firms, combining outward and intra-acquisitions. Again, Great Britain (excluding Scotland) is easily the location of the greatest levels of activity and by an even greater margin than in inward sales. The total activity by British firms is more than double the figures seen in the Netherlands and France.

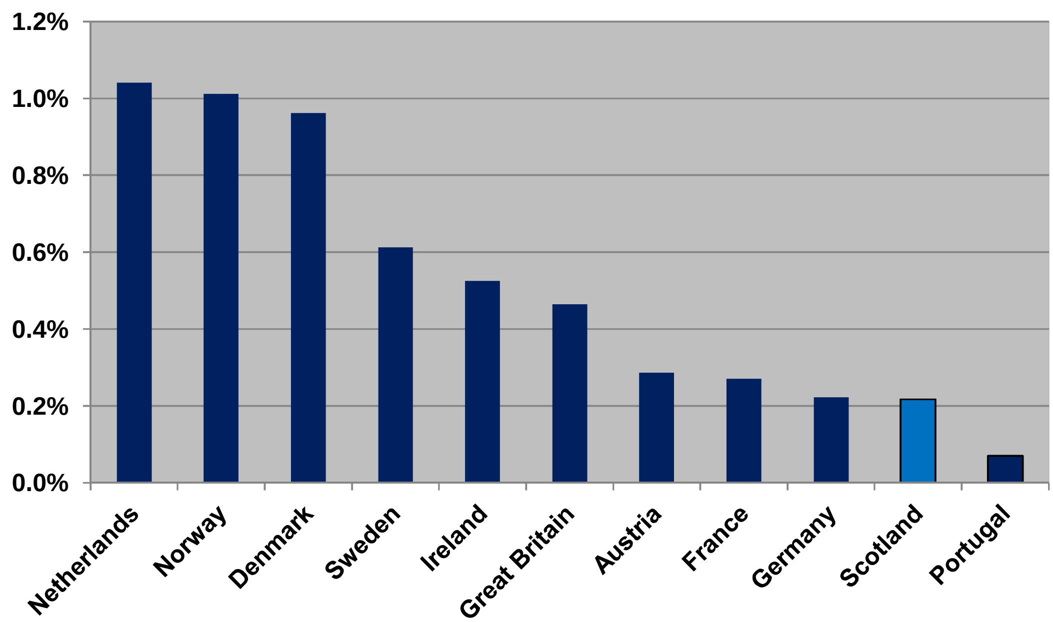
Figure 12: Total Acquisitions (Outward and Intra) By Nation (2003-12)



Source: ZEPHYR. NB: Great Britain excludes Scotland's figures

Scotland has the lowest number of acquisitions made by its companies (Portugal aside) and comes significantly below similarly sized economies in Norway and Denmark. Again therefore, Scottish companies are less active in making acquisitions than nearly all other nations. This is strengthened when looking at the rate of acquisitions as a percentage of the business base (Figure 13). It demonstrates that companies across Europe are more active in pursuing acquisitions than Scottish firms.

Figure 13: Total Acquisitions made by a nations firms as a percentage of overall business base (2003-12)

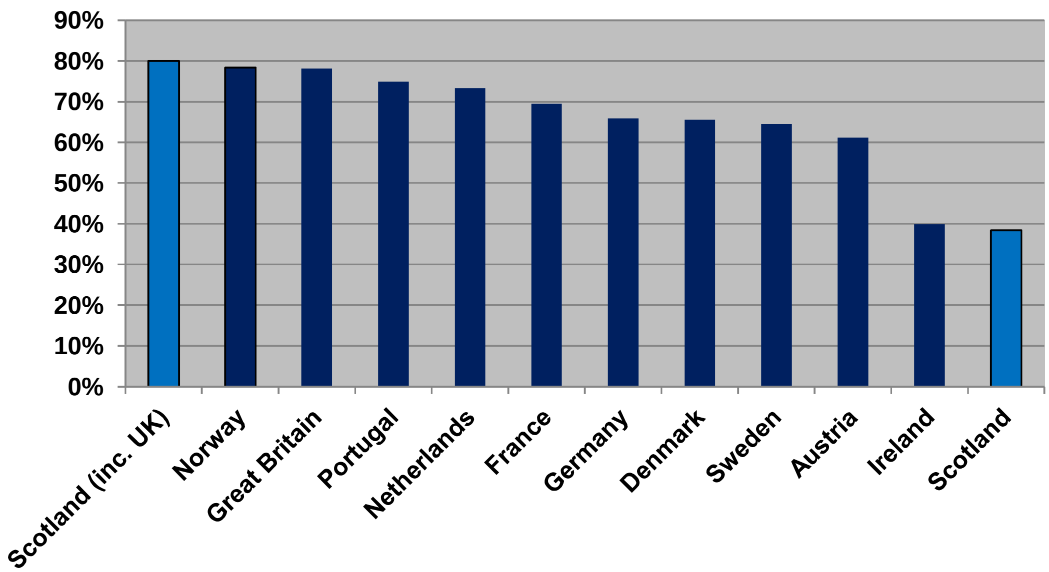


Source: ZEPHYR and Eurostat

Location of acquisition activity

Figure 14 looks at the level to which companies from a nation focus their acquisition activity within their own borders. In so doing, it can serve as one potential indicator of how international a nation's firms are. Figure 14 suggests that Scottish firms are the most international in their acquisitions, with only 38% of total acquisitions being made within Scotland. But when we take the UK as a whole, then Scottish companies display the least international outlook in their acquisitions, with four of every five acquisitions made within the UK market.

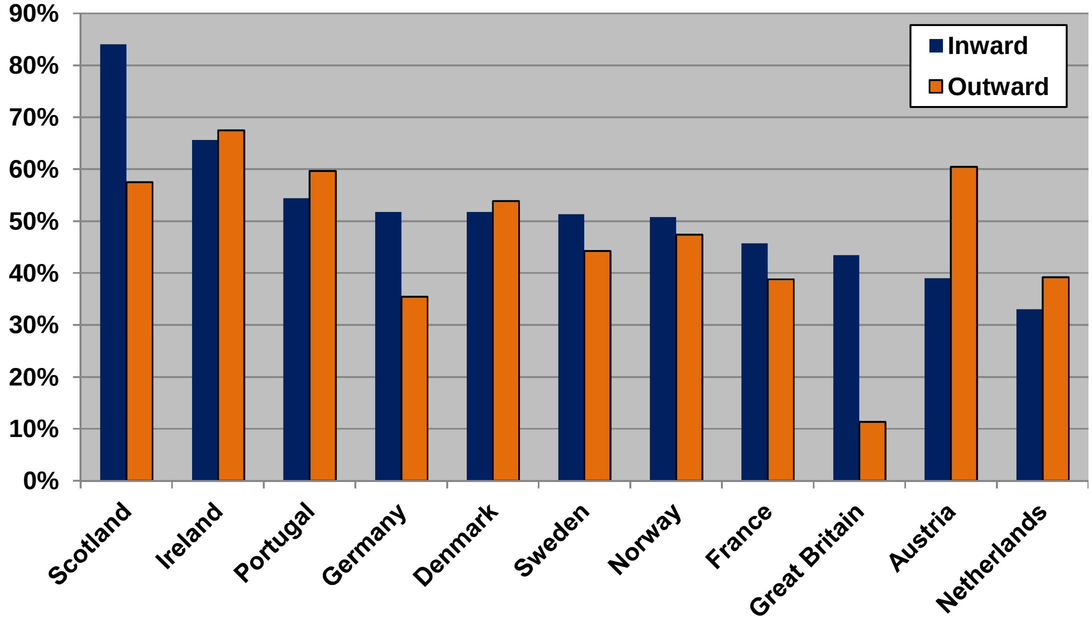
Figure 14: Percentage of acquisitions made by a nations firms within their own nation (2003-12)



Source: ZEPHYR

If Scottish companies are using acquisition to grow as this research considers and emerging evidence is starting to consider (Nesta 2014) then Scotland's lower overall rate of acquisitions and in particular, international acquisitions may be seen as holding back the potential growth of its firms. Taking this analysis further, Figure 15 looks at the percentage of inward sales and outward acquisitions with each nation's own five largest international markets.

Figure 15: Percentage of acquisitions made with a nation's five largest markets (excluding its own) (2003-12)



NB: Scotland's figures treat Rest of the UK as separate. Source: ZEPHYR

84% of Scotland's inward trade sales and 57% of its outward acquisitions are with its five largest markets, meaning that Scotland has a greater reliance on fewer nations than others. What is also notable is that Scotland, Ireland and Portugal, who are all geographically peripheral in Europe, display greater levels of concentration in its five largest non-domestic markets. This perhaps suggests that firms from nations further from multiple markets perhaps face additional obstacles than other nations closer to multiple markets.

Figures 16 and 17 demonstrate how geography and cultural familiarity has a direct bearing on the acquisitions market of each nation. For many nations, the leading inward acquirer(s) is often the nation(s) closest to it, which often is culturally very similar. For example:

- France has strong presence from British, German, Belgium and Spanish firms; all of whom share a border with France
- Germany sees inward acquisitions from Switzerland, Netherlands and Austria;
- Austrian firms have been predominantly acquired by German, Swiss, Czech, Croat and Hungarian firms, all close geographical neighbours;
- Each Scandinavian country has a strong presence of other Scandinavian nations;

The notable exception is the consistent presence of the United States and Great Britain at the forefront of activity with nations such as Ireland, France, and the Scandinavian nations, arguably due to their leading role in the global acquisitions market.

Figure 16: Top Five Acquiring Nations of Each Country's Firms (2003-12)

	1st	2nd	3rd	4th	5th
Austria	Germany 22.2%	Czech Republic 4.5%	Switzerland 4.1%	Croatia 4.1%	Hungary 4.1%
Denmark	Sweden 17.7%	USA 11.9%	Norway 7.8%	Great Britain 7.6%	Germany 6.8%
France	USA 17.7%	Great Britain 11.7%	Germany 7.2%	Belgium 5.3%	Netherlands 4.5%
Germany	USA 19.8%	Switzerland 18.3%	Great Britain 10.1%	Netherlands 7.8%	Austria 5.9%
Great Britain	USA 28.1%	France 4.6%	Ireland 4.1%	Germany 3.5%	Australia 2.9%
Ireland	Great Britain 36.7%	USA 20.7%	Germany 2.6%	Netherlands 2.5%	Denmark 1.6%
Netherlands	USA 10.7%	Great Britain 7.6%	Belgium 5.8%	Germany 5.3%	France 3.6%
Norway	Sweden 19.2%	USA 10.6%	Denmark 8.2%	Great Britain 7.3%	Finland 5.5%
Portugal	Spain 29.8%	Great Britain 8.2%	France 6.8%	Netherlands 5.4%	USA 4.3%
Scotland	Rest of the UK 55.5%	USA 10.8%	Norway 4.1%	France 3%	Netherlands 1.7%
Sweden	Norway 12.2%	USA 10.6%	Finland 10.6%	Denmark 8.5%	Germany 4.1%

NB: Omits all intra-deals. Source: ZEPHYR

Figure 17: Top 5 International locations of outward acquisitions by each nation (2003-12)

	1st	2nd	3rd	4th	5th
Austria	Germany 30.7%	USA 10.7%	Switzerland 6.9%	Netherlands 5.5%	Great Britain 5.2%
Denmark	Sweden 13.4%	Norway 7.6%	Germany 6.8%	Great Britain 5.8%	USA 5.5%
France	USA 10.7%	Great Britain 10%	Germany 6.4%	Spain 6.3%	Belgium 5.5%
Germany	USA 9.1%	Great Britain 7.9%	France 6.8%	Switzerland 6.5%	Netherlands 5.2%
Great Britain	USA 21.8%	Germany 6%	France 5.7%	Ireland 4.3%	Australia 4.1%
Ireland	Great Britain 36.7%	USA 20.2%	Netherlands 4%	Belgium 3.8%	Germany 2.3%
Netherlands	Belgium 10.3%	Germany 9.6%	Great Britain 7.5%	USA 7.3%	France 4.5%
Norway	Sweden 22%	Great Britain 9%	Denmark 8%	USA 4.9%	Finland 3.4%
Portugal	Spain 35%	Brazil 12.4%	France 4.8%	USA 4.3%	Great Britain 3.2%
Scotland	Rest of the UK 67.2%	USA 9%	Australia 2.6%	Ireland 2.4%	Netherlands 2.1%
Sweden	Finland 10.2%	Norway 9.6%	Denmark 8.6%	Great Britain 8.2%	USA 7.7%

NB: Excludes all intra-deals. Source: ZEPHYR

This shows that firms prefer acquisitions with firms from geographically closer nations with similar cultural aspects (language etc). Obviously each company will factor in these aspects to varying degrees, but it is a pattern evident across many nations.

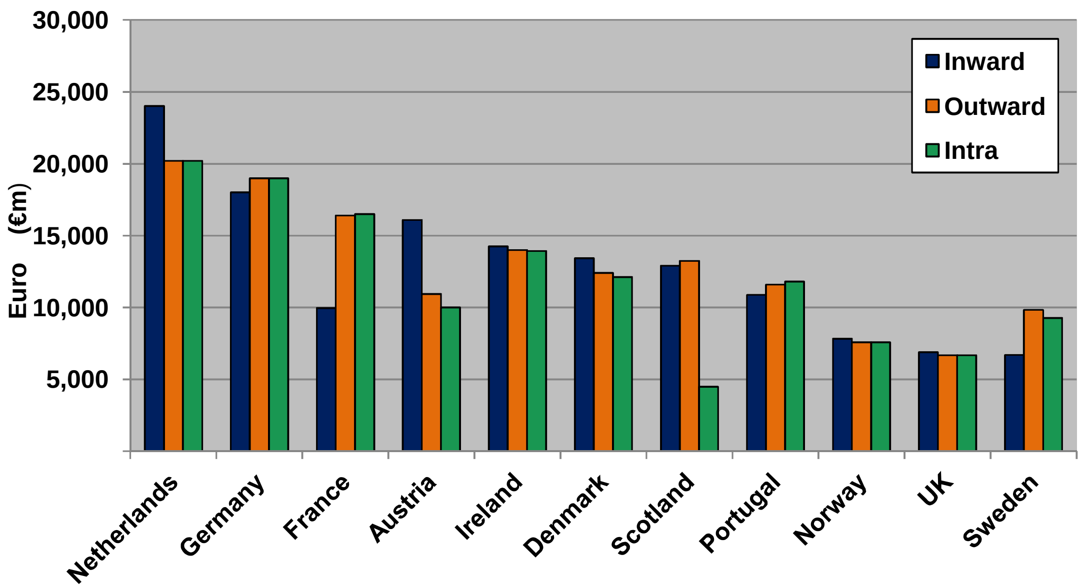
In a European context, geographically peripheral nations such as Scotland, Portugal and Ireland not only see less activity involving their firms, but the lack of neighbouring nations leading to a greater concentration of cross-border activity. It suggests an additional set of barriers to international sales and acquisitions (and perhaps even internationalisation generally) exist for firms in these nations and may limit this potential avenue for growth.

Company Maturity - Deal Size

The ZEPHYR database can give an indication of the size of the companies involved in the acquisition through the size of the deal (where available) and the company age (calculated through comparing the date of incorporation with the completion of acquisition date).

Taking the deal size first, Figure 18 sets out the median deal size across each type of deal for each nation. It shows that in comparison to other nations, Scotland performs within the mid-range for inward acquisitions of its firms, at around €12.9m (£10.8m). This is considerably lower than the Netherlands but larger than nations such as Norway and Sweden. Scotland also has a larger inward acquisition deal size than the United Kingdom.

Figure 18: Median Deal Size by nation and Acquisition Type (2003-12) (€m)



Source: ZEPHYR

In terms of outward acquisitions the median premium of €13.25m (£11.1m) paid by Scottish companies is larger than many comparable nations (Austria, Denmark, Norway, Sweden and the UK). This suggests Scottish companies making cross-border acquisitions are moderately larger but certainly not significantly smaller than those doing likewise in several other nations.

It is in intra-acquisitions/trade sales where Scotland is noticeably different from all other nations. The median deal size of €4.5m (£3.77m) is the smallest observed and suggests that a significant proportion are acquisitions of lower value Scottish companies, who perhaps may be younger as Figure 4 highlighted. 52% of Scottish companies acquired by other

Scottish firms are under ten years old, the same proportion as inward acquisitions, but with a significantly lower deal median.

Is this market simply the acquisitions of young, small firms in domestic industries, increasing market share for the acquirer by eliminating an up and coming competitor? Or is it predominantly of younger firms, with the acquirer securing a new technology, product or market to merge with its own services and expertise? If so, are these domestic companies then moving on further, perhaps they growing as a result of the intra-acquisition, ultimately leading to cross-border sales or acquisitions? Indeed, is this a pattern applicable elsewhere or confined to Scotland? The low intra-acquisition median compared to other nations suggests that there may be a trend within Scotland not replicated elsewhere. A comparison of the age structure of firms engaged in acquisition may assist our understanding of this.

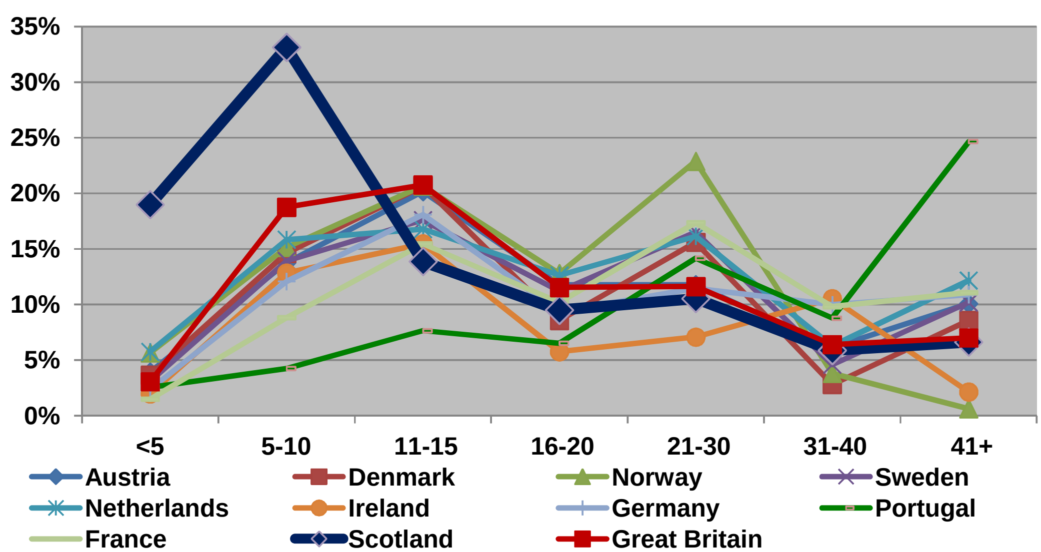
Company Maturity – Age

Figure 4 highlighted the prevalence of younger companies (aged under 10 years) in Scotland's acquisition activity:

- 52% of inward acquisitions
- 39% of outward acquisitions
- 52% of intra-acquired companies
- 37% of intra-acquirers

Figures 19-22 show acquisition activity takes place earlier in the lifetime of Scottish companies than in all other nations. This is also the case for British companies but not to the same extent. The age profile of inward acquisitions particularly highlights the early acquisition of Scottish companies (Figure 19).

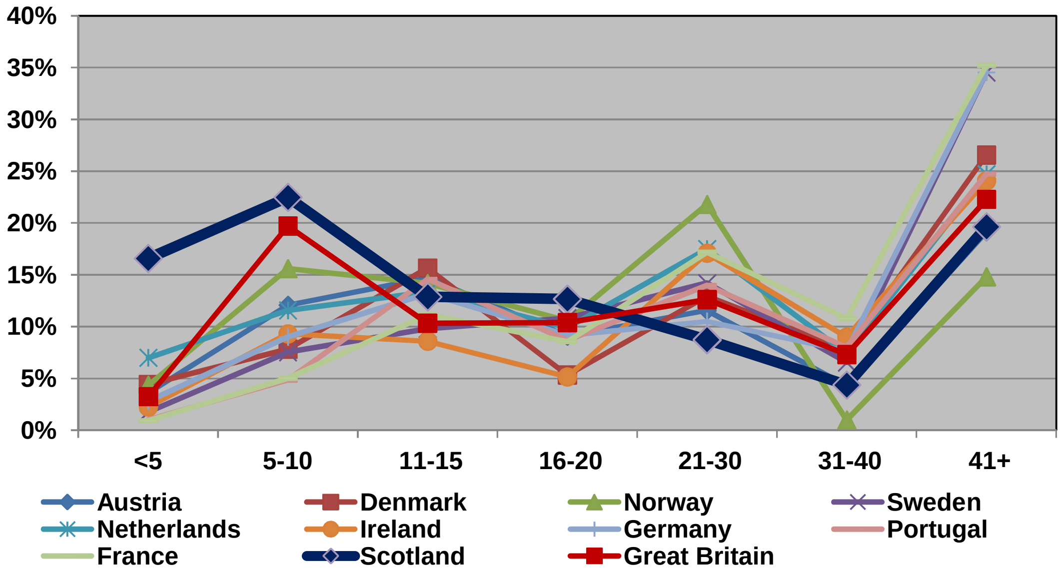
Figure 19: Inward Acquisitions Age Profile. By Nation (2003-12)



Source: ZEPHYR. NB: Excludes deals with no age given

The same pattern for activity at a younger age is also observable for outward acquisitions, but the age profile for activity by Scottish companies more closely reflects the trends seen in other nations (Figure 20).

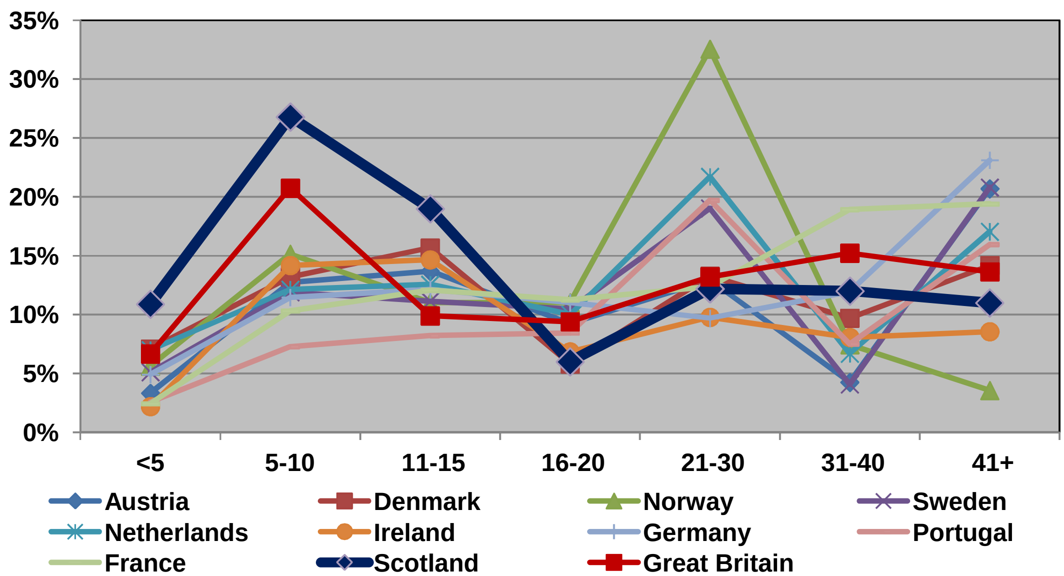
Figure 20: Outward Acquisitions Age Profile. By Nation (2003-12)



Source: ZEPHYR. NB: Excludes deals with no age given

Scottish companies making acquisitions within Scotland are also considerably younger than other nations (Figure 21), which could be taken as evidence for some firms using acquisition as part of a clear strategy to grow through acquisition.

Figure 21: Intra Acquirers Age Profile. By Nation (2003-12)

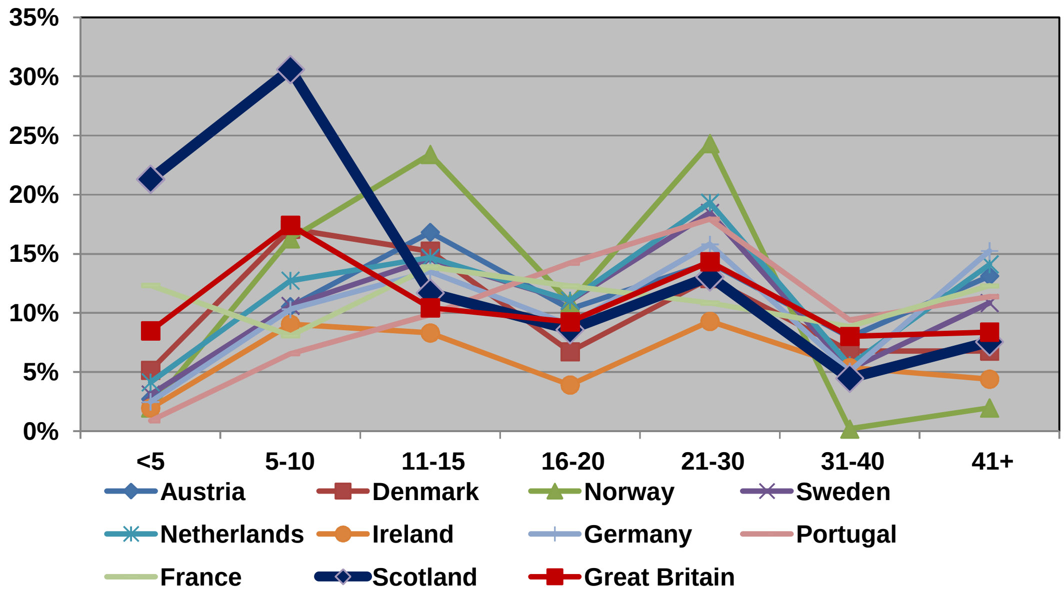


Source: ZEPHYR. NB: Excludes deals with no age given

Once again early activity within Scotland is observable when looking at the profile of firms being acquired, with an early peak (Figure 22) before settling back into a pattern comparable to other European nations.

The inward acquisition median for Scottish companies making trade sales suggests that whilst Scottish companies acquired from overseas are young, they are not necessarily small (when compared to other nations) and appear to be companies that have been growing in their early years. Similarly, the deal size for outward acquisitions compares favourably in comparison to others, but is paid by Scottish companies that are younger than elsewhere. The acquisition of young firms is also seen in the intra-acquisitions market, but the significantly lower median suggests these are of firms who are smaller, and who may not have experienced strong growth in their early years, albeit with some aspects of value which attracted an acquirer.

Figure 22: Intra Acquired Companies Age Profile. By Nation (2003-12)



Source: ZEPHYR. NB: Excludes deals with no age given

Therefore, the intra-acquisitions market may be characterised by acquisitions of Scottish firms who have not yet reached the rate of growth of others (indeed, trade sales may be a means by which they feel they can achieve this) or have no potential, no willingness or no ability to grow, and therefore activity is principally driven by domestic companies seeking to scale up their operations through eliminating competition and increasing their market share. Interviews with a range of companies who have been part of the intra-acquisition market should shed some light on the dynamics at play.

Trading status post-deal

The post-deal status of a company can give some indication of the motivations behind and the consequences of each deal. Dissolution and inactivity suggests the principal objective (or at least a strong consideration) was to acquire a company to ultimately eliminate it; either after extracting the valuable aspects or simply eliminating it as a competitor[86]. In contrast, a company remaining active when it has been acquired, suggests a different set of motivations were behind the deal.

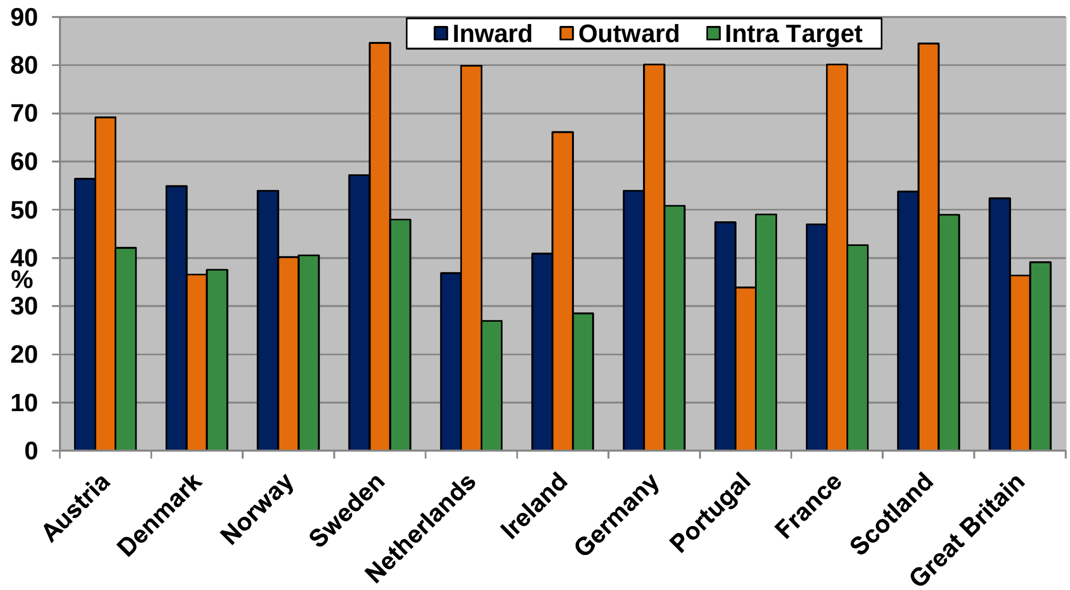
It suggests that the company has been targeted because it is profitable (or has the potential to be profitable) and has significant value (or potential to be valuable) to the acquirer in its

[86] It should be noted that the company being dissolved or liquidated post-acquisition does not automatically mean its activity ceased. It can signify the acquired firm being brought within its acquirer's umbrella in a different legal form, but one that has no material impact on the activities of the company within its nation. Unfortunately ZEPHYR does not provide the means to distinguish these firms from those who see activity cease.

current location, with its current market and customer base. It suggests the strategy behind the acquisition recognised the potential of achieving synergies from bringing together the two firms, which literature shows provides the greatest chance of success.

The data shows Scotland has one of the strongest post-acquisition active rates in Europe, across all types of deal (Figure 23). In inward acquisitions, Scotland's rate of (53.77%) is above the rates seen in other nations such as France, Netherlands and Ireland. Scotland also comes ahead of the UK and is only just over 3% behind Sweden who have the best rate of 57.21%.

Figure 23: Percentage of companies remaining active post acquisition (2003-12)



Source: ZEPHYR. NB: Figures reflect trading status at 31 December 2012

Scotland's outward acquiring companies enjoy an 84.5% post-acquisition active rate, to which only Sweden is comparable; both are ahead of all others nations. A range of other nations have around the 70-80% level before a considerable gap opens up to nations like Denmark, Norway, Portugal and Great Britain who see their post-acquisition active rate around the one in two rate.

Continuing its strong post-acquisition active rates, Scotland again features at the top end of ongoing rates for firms acquired domestically (48.9%). The active rates across all nations are generally lower, but Scotland still has one of the highest rates (only behind Germany – 50.8%) ahead of the level seen in all other comparable nations, and ahead of the Great British rate.

A post-acquisition active rate for Scottish companies of 'only' one in two for inward and intra acquisitions is considerably lower than the rate for companies making acquisitions, but this is still a strong performance internationally. It suggests acquirers see more value in Scottish companies, their domestic market as well as their supply chain, networks, clusters etc. This could lead to greater benefits not only for Scottish firms, but the Scottish economy.

Summary

- Scottish companies are acquired both internationally and domestically at a lower rate than several similarly sized economies.

- Scottish companies are also less acquisitive than comparable nations, both internationally and domestically.
- 4 in 5 acquisitions made by Scottish companies are of firms within the UK, a higher rate of reliance on its own market than any other nation.
- Across Europe, geographical proximity and cultural similarities shape each nation's acquisition and sales activity.
- Activity in sales and acquisitions takes place earlier in the life span of companies in Scotland than elsewhere.
- But Scotland's median deal size for cross-border sales and acquisitions is broadly similar to comparable nations.
- In contrast, Scotland's intra-deal market has the lowest median deal size across Europe.
- Across each type of transaction, in the post-deal period, Scottish companies have amongst the highest post-deal active rates.

Conclusions

This section has compared how Scotland's sales and acquisitions market to several European nations. It highlights that Scottish companies – whether going through a sale or making an acquisition, are less active than firms in other economies, and of those that are active, there is a strong reliance on the United Kingdom market; a greater reliance on a single market than anywhere else in Europe.

It also begins to indicate that some of the common perceptions regarding takeovers of Scottish companies are not as straightforward as assumed. For example, whilst it is accurate to note that Scottish companies go through a trade sale earlier than elsewhere, not only is this also the case for Scottish companies making acquisitions, but the signs are that this activity is not as damaging to Scottish companies and the wider economy as some believe to be the case. The median deal size is comparable to many nations and the post-deal active rate in Scotland stands amongst the highest across Europe, which suggests that there are other factors driving activity within Scotland.

To begin to explore some of the issues and to add a more informed consideration to discussions on this matter within Scotland, a select number of interviews were conducted with Account Managed companies who have been through a sale or acquisition.

SCOTTISH COMPANIES' EXPERIENCE OF ACQUISITIONS

Introduction

To complement the analysis from the ZEPHYR database, a series of interviews were conducted with companies Account Managed by Scottish Enterprise. Each of the companies interviewed had been through either an acquisition at least once.

These companies span a wide range of sectors (Figure 24); comprising different ages, spanning multiple locations across Scotland and all with different experiences which led to their first acquisition and subsequently, post-acquisition. They also were at different stages of their pre and/or post-acquisition process.

Figure 24: Profile of companies interviewed

Company Sector	Inward Acquisition	Outward Acquisition	Intra-Acquisition
Food & Drink	X		X
Technologies and Advanced Engineering	X		XX
Technologies and Advanced Engineering		X	X
Financial Services		XX	
Life Sciences	X		
Food & Drink			X
Energy	X		
Energy	X		X
Non-Sector	X		
Food & Drink		X	
Energy		X	
Non-Sector	X	X	

In total, 12 consultations were carried out and covered 19 deals in total (7 inward, 6 outward and 6 intra-acquisitions) giving a broad representation of not just each type of deal but also the interaction and interconnectivity between the types of deals. This enabled each interview to explore each companies own history and background, when the acquisition occurred and how the company and its management approached and completed the deal before moving on to subsequent deals (in some cases).

The companies were randomly selected from a list of companies who have been through a sale or an acquisition and who have been, or remain Account Managed by Scottish Enterprise. These case studies were not meant to be exhaustive and cover all eventualities, but it does begin to highlight the experiences of Scottish companies.

This chapter sets out the findings, in particular focused on the emergence of a series of common observations emerging from the interviews.

How deals emerge

Before looking at the reasons why companies decided to become involved in acquisitions and sales, it is worth outlining how they came about and what circumstances companies faced which ultimately led to a deal being concluded.

Figure 25: How acquisitions had arose

A range of circumstances had led to an acquisition being considered. These included:

- Companies had considered the ways by which they could achieve the desire growth and true potential of the company and concluded a sale or acquisition was the most beneficial approach to take
- Globally, the markets were becoming more competitive and profit margins were being squeezed due to price competition and the only way to grow was to secure investment, which the company did not have and could not access in a way other than acquisition
- The company had been turned around after a period where it had struggled and been acquired due to its potential for growth and relatively low market price
- Ownership was beginning to approach retirement age and thinking about an exit, and an offer came in around this time which was deemed acceptable. In a similar example, the company founder was seeking an exit due to retirement and a fellow shareholder was also keen for an exit. However, this company took a longer-term approach to consider its long-term objectives and decide its path accordingly.
- One company was acquired by another to provide excess capacity for delivering on their order book. However, as time developed, the acquired company took on a leading role in the parent company.
- Some companies had existing investment for which a return was required. Therefore, considering how to facilitate the exit was always a consideration. However, pursuing the most appropriate exit was not always a long-term process, and as a result of a lack of time allocated to dedicating this time to transitioning, the most beneficial offer presented at the time was the one accepted..
- For some Scottish companies the recession provided the opportunity to make acquisitions, securing value from obtaining skilled workers, equipment, plants, order books and customers; again highlighting the opportunistic elements that drive much acquisition activity.

Interviews made it clear that companies are consistently presented with opportunities for sales and acquisition. As one Managing Director noted *"they're always coming across my desk, some I take a few minutes to think about; others I just ignore because it's not the right time or there's something wrong that we don't want a part of. They're always there and you never know when something might just appear at that right time. Whatever that is."*

Even when companies admitted to having prior thoughts regarding acquisitions, they acknowledged their activity was ultimately shaped by the opportunities that presented themselves. Companies admitted they were *"…always looking. We never stop. You just don't know what opportunities you'll miss… we're always talking with customers, clients. That's how these come about."*

Of the 19 completed deals, 6 could be seen as unplanned in that the situation which led to the completion of the deal arose through circumstance and events. Of these six, two were outward acquisitions by Scottish companies, whilst four were inward sales of Scottish companies to non-Scottish acquirers.

In addition to an approach taking advantage of an opportunity, unplanned deals also occurred when *"things just happened"* and decisions were made based purely on information and insights available at the time. They may have ultimately proved beneficial for the company now, but this appeared to be more a consequence of happenstance than any particular strategy. Therefore it is not unreasonable to assume there may be further Scottish companies in particular who have gone through a sale for which a lack of long-term planning has proved detrimental. They may not have survived post-deal, or have made a decision quickly which did not prove beneficial to the company in the long-term.

Some companies have displayed an ability to seek an acquisition in order to drive growth, whilst rooting this approach in the reality of current economic conditions, thus enabling them to take advantage of opportunities that presented themselves. It was evident in the six 'unplanned' cases that these arose through the networks of Scottish companies, rather than the company having taken a deliberate approach to seek out an acquisition. In particular, it was the skill and vision of the management which enabled companies to adapt successfully.

For example, it was whilst considering its options and how it wanted to achieve growth, including the level of investment needed to expand its products and services and the risk that would be attached to this, that one company received an offer to acquire the company via its networks. This would allow access to the investment required and open up the company to tap into the resources and support of a UK-wide business. After full consideration, the company felt the deal on offer would allow it to achieve its goals and be less of a gamble than other options. They therefore accepted the offer and have seen turnover and skilled jobs both within the company and the supply chain grow subsequently.

Another Scottish company grew through making acquisitions during the recession, securing plants, machinery, order books and skilled staff within England. Again, the acquisition opportunity came through the company's informal networks (in one case a third party suggesting that the eventual target company would be open to a takeover) and was not being actively sought at the time. Indeed the company did not have an acquisition strategy, but when opportunities arose through engagement with networks, it took advantage. The impact of this was that a plant in England which turned over £1.6m per year increased to £2.8m and then £3.3m in subsequent years, whilst the turnover of the Scottish company doubled to £13m between 2010 and 2013.

This highlights not only the approach of some Scottish companies but also the acumen of their management who have used market conditions to their advantage to secure attractive deals. Whilst the long-term ambition has been to increase turnover and profitability, management have been flexible in how they achieve this. Rather than being rigidly committed to an acquisition strategy, organic growth or seeking to build up a company in order to realise a sale and a return on investment, they were opportunistic and flexible enough to constantly remain open to all viable opportunities as the economy as well as their industries and sectors evolve.

A change in circumstance ultimately led to a sale of a Scottish company to an inward acquirer in two cases. In both cases the company's management was beginning to consider options to facilitate their exit due to approaching retirement. However, there was a view that they were keeping their thoughts and intentions close to their chest, creating uncertainty for the remaining members of the management team. A range of options were apparently considered which would facilitate their exit, with a return on their investment, but then also secured the status of the company going forward was not always evidently preeminent for the management/owner.

For those looking to remain with the company post-exit, in both cases, competition from the Far East was beginning to put a significant downward pressure on prices. For one company, the competition had become more acute within the past 6 months due to the opening of a mass distribution centre in the UK. This took away the despatch time advantage previously enjoyed, meaning that an alternative response was required.

At the same time, a previously diverse sector was going through a consolidation as a few major global players sought to upscale through a series of branches across the globe. This further squeezed the company since competitors were becoming part of a global chain of plants and through that, securing investment to drive up their productivity, thereby heightening the competition.

The remaining Directors began to view the impending exit as an opportunity to consider the long-term vision for the company, and in particular how they could compete against these twin challenges. Investment in order to drive up productivity was considered to be the best available option. But within current means and without the level of backing needed on offer from the bank, it was not possible within current frameworks.

A second option was to cut prices. It was rejected almost immediately by the Managing Director who spoke of his steadfast refusal to contemplate cutting the prices of their goods, stating that it would be *"the start of a slippery slope we'd never be able to get off. … It'd be a race to the bottom. We wouldn't win and then what we would be left with?"*

In this case, the best option available was a sale to an international company who would give the best opportunity to achieve their goals. They had seen the benefits that it had brought competitors. Consequently the company began to plan and enter into discussions with potential suitors to identify the best fit for the company. In this case, the company used a desire for an exit due to retirement to make a clear statement of ambition to compete in the face of changing circumstances, rather than letting the opportunity pass the company by.

So whilst there are companies whose management have a mindset to strike deals and grow via sale or acquisition, there are companies for whom acquisitions and sales arise through very different circumstances which can include a simple combination of chance, timing and economic climate. However they came to the sale or acquisition, there was a common thread running through each case.

Reasons for completing a deal

Interviews highlighted three principal reasons why the Account Managed companies had been involved in acquisitions and sales activity:

Figure 26: Reasons for completing an acquisition

- to achieve growth (highlighted by 11 companies);
- to facilitate a management exit (3 companies) ; and
- to provide a return for investors (4 companies)

1. *To achieve growth*

The primary objective has been to realise growth – either triggering a new phase or continuing a current growth phase. In all but one interview, the overriding objective behind the deal had been to grow the business. Companies spoke about their growth potential in their domestic market being *"maxed out"* and having reached or approaching a *"glass ceiling"* whereby further growth was simply not possible without significant investment. Whilst existing markets were strong and profitable, opportunities to grow within them were felt to be limited. Therefore companies across a range of sectors in Scotland recognised that securing this additional growth required a new approach; a *"game changer"* for the company to grow within Scotland and internationally.

- As a demonstration of ambition

Believing that limitations to their ambitions existed, led to a realisation for companies that they were *"at a crossroads"*. Management in five companies reflected back on this as the point when the company articulated its clear ambition to grow. Each acknowledged that it would have been *“easier to stay local”* and profitable in their current market (retaining a good salary and comfortable lifestyle) and not strive to achieve further growth. But each also recognised that eventually their markets would change and they would no longer be able to compete. As one Managing Director put it, *“you’d be in effect managing a declining business”*. Each felt an onus on them, given the time, money and effort invested in the company over the years, to strive for more, and to do so mean they had to consider either an acquisition or sale as an avenue to growth. There was an ambition behind their decisions.

These growth-focused companies gave a range of reasons as to why they felt the approach they decided upon was the best route to maximise their potential. The similarities between the reasons given by Scottish companies who went through a sale and those who acquired were striking.

Figure 27: Reasons for pursuing an acquisition

Reasons given for pursuing acquisitions were:

- It was the quickest way to achieve and/or accelerate growth;
- It was a lower risk option compared to investing in the existing company and activities (e.g. acquiring a company with knowledge, skills, customers is less risky than developing their own)
- The realisation of synergies between the companies that have shared goals
- Products and services would be enhanced through bringing together two companies to deliver more than what they could achieve separately, thereby adding more products and services to the company’s offer;
- It gave the Scottish company a stronger presence and/or a base in either an existing market or in a target market, at a pace that could not be realised any other way;
- It provided instant access to networks, contacts and relationships previously unavailable, which could be exploited for further growth plans;
- It provided the company with a healthier financial position, a stronger balance sheet and often removed debt and other financial restraints from the company;
- It provided instant access to a trained, skilled and quality staff resource, avoiding the need to recruit and attract such staff, and the difficulty associated with this;
- It provided a level of technical support and expertise not previously available to the Scottish company;
- They had seen competitors pursue alternative strategies (i.e. make the investment themselves) and have limited results as a consequence;
- It allowed the company to deepen its standing internationally;
- Being acquired secured investment, particularly capital investment which the Scottish company alone was not able to make.

Each of these reflected the prevailing view from companies that acquiring another company or being acquired would not only be the quickest option for realising growth, but also the safest option to take providing the right decisions were made. Companies repeatedly expressed a view that they would have found it harder to penetrate further into markets, make necessary investment and access required knowledge, expertise and contacts without acquiring or being acquired – and that the path they took was the fastest and most effective way for them to reach into those markets and networks.

To build this up organically would in their view, take too long, be too costly and have a lesser chance of success. For each company therefore, their decision to acquire or be acquired was presented as the most logical step to take.

- To break through barriers which hindered growth

One of the principal reasons which led to their belief that a ‘glass ceiling’ had been reached, was the need to secure and make further investment. In four interviews Scottish companies demonstrated a clear pattern of investment into the company, its supply chain and workforce over a period of years which had led to growth which they were looking to maintain.

Adding products and services through an acquisition was seen as the approach to take because whilst each company had an established and positive relationship with the bank, they were not able to secure the level of investment now needed. At the same time, the company was also not able to find the additional resources from within to make the investment, not to mention the difficulties in finding and attracting staff with the necessary skills. This led to a consideration of all options as to how these aspects could be found.

“…and we felt that if we could get a buyer who would make the investment, show the commitment to our workforce and our brand in Scotland, then it would help us, but also help them too. We had a lot to offer them in return.”

Again, being connected into the global marketplace through a range of networks meant that potential opportunities were never far away, but it was emphasised how important it was to find the right company to secure the most beneficial deal. As one Chief Executive put it *“It’s not the biggest cheque, it’s who would work with us to grow in the long-term.”*

For this company, within the first year post-acquisition, there was heavy investment in machinery and the plant, above what would have been possible without it; *“It also showed our staff that they were valued and part of what we wanted to achieve.”* A new long-term plan is now in place which is built on increasing turnover, but using up the additional capacity that emerged as a result of the investment made post-sale, to increase productivity all within Scotland.

Further examples showed acquisition secured instant access to additional benefits. In particular, having expert support and resource to draw on and secure skilled, trained and qualified staff were cited as two hugely beneficial aspects from concluding the deal. It was repeatedly noted by companies how challenging it was to find, recruit and retain skilled staff in a range of sectors such as engineering. In some cases, becoming part of a larger company who had that resource available, or acquiring a company with skilled staff enabled the Scottish company to use that resource to enhance their products, services and ultimately the size of work that was able to be carried out.

It also bypassed the time involved in training staff, in addition to the risk that comes with making the significant investment needed to train them, that they may leave shortly after becoming trained for a higher-paid post. Again, in this sense, acquisition provided the safest route for Scottish firms to pursue.

This drive to achieve scale was described in multiple interviews as recognition of the need, and subsequent benefits of being able to be a *“one-stop shop”*, whereby all aspects could be delivered by one company. Being able to grow depended on securing bigger contracts with clients who demanded the simplicity involved from having one company interfacing with them for all aspects, rather than having to have multiple contracts across multiple companies.

- Greater financial security and scope

Scottish companies saw being acquired as providing greater financial security, enabling them to compete for larger contracts with bigger companies, in order to yield even greater returns. Achieving and sustaining the level of growth they were experiencing had meant stretching their financial capabilities as far as possible, but in turn this hindered them continuing this approach into the next phase.

The situation that several companies faced can be neatly summed up by one Chief Executive of a Scottish company who was acquired by an American firm and remained in charge of the Scottish office of this global company:

"It also meant that I focused less on the next round of funding – I don't think people really understand how much that can take up your time. It's all about moving from funding round to funding round, you never seem to look beyond that. You can't. It takes over and you aren't running the company and making it grow. It does grow, obviously… but you're not devoting as much of your time to make the most of it because you're always focused on the money. Being part of the NAME WITHELD means I can focus on our customers, our role in the company, getting more and bigger business in, making links across the globe and think more strategically."

Three companies highlighted that being sold took away existing debt worries. In addition, two further companies found that a large percentage of their turnover relied on one or two major contracts. This presented a risk on their balance sheets and had deterred potential clients from placing work in Scotland. Being part of a global company would spread this risk hence why being acquired became an attractive route to growth.

Being acquired freed up Scottish companies to apply for and secure larger contracts with bigger companies, taking on additional work to break through the 'glass ceiling' they had felt. Whereas previously they were unable to get these contracts due to concerns over the size and viability of the company to deliver, the company was now able to be more ambitious, offer a greater range of products and services, and draw on a wider skill base and expertise. All of this was now possible without any concerns about the size of the deal, enabling the company to focus on delivering a high quality service. In turn, this helped to de-risk the company whilst growing its portfolio and increasing its global footprint. All of which, was *"simply not possible if we hadn't teamed up with NAME WITHELD. It ticked every box we had".*

- Growth through partnership

This element of 'teaming up' and working in partnership highlighted that deals were increasingly being seen as a partnership, despite being acquired. Seeking a *"partner"* as one acquired company put it, would give the company access to networks and markets that they had been unable to establish themselves, in addition to being able to call upon greater resources to continue growth. They felt that the advantages of being part of a global group with a greater suite of products and services far outweighed standing alone with a limited range, which was of little interest to global companies seeking a client to provide everything themselves. As one MD of an acquired company put it, *"we had hit the limit of what we could do standing alone, it was time to partner up."*

Despite being acquired, they began to explain that the deal was struck between two companies who had different objectives but similar aspirations. Whilst the Scottish company was seeking to expand its international footprint alongside and secure the additional investment required to improve productivity, the acquiring international company was keen to expand into the UK, particularly into Scotland, giving it proximity to identified growth opportunities. Whilst these were different perspectives which ultimately led to the deal being struck, both were primarily motivated by a desire to grow which the acquisition enabled.

2. To achieve a management exit

In two interviews, the explicit aim from the outset of the company was to achieve an exit and secure a return on investment. For a further two companies, as the company had developed, an exit had been sought for different reasons. In each of these cases whilst the acquisition may have primarily been about facilitating an exit, it was ultimately used to seek a path to growth; as a 'trigger' point to take the company forward in a new direction to secure growth. That was not to say that there was a long-term planned approach to the exit as noted previously. In two cases, it was clear that the desire to find an exit came about rather hastily and was secured relatively quickly. Whilst on reflection there was an admission that perhaps things could have been done differently, company management felt the best decision for the long-term future of the company had actually been made. In particular, they cited the new perspective and experience of sales, acquisitions and growing companies that was brought by new members of the management team were critical in taking the company forward, and *"to the next level"*.

One aspect that may have contributed to this was that the entrepreneur seeking the exit also wished to maintain their reputation in their chosen field to allow them to continue to work in this area (in some cases), and having the company being seen and recognised as successful was central in this. Therefore criteria had been inserted into the sale contract to retain brand name, key accounts for the acquired company and guarantees for staff that remain, also securing benefits for the Scottish economy. It shows that whilst a management exit may have been sought, it was not simply about getting out and leaving the business to the whims of its acquirer.

"We spent years on this company, it's our legacy so we weren't going to hand it to just anyone. They had to make sure it worked for us beyond the sale, otherwise we'd have looked elsewhere."

That the exiting management had a desire to remain active, as well as the need for their replacement to have relevant skills, expertise and experience begins to highlight the level of recycling of individuals and entrepreneurs that arise through trade sales. This is covered in more depth further on in this section, but it is evident that without acquisitions, this recycling would simply not happen and stimulate further activity and impact in the economy.

3. To provide a return for investors

From interviews, it became evident that companies with investment from angel investors, private finance and in some cases Scottish Enterprise possessed a greater awareness of the role an acquisition could play in securing a return for investors. These companies knew there would need to be an exit for existing funders and so continually factored this into their planning process. This awareness meant they were ultimately able to both provide a return to those investors who assisted them to grow to date whilst using the deal to shape the long-term future of the company. Each believed that acquisition presented the best opportunity to facilitate an exit and achieve growth.

It should be recognised that for many start-up companies, having a clearly understood and articulated exit strategy is a must. Without this, initial funding from private equity and angel investors will often simply not be available. Investors do not wish to make investments without knowing how and when a return will be realised. It became clear in interviews that whilst it added an additional layer of consideration for management, it also served as a helpful practice to ensure the inevitable exit was factored into the long-term plans for the company.

In no interviews was it made clear that pressure from investors necessitated the acquisition. That the company was seeking to grow and continue to do this meant they were looking for future investment, and the initial investment from supporters had simply run its course.

For example, one fast-growing young Scottish company had always been aware that their initial investors would require a return but in the interim period had undergone a period of substantial growth. At an appropriate juncture they began to work on considering the range of options open to them to find the next phase of investment whilst facilitating the necessary return for the original backers. This was a long-term approach spurred in part by the knowledge that an exit would be eventually required. The strongest argument was to replace the current suite of investors with one single private finance backer. This would simplify their current arrangements, enabling the company to work with a single backer with a longer term perspective, on growing the company in line with forecasts and current trajectory.

At the same time, unbeknownst to the Scottish company, a global company whom the Scottish firm worked with had commissioned consultants to draw up a list of potential acquisition targets in the UK. The Scottish firm appeared on this list and were subsequently approached regarding a potential acquisition. Initial scepticism and wariness (so much so that refinancing was referenced as 'Plan A') ultimately dissipated as discussions between the two companies began to articulate a shared set of objectives, as well as clear synergies developing. For example, being part of this global company would *"open doors around the world that we have tried and tried, but just cannot get open…There's no issue now – the doors are open."* for the Scottish company, whilst giving the global firm a strong and viable base in the UK market, and opportunity from its potential new Scottish base to break into markets with the access the Scottish company already enjoyed.

So when faced with the decision about which would unlock the potential growth trajectory for the Scottish company, due diligence demonstrated that an acquisition would provide everything refinancing would but with additional benefits through improved networks, access to markets and a deeper balance sheet. All of these would be achieved sooner than would have been the case developing organically, if indeed they ever would.

Reaching these goals only arose because of the drive to facilitate an exit for initial investors. It allowed the Scottish company to yield investment and higher growth in jobs, not just in the company but also the supply chain, whilst freeing up investors with increased returns to re-invest in more companies.

Economic conditions drive activity

Evidence from the literature has highlighted that when economies are in recession or particular markets are depressed, this can allow companies to secure advantageous prices. As detailed earlier this enabled a Scottish company to make two acquisitions in 2010 and 2011 which have added considerable profitability to the company and its turnover.

There is also a perceived downside to turbulent economic conditions, as some financial buyers target companies to profit through a re-sale. It could be argued that these 'financial acquisitions' offer the potential for having the most damaging and limiting effect for companies simply because of the assumption that they are focused solely on securing a profit through a sale.

One interviewee was the current manager of a company previous underperforming and once it had been *"through a turnaround"* which included a restructuring it was acquired by a foreign investor shortly before the recession of 2008.

There was no link between acquirer and acquired beforehand, the deal was purely financially motivated to achieve a profit from re-sale of a company after securing it for a *"bargain price"* as it came out of its difficulties. This proved a challenge which perhaps hindered the growth potential of the company, but at the same time, its turnover continued to grow, as did its employee numbers, its local supply chain and economic value within Scotland. Despite being acquired simply to achieve financial benefits through a future exit which will not be reinvested back into the Scottish economy, the company has continued to grow under a strong management team, and now stands ready with aspirations to acquire in order to add further value to the company within Scotland.

Is acquisition a route for Scottish companies to internationalise?

From all twelve interviews, acquisition was viewed as a means to take internationalisation further by expanding products and services in order to offer more to new and existing clients and customers. The seven inward acquisitions have provided opportunities for the Scottish company to broaden and deepen their international networks and customer base. The acquisition not only brought financial benefits and investment, but through partnering with a company based abroad, they were now able to use their new owners contacts to extend their activity internationally. The ability to deepen their international connections was a major driver for Scottish companies to consider a trade sale to a foreign company.

For outward acquisitions, Scottish companies' desire to deepen their international role was present, but less apparent as a principal objective. The main objectives of acquiring an overseas company tended to be securing key aspects of its supply chain, avoiding a range of logistical and bureaucratic aspects, including regulation, planning and taxation in overseas markets, avoiding time and resources being spent on matters that can be easily dealt with in the acquired firm's nation. It also gave the Scottish company greater control over products and services, streamlining production and enhancing the offer to customers, in turn enabling the business to grow internationally.

Small scale, high value intra-acquisitions

A notable feature observed was how a number of companies interviewed had acquired other, smaller Scottish companies (in relatively small deals) and used this to build capacity for additional work, bigger contracts and move further into new and existing markets. Through small scale acquisition these companies were able to add value to existing operations through expanding their product/service range, adding skills and capabilities to create a *"one stop shop"* for customers, enabling them to accelerate their growth. This then put the company into the next tier where they were working alongside larger companies, usually internationally, and had led to further sales and acquisitions in future.

It was acknowledged in these cases that the value added from the acquisition was far greater than the premium paid and ultimately led to (when there was an exit) a higher premium being paid by the acquirer of the Scottish company.

The Impact of Recycling

Interviews began to identify clear evidence of recycling holding a range of benefits which include more softer aspects, being created to the Scottish economy, that are being repeated on an ongoing basis. It has also began to show that the scale of recycling is far wider than simply focusing on the returns from sales and the subsequent career path of company management after an acquisition or exit.

It became apparent during interviews that recycling occurs at different levels of the economy. Whilst some of the exits may be of low value which previous research has suggested *"limits"* the ability for that individual to recycle investment[87], they provide value to the acquirer. In two cases, deals had added greater value to the acquiring Scottish company than the premium paid. It also enabled individuals who had started up a company working on a specific product who had little interest or desire to be part of a bigger company to return to what they do best, and perhaps repeat the process of developing a service/product before selling onto a further Scottish company and in so doing, stimulating ongoing development in the economy.

This is one aspect of recycling which began to appear throughout this research. Further examples of the types of recycling from this research alone are found at Figure 28, and there is no indication that this is an exhaustive list.

[87] Mason & Brown (2012) p.69-70

Figure 28: Recycling occurring within the economy from acquisitions

Financial

- With the deal, entrepreneurs who have exited companies have gone onto re-invest their return, across more than one company.
- Throughout the lifetime of the company, financial benefits have come via salaries, tax, supply chain, etc which have rippled out into the wider economy
- Acquisition has led to additional benefits being paid to staff, which are then invested amongst the local economy through retail and services
- Growth in the supply chain, with the subsequent impacts in the local economy

Knowledge

- Engagement with new practices, methods and companies at a global level has given Scottish leaders experience and skills previously unavailable.
- Entrepreneurs who have exited companies have gone onto share their learning and experiences with multiple companies. Without their exit this knowledge could have been restricted to one single firm.
- Employees of Scottish companies have been able to experience working practices in other nations, enhancing their skills and abilities, to increase their earnings elsewhere.

Individuals

- Staff who have worked within a company who has grown and through that, have a range of experiences which they can bring to enable future growth of the company or to apply in another company, potentially in starting one up.
- Entrepreneurs within Scotland who have started up businesses with a specific focus on products and services, to sell them on and then go back and work on establishing a further product and service

Reputation

- Sales and acquisition activity involving Scottish companies has raised the profile of Scotland, and its firms in certain sectors at an international level, which may lead to further investment opportunities

Alternatives to Acquisition

This chapter has focused on the reasons behind and consequences of pursuing an acquisition. However, interviews have also explored the alternatives companies have considered. Both routes are clearly being used as an avenue for growth, but are not the only option available to companies; for example, there is also investment in existing structures, a stock market listing, employee ownership or joint ventures.

Companies outlined their belief that these other avenues would not have allowed growth to occur as quickly and not to the level anticipated and subsequently being realised. In addition, some companies were established with the objective of realising a sale and a return on investment. Therefore, going through an exit was the only option ever fully considered or desired. It also needs to be noted that for many start-up companies, a condition of securing initial investment is to have a clear exit plan. In that sense, an exit was an inescapable part of the whole process and in the interviews it was evident this has been used to trigger a further or new period of growth for the company. On investing capital to grow, a range of reasons were put forward as to why this was not pursued, including not having the capital needed available to invest to the level required, and not being able to secure the funding elsewhere.

In summary, the reasons for pursuing an acquisition above other available alternatives came down to *risk* and to *speed*. On completion of the deal, companies had a ready-made supply of skilled staff, machinery, networks, knowledge and markets/orders. The ability to obtain these benefits almost instantly allowed growth to be realised much quicker than attempting to build these organically. In addition to this, it could be implied that companies saw a sale or acquisition as better value/lower cost route to growth. Companies had considered investment and diversification in order to grow but felt that there was no guarantee if or when the investment would pay off. One cited an example of a competitor in Scotland who had chosen to invest, but *"hadn't seen anywhere near the return they might have hoped for, and they have no real indication as to when they will, if indeed they do."* It was noticeable how no companies had considered flotation at any point as a way of taking the company forward.

For those companies who admitted on reflection that they perhaps did not consider the full suite of potential options open to them, two principal reasons were given. The first of these were that the decision to seek an exit was taken hastily and based on the need to enable a management exit at the time, which in turn led to ownership/management holding their own counsel about their options. In these cases, outcomes had been beneficial ultimately for the company, but on reflection, one interviewee felt that some external advice may have been beneficial; *"it might be a role for Scottish Enterprise, to come in and say these are your options, think about what you can do."* It appeared throughout the research that each company had their own approach to considering their various options, and that the time, effort and planning that went into each varied considerably.

For those companies who put time and resources into considering their objectives and laying down a clear plan to deliver on these, their experience was more positive. They felt more strongly that they had achieved, and in some cases, surpassed their ambitions. Whilst the pre-deal diligence was exhausting and thorough, it was believed to be time and energy well spent.

Those companies for whom decisions arose more from circumstance, whilst they did not regret decisions that were taken, it was acknowledged that some aspects may have been fortuitous and that potentially more diligence could have been undertaken to ensure the deal was the absolute best outcome for the company.

Summary

- Opportunities for acquisition are consistently presented to companies
- These opportunities shape the activity of Scottish companies regardless of whether an acquisition is part of an overall approach or plan
- Changes in circumstances, both within the company (e.g. retirement) but more widely in the economy (e.g. the changing nature of competition) are often factors leading ultimately to an acquisition
- Ambitions which drive sales and acquisitions are as follows:

  a) to *achieve growth*
  - Reflecting an ambition to strive to achieve more, and finding that an acquisition was the safest and most efficient way to achieve this
  - It allowed companies to break through barriers and obstacles to growth they were beginning to experience
  - It provided companies with a stronger financial position, enabling them to take on more work, and a greater range of work

  b) to *provide a return for investors*
  - Given the requirement for initial investment to have a clear exit strategy, exits provided an opportunity for companies to use a sale as a trigger point to drive growth

  c) to *facilitate a management exit*
  - Again, the desire for an exit focused company management on their ambition for the company, and in the cases interviewed, use it to springboard for growth

- Intra-acquisitions are often used by Scottish companies to trigger a period of growth, which can lead to further activity including a trade sale to an international company
- Acquisitions cause continuous ripple effects in the economy as individuals and capital move on as a result of deals being concluded. This recycling extends to softer aspects including reputations of people, places and sectors as well as the continuous learning from experiences of positive and negative acquisitions
- When faced with the opportunity of an acquisition, companies did not always consider in full every opportunity potentially available. This was due to a combination of a lack of time and general unawareness of alternatives, and a focus on acquisition as an avenue to pursue, driven by the belief that it was the best option available for the company.

CONCLUSIONS AND POLICY IMPLICATIONS

This research set out to explore an area in the Scottish economy about which little was known and much was assumed. It has highlighted trends and patterns of deals Scottish companies have made over the past decade, comparing this to similar economies. This has been complemented with a series of consultations with a diverse range of companies, each highlighting their experience of acquisition.

Whilst the relatively small group of Account Managed case studies has limitations in terms of its applicability across the whole economy, it has provided sufficient detail to begin to draw out a series of conclusions about the acquisitions market in Scotland and its effect on company growth and the wider economy.

Understanding the role of sales and acquisitions

Throughout the research it became increasingly clear that any consideration of the role and influence of acquisition needs to recognise two critical aspects.

Firstly, it is not automatic that what is good and beneficial for the company can be viewed similarly as desirable for the wider economy. Companies have their own, likely much narrower objectives focused around their growth, their market, securing investment, their supply chain, their staff and ultimately their bottom line. Wider issues around securing benefits within Scotland, the potential repatriation of profits overseas are not the principal concern of companies, as was made clear in interviews. If the two aligned then companies are content to see wider benefits, but it is not their primary objective. Therefore, any approach to support companies will need to recognise that companies can act in a way that is primarily focused on their own priorities, with wider issues around the Scottish economy remaining secondary.

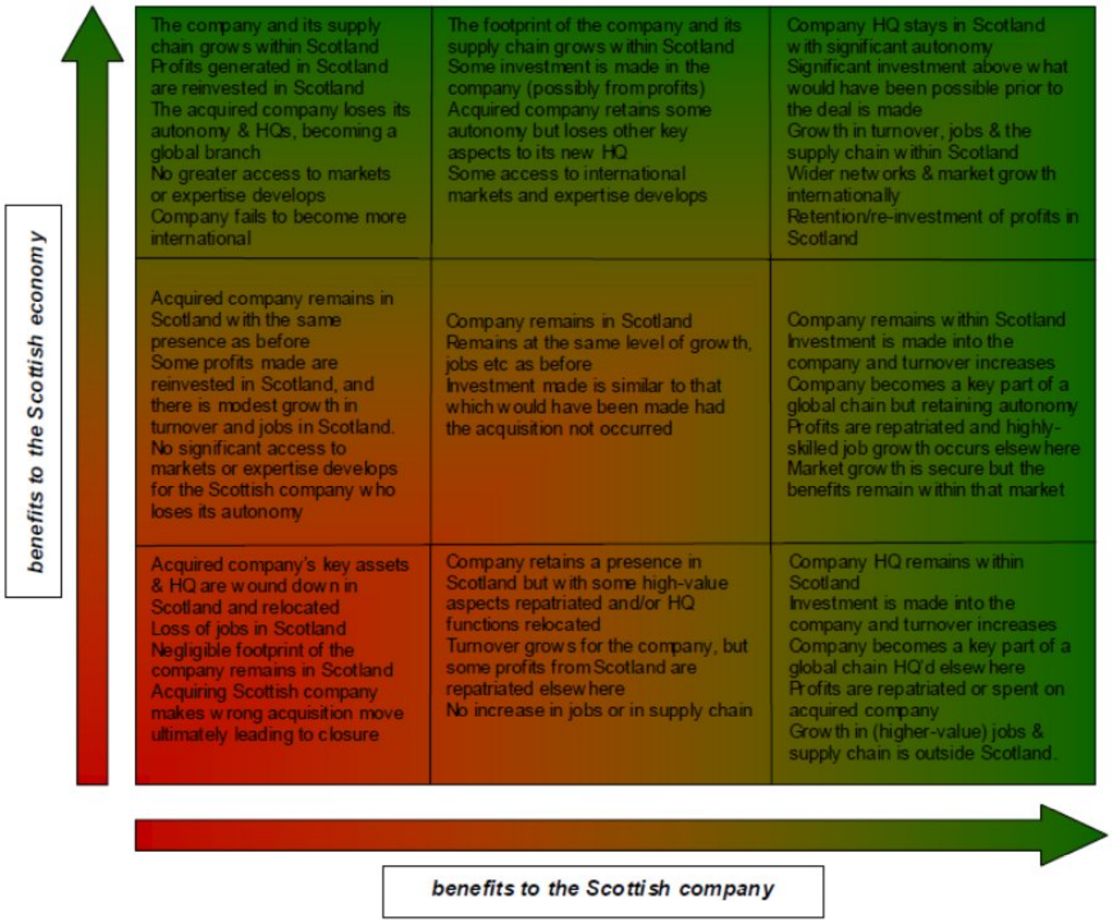
To begin to highlight how these two goals are not always mutually exclusive, Figure 29 plots a typology matrix along two axes, which shows what could lead to benefits for both companies and the economy; but also how the two aspects could diverge. This is based on the understanding gained through the case studies in this research but is a matrix designed to assist understanding and does not represent every business involved.

In addition, acquisitions need to be understood in the wider economic context, contrary to much research which tends to analyse deals in isolation. For example, if one company closes following an acquisition, those individuals who were part of the previous company may establish another company (if not multiple companies) and this is not restricted solely to management.

Recycling is also not solely about creating new companies. It can include staff members in the company using the skills, expertise and experience developed to start a new venture. At the same time, taxes, NI and salaries are paid which ripple outwards into the local and national community.

Furthermore, a range of reputational aspects can emerge from acquisitions, which are harder to quantify and often do not have an expiry date to the way in which learning can be passed on. Knowledge too, both good and bad, can flow from the experiences of everyone involved and observing a deal and be used to inform subsequent decisions and practices employed in acquisitions.

Figure 29 Acquisitions theoretical matrix



<u>Both sales and acquisitions have enabled Scottish companies to grow when embedded within Scotland</u>

This research has found that acquisitions of and by Scottish companies can and does lead to additional benefits being created within Scotland, both for the firm and the wider economy. There were three principal motivations for acquisitions: to facilitate growth, to enable a management exit and to provide a return for investors. Each of these factors has acted as a trigger point for growth, in line with current understanding around company growth not being linear[88].

It highlighted that inward acquisitions of Scottish companies can and do bring additional benefits to companies and the wider economy through growth in jobs, turnover, growth in the supply chain, investment in plants and machinery as well as staff. All of these benefits were above what the company would have been able to provide had it remained independent and may not have been able to provide through organic growth, certainly not at the same pace.

One of the reasons the inward acquisitions in this study have proved to be more beneficial, not just for the company but the economy, is because the acquired Scottish companies have been embedded within Scotland. When discussing the motivations of the buyer in interviews, it became apparent that the network of skills, public agency support, available expertise, and

[88] Scottish Enterprise, 2012

infrastructure, access to the Scottish and UK markets was attractive – and in many cases, essential features of the deal. These aspects lent themselves to an outcome which retained the company in Scotland post-sale, along with wider benefits to the company and economy, a view reinforced by Scotland's positive post-deal active rate compared to other European nations.

This suggests albeit from a small number of case studies, that current policies designed to support, nurture and ultimately embed companies within Scotland are proving successful in yielding benefits for companies and the wider economy. It provides a strong indication of what type of approach can work.

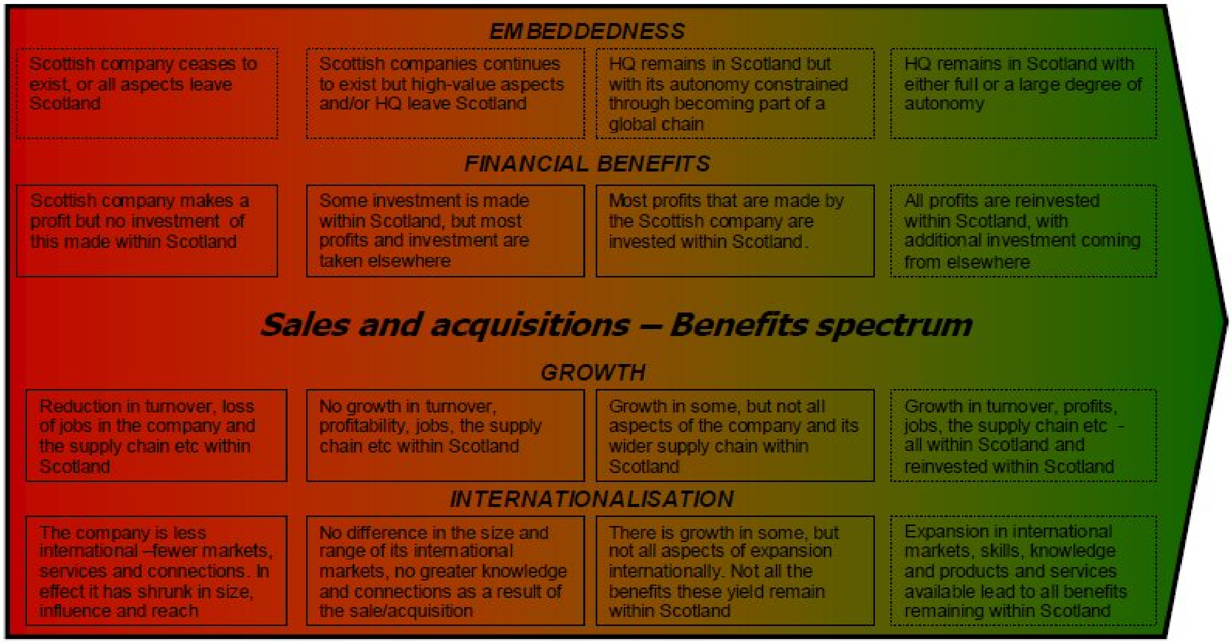
Cross-border acquisitions are time-consuming and resource intensive and can draw away the benefits assumed to flow back to Scotland, such as the repatriation of profits. The experience of the companies included as case studies here is that acquired companies in other nations require significant investment and attention from their new management, resulting in a lack of focus and investment in the headquarters back in Scotland.

It has also highlighted as any inward acquisition would, the issue around profits and whether there is any leakage of profits from Scotland as a result of an acquisition. The assumed wisdom is that an inward acquisition leads to repatriation of profits. It is evident that being acquired from outside Scotland invariably led to some profits made in Scotland not remaining here. However, it was emphasised in interviews that without the sale taking place, the company would not be experiencing the growth in jobs, in the supply chain and have secured the investment it has subsequently. They would also not have the access to international networks, larger contracts and greater expertise. In the minds of management some degree of profits not remaining within Scotland was an acceptable trade-off in order to secure wider benefits within Scotland for the company – and for the wider economy.

Similarly, Scottish company making an outward acquisition will be able to maximise the profits back within Scotland. However likely this is, this research has shown that it is not as simple as this, as profits (often more than originally envisaged) end up being invested in the acquired company, outside of Scotland, thus reducing the benefit they can have for the Scottish economy.

Again, to aid understanding of the complexities underlying the nature and impact of cross-border acquisitions involving a nation's firms and to support the development of approaches to minimise the risk of damaging sales and acquisitions, whilst ensuring as far as is possible, the benefits can be maximised, a spectrum plotting 'best' and 'worst' case scenarios has been developed (Figure 30).

Figure 30: Spectrum of benefits and risks to a company and the wider economy from an acquisition



<u>Companies have often chosen acquisition to overcome barriers they felt hindered their growth potential</u>

Companies have chosen to go down a route which led to an acquisition as a result of feeling a range of barriers were preventing them from reaching their aspirations. Companies have spoken about their growth potential in their domestic market being *"maxed out"* and having reached or approaching a *"glass ceiling"* whereby further growth was simply not possible without significant investment.

Whilst existing markets were strong and profitable, opportunities to grow within them appeared limited. Therefore companies across a range of sectors in Scotland recognised that securing additional growth required a new approach; a *"game changer"* as one described it. To build this up organically would in their view, take too long, be too costly and have a lesser chance of success as some had noted from the experiences of their competitors within Scotland.

Being acquired was also seen as providing greater financial security, which in turn enabled companies to compete for larger contracts with bigger companies, in order to yield even greater returns. Achieving and sustaining growth at the level they were experiencing had meant stretching their financial capabilities as far as possible, but in turn hindered them continuing this into the next phase. Being acquired had freed up Scottish companies to apply for and secure larger contracts with bigger companies, taking on additional work to break through their 'glass ceiling'.

They felt the advantages of being part of a larger international group with a greater suite of products and services available outweighed standing alone with a limited range of little interest to global companies seeking a client to provide everything themselves. As one MD of an acquired company put it, *"we had hit the limit of what we could do standing alone, it was time to partner up."*

In policy terms, the case studies have clearly highlighted what factors companies feel affect and limit their potential to grow and which ultimately led to consideration of the role that an acquisition can play. The availability of funds to invest, the access to markets and potential clients, greater finance reserves as well as the chance to grow the products and services they could offer were reasons that attracted companies towards either option. These indicate these as areas which companies prioritise and are focused on. Looking to remove these barriers can serve to provide companies with more options over their future growth, enabling them to make the best decision available rather than be constrained towards any particular option.

<u>Alternatives to acquisitions are not always explored or considered by companies</u>

The majority of company interviews highlighted that serious consideration was only really given to an acquisition. This was principally because of the belief that it was the quickest and safest route to achieve their ambitions. In these cases it was clear that all alternatives had been considered along the decision-making route, before an acquisition emerged as the preferred option.

In some cases, there did appear to be a lack of awareness of alternatives that could have been pursued. This led to the deals displaying a lack of long-term planning, or at least some strategic oversight. Whilst this had been successful in the experience of the company's interviewed this was more as a result of making a decision based upon circumstances and opportunities at the time rather than a long-term plan for growth.

This lack of long-term planning going into the acquisition process could be seen as leading to just sheer luck determining the outcome. That on reflection, some Managers felt they could have considered more options when contemplating a change in ownership or had further support suggests a potential role for policy-makers to assist companies to ensure this is the case when necessary.

However, it will need to be considered how companies are identified for this support. The cases in this research have demonstrated that those companies who could have been assisted in understanding all potential options, made decisions quickly – usually to facilitate a management exit. This represents a challenge and a requirement to identify companies that may potentially be facing a management exit in the medium to short-term and engage them in discussion.

Some of the trigger points the research highlighted could potentially be used to identify companies in order to offer support and in turn facilitate a fuller consideration of all available options for companies, and the selection of the most beneficial for the company in the long-term.

<u>Why does an acquisition fail to realise its objectives?</u>

Acquisitions can be used as a model to achieve growth, but the likelihood of this depends on a range of factors which increase the chance of success and of failure. This can provide lessons for companies and policy makers to ensure that when an acquisition is explored, elements which bring the greatest chance of success can be implemented. Interviews enabled the development of a range of aspects prominent in successful an unsuccessful acquisitions or sales (Figure 31).

Figure 31: Features of acquisitions deemed to have been beneficial and unsuccessful

Beneficial acquisitions	Unsuccessful acquisitions
• Company leadership, possessing a long-term vision • Management's ability to adapt and seize appropriate opportunities	• A lack of clarity amongst management about the company's ambition and focus • A lack of time to consider all

• Having clear objectives in selecting the opportunities to pursue • In inward acquisitions, retaining the incumbent management has secured positive benefits from their knowledge and commitment, and also ensuring value remains and grows within Scotland • Investment in equipment, staff development and opportunities – presenting a clear commitment to the company and its workforce in Scotland • Taking time to research options in order to identify the most beneficial deal partner. • In some cases it has appeared to be little more than *"luck"* and taking advantage of fortunate and timely circumstances arising and coinciding	available options • A lack of resources invested in considering the merits and risks involved in potential targets/suitors • An inability to recognise a changing environment, both globally and within particular sectors • An inability of management to adapt with circumstance • Being too ambitious and also, too conservative in plans • *"Bad luck"*

Role of management/advice

Of the items that determine success or otherwise, interviews confirmed the literature's perspective that the role and skills of management is arguably most critical to deals. Interviews consistently emphasised the value of prior experience. Not just of acquisitions, but in business more widely. The ongoing development of knowledge and experience, driven in part by recycling has helped Scottish managers understand what is important in making deals, and bring that experience to the benefit of their current companies.

Acquisitions continuously recycle investment, knowledge and skills for the economy, both in the present and the future

Current literature focuses solely on recycling in two forms - the level of capital returned through the acquisition to investors and/or entrepreneurs, and them alone; and subsequently what these individuals move onto next. This narrow definition and application of recycling fundamentally misunderstands this area, neglecting that recycling goes much further than simply these two aspects.

The observed trend of companies making small intra-Scotland deals before moving on to further deals, including internationally, suggests that a chain of acquisition exists, where companies with growth aspirations initially use the Scottish market to realise synergy gains in order to grow to a new level. Once at this level they may consider further acquisitions of further Scottish companies to continue this growth trajectory, but they are also at a level where cross-border acquisitions are also a possibility. It appears that, following a period of growth which includes one (or perhaps two) intra-acquisitions companies feel that they have reached a ceiling which hinders further domestic growth. After making an acquisition, this point has been when they have considered an alternative approach including being acquired in order to continue this growth.

The experience of three case study companies was one of making intra-acquisition(s) whilst growing, only to then consider cross-border sales when their growth potential was beginning to become limited. Their experience showed growth through each of the phases and demonstrated how acquisitions can be an important driver of growth and a feature of growth companies.

Interviews showed that small intra-acquisitions often add considerable value to fast-growing companies (beyond that of the deal price) which enable them to grow and in some cases, go onto further acquisitions. These have ultimately proved more beneficial to companies, staff, and the economy than the actual size of the intra-acquisition, without even beginning to factor in the wider benefits that spin out of acquisition. So whilst the median deal size between two Scottish companies may be noticeably lower than elsewhere, this can mask the full value.

It serves again to highlight that the true value of acquisitions, both in measurable and in softer aspects, is never truly complete and constantly continues to spin out and evolve.

Existing evidence demonstrates that repeat entrepreneurship, in particular from 'business failure' often provides the basis for future success[89]. This research has built on this understanding and demonstrated that learning is not restricted solely to the entrepreneur and those in management, and can extend to those holding junior positions in a previous company who have progressed into management in a future company. It adds a further dimension to our understanding of recycling which merits wider consideration of its impact on the economy.

Further insight on the true nature and role acquisitions play in a modern, vibrant economy would be benefitted through a separate study considering the full extent, scope and if possible, scale of recycling that emerges via acquisition. This study began to only scratch the surface of this issue which has predominantly focused on only two aspects but neglects to consider the fuller impact of recycling and its interconnectivity into the economy, some of which were included at Figure 28.

<u>International Activity of Scottish companies</u>

Acquisitions have been used to deepen international activity, providing a quicker route into markets, through securing additional resources, expertise and skills instantly, rather than adding these elements incrementally. In addition to this, it has also added to the international experience and perspective of Scottish companies and their employees.

Examples cited in the research showed that staff has been given the opportunity to work elsewhere on secondment, learn from practices at larger multi-national companies and be exposed to new practices and opportunities for development. In addition, management have been given the opportunity to enhance their management capability, through operating at a global and international level as a result of no longer having to focus on specific issues constantly, in particular securing on-going funding.

It is reassuring that Scotland's acquisition market shares common features and trends as similarly sized economies, and in many indicators it could be argued that Scotland's market has more positive indicators than elsewhere. For example, companies are not being acquired at a larger rate than elsewhere (though conversely, they are also less acquisitive than other nations) and post-deal active rates for acquired Scottish companies are amongst the highest in Europe.

Companies are active earlier in Scotland than elsewhere, which could signify that young Scottish companies are being acquired from abroad with greater loss (or potential loss to the economy). This is not the case however. Companies are younger, but indicators of company size from ZEPHYR appear to show that trade sales to international companies compare favourably to elsewhere. Even if companies are acquiring younger Scottish firms by overpaying, this reaffirms that the acquirer may be seeing the company not just as an asset to strip in order to compliment the core bases of the business, but to expand into Scotland,

[89] Byrne, Mullen, Marlow & Mason (2011), Cope (2011), Nielsen & Sarasvathy (2011)

recognising the value of the Scottish and UK market, and that the company has been strongly embedded.

Whilst the data comparisons may provide some comfort to those who fear the loss of value to Scotland above that experienced elsewhere, one potential future scenario needs to be highlighted. If we accept that being acquired provides a viable route to company growth, then the lack of internationalisation amongst Scottish companies could be seen to be hindering their growth. Scottish companies have a strong reliance on the UK market, a greater reliance on one country than any other. At this time policy initiatives are focused on increasing levels of internationalisation within the Scottish business base, principally through continuing the expansion in exports. These will bring clear benefits to the companies and the wider economy.

Being active internationally will also give Scottish company's access to a new set of networks and contacts which this research has suggested will likely lead to an increased opportunity for potential acquisitions. This could as this report has shown, lead to further growth and benefits for Scottish companies, but potentially threatens the benefits obtained through helping companies internationalise if wider economic benefits leave Scotland.

It is at this point that successfully embedding companies within Scotland will become increasingly important. Evidence from the case studies in this study suggest that the activities of Scottish Enterprise and its partners in building a world class business environment for potentially world class companies are successfully rooting companies ultimately acquired within Scotland, but in striving to increase the internationalisation of Scotland's business base, with a likely consequence being an increase in acquisitions as companies broaden their network, even greater importance and focus will be required on approaches which embed companies within Scotland.

Concluding thoughts

Based on the evidence of this research, acquisitions are adding value to the Scottish economy. Companies are acquiring and being acquired in order to enable growth via long-term strategic decisions and through taking advantage of opportunities arising due to circumstances such as the recession or a management exit.

The research begins to question some of the prevailing attitudes around the effects of acquisitions, providing evidence which indicates that it can and does add value to the Scottish company in the long-term, the wider economy and lead to growth. It is wrong to assume that inward acquisitions of Scottish companies are automatically wrong and lead to a loss of value, particularly in high-value aspects. This is, in part down to steps to embed companies within Scotland, which appear to be proving successful.

Similarly, we cannot assume that outward acquisitions made by Scottish companies are always successful and lead to greater economic benefits to the Scottish economy. The reality of cross-border transactions is too complex to be seen in such a simple way. Each deal is intrinsically unique and comprised of a multitude of different factors which at any particular point in time will influence the success or otherwise of the deal.

Despite this, a series of challenges are identified. There are a range of barriers which companies face in their growth trajectories which in the cases of companies interviewed in this research led them to an acquisition. These include an inability to secure the level of investment needed to grow organically, and certainly not at the same pace. At the same time, the company was not able to find the additional resources from within to make the investment, not to mention the difficulties in finding and attracting staff with the necessary skills. This prevented them from adding products and services to grow within their market and beyond, both within their sector and geographically.

Given the consistent message given throughout this research that companies are constantly considering what to do in order to grow, it may prove beneficial to increase understanding of some of these barriers and how they can be removed to give Scottish companies the best opportunity to grow. Although, given the scale of some of these challenges and how acquisition can specifically unlock these, focus may be required on those areas where the biggest difference can be made.

In addition to this, it was striking how when companies considered their options in the face of one of the three principal motivations for an acquisition, there was at times, a lack of consideration of other options. In seeking to support the development of global Scottish companies, raising the understanding of other routes to growth will need to be considered.

As a percentage of its business base, Scottish companies go through acquisitions at a lower rate than companies in other nations and when they do, there is a heavy reliance on the UK market. This suggests that it is not the existence of deals which is limiting the potential for Scottish companies to grow through this mechanism, but perhaps the lack of international companies.

These international comparisons suggests the challenges of growing companies within Scotland is not as a consequence of too many companies opting to be acquired, but instead begins to draw in wider issues including some wider issues around internationalisation, ambition and leadership. Understanding some of these barriers and perspectives further in this context will add to our understanding of what limits the number of truly global companies within Scotland. However, since evidence points strongly to a correlation between the networks of companies and acquisition activity, increasing the level of international Scottish firms will likely lead to an increase in acquisitions, which increases the importance of the approaches to embed companies within Scotland.

Finally, recycling is a critical part of the wider economic impact of acquisitions. It is an essential feature of the economy since it provides companies with the opportunity to add experienced and knowledgeable employees, it provides returns for investors and it also adds to the continuous learning within business. A further study looking specifically at recycling – both the hard evidence from following people and the money, but also the softer aspects such as reputation, learning and experience, could be particularly valuable in understanding the full impact and value of acquisitions.

These conclusions challenge some of the commonly held views regarding the value and effects, particularly of the acquisition of Scottish companies. The evidence gathered for this study found a prevailing view amongst Account Managed Scottish companies that acquisitions form a central part of their plans for growth for their company and their staff, regardless of the circumstances that faced them. As a characteristic of modern business, acquisitions are clearly one route through which to achieve company growth.

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APPENDICES

Appendix 1

SE Sector Definitions

Energy (including renewables):

SIC 05: Mining of coal and lignite

SIC 06: Extraction of crude petroleum and natural gas

SIC 09: Mining support service activities

SIC 19: Manufacture of coke and refined petroleum products

SIC 20.14: Manufacture of other organic based chemicals

SIC 35: Electricity, gas, steam and air conditioning supply

SIC 36: Water collection, treatment and supply

SIC 38.22: Treatment and disposal of hazardous waste

SIC 71.12/2 Engineering related scientific and technical consulting activities

SIC 74.90/1 Environmental consulting activities

Financial and Business Services:

SIC 64.1: Monetary intermediation

SIC 64.3: Trusts, funds and similar financial entities

SIC 64.9: Other financial service activities, except insurance and pension funding

SIC 65: Insurance, reinsurance and pension funding, except compulsory social security

SIC 66: Activities auxiliary to financial services and insurance activities

SIC 69.1: Legal activities

SIC 69.2: Accounting, bookkeeping and auditing activities; tax consultancy

SIC 70.2: Management consultancy activities

SIC 71.129: Other engineering activities (not including engineering design for industrial process and production or engineering related scientific and technical consulting activities)

SIC 73.2: Market research and public opinion polling

SIC 74.3: Translation and interpretation activities

SIC 78.109: Activities of employment placement agencies (other than motion picture, television and other theatrical casting) n.e.c.

SIC 78.3: Other human resources provision

SIC 82.1: Office administrative and support activities

SIC 82.2: Activities of call centres

SIC 82.3: Organisation of conventions and trade shows

SIC 82.91: Activities of collection agencies and credit bureaus

SIC 82.99: Other business support service activities n.e.c.

Food and Drink:

SIC 01: Crop and Animal Production, Hunting and Related Service Activities

SIC 03: Fishing and Aquaculture

SIC 10: Manufacture of Food Products

SIC 11: Manufacture of Beverages

Life Sciences:

SIC 21: Manufacture of basic pharmaceutical products and pharmaceutical preparations

SIC 26.6: Manufacture of irradiation, electromedical and electrotherapeutic equipment

SIC 32.5: Manufacture of medical and dental instruments and supplies

SIC 72.11: Research and experimental development on biotechnology

SIC 72.19: Other research and experimental development on natural sciences and engineering

Textiles

SIC 13: Manufacture of textiles

SIC 14: Manufacture of wearing apparel

SIC 15: Manufacture of leather and related products

Sustainable Tourism (Tourism related Industries)

SIC 55.1: Hotels and similar accommodation

SIC 55.2: Holiday and other short-stay accommodation

SIC 55.3: Camping grounds, recreational vehicle parks and trailer parks

SIC 56.1: Restaurants and mobile food service activities

SIC 56.3: Beverage serving activities

SIC 79.12: Tour operator activities

SIC 79.9: Other reservation service and related activities

SIC 91.02: Museum activities

SIC 91.03: Operation of historical sites and buildings and similar visitor attractions

SIC 91.04: Botanical and zoological gardens and nature reserve activities

SIC 93.11: Operation of sports facilities

SIC 93.199: Other sports activities (not including activities of racehorse owners) nec

SIC 93.21 Activities of amusement parks and theme parks

SIC 93.29: Other amusement and recreation activities

Technologies and Advanced Engineering

SIC 24: Manufacture of Basic Metals

SIC 25: Manufacture of Fabricated and Metal Products, except mach/equip

SIC 26: Manufacture of Computer, Electronic and Optical Products

SIC 27: Manufacture of Electrical Equipment

SIC 28: Manufacture of Machinery and Equipment (not elsewhere classified)

SIC 29: Manufacture of Motor Vehicles, Trailers and Semi-Trailers

SIC 30: Manufacture of Other Transport Equipment

SIC 33: Repair and Installation of Machinery and Equipment

SIC 62: Computer Programming, Consultancy and Related Activities

SIC 71: Architectural and Engineering Activities; Technical Testing and Analysis

Aerospace, Defence, Marine

SIC 13.940: Manufacture of cordage, rope, twine and netting (NB Not exclusively 'marine')

SIC 25.400: Manufacture of weapons and ammunition

SIC 26.110: Manufacture of electronic

SIC 26.701: Manufacture of optical precision instruments

SIC 28.110: Manufacture of engines and turbines, except aircraft, vehicle and cycle engines

SIC 30.110: Building of ships and floating structures

SIC 30.120: Building of pleasure and sporting boats

SIC 30.300: Manufacture of air and spacecraft and related machinery

SIC 30.400: Manufacture of military fighting vehicles

SIC 33.150: Repair and maintenance of ships and boats

SIC 33.160: Repair and maintenance of aircraft and spacecraft

SIC 38.310: Dismantling of wrecks

SIC 84.220: Defence activities

Chemical Sciences

SIC 19: Manufacture of coke and refined petroleum products

SIC 20: Manufacture of chemicals and chemical products

SIC 21: Manufacture of basic pharmaceutical products and pharmaceutical preparations

Construction

SIC 41: Construction of buildings

SIC 42: Civil engineering

SIC 43: Specialised construction activities

Forest & Timber Technologies

SIC 02: Forestry and logging

SIC 16: Manufacture of wood and of products of wood and cork, except furniture; manufacture of articles of straw and plaiting materials

SIC 17: Manufacture of paper and paper products

Creative Industries

SIC	Description	Proportion of SIC (%)
73.11	Advertising agencies	100
73.12	Media representation	100
71.11	Architectural activities	100
47.78/1	Retail sale in commercial art galleries	100
31.09	Manufacture of other furniture	100
32.12	Manufacture of jewellery and related products	100
32.13	Manufacture of imitation jewellery and related articles	100
47.79/1	Retail sale of antiques and antique books	100
95.24	Repair of furniture and home furnishings	100
71.12/1	Engineering design activities for industrial process and production	100
90.01	Performing arts	100

SIC	Description	Proportion of SIC (%)
90.02	Support activities to performing arts	100
90.04	Operation of arts facilities	100
78.10/1	Motion picture, television and other theatrical casting	100
59.2	Sound recording and music publishing activities	100
18.20/1	Reproduction of sound recording	100
32.2	Manufacture of musical instruments	100
74.20/1	Portrait photographic activities	100
74.20/2	Other specialist photography (not including portrait photography)	100
74.20/9	Other photographic activities (not including portrait and other specialist photography and film processing) n.e.c.	100
18.20/2	Reproduction of video recording	100
59.11/1	Motion picture production activities	100
59.11/2	Video production activities	100
59.13/1	Motion picture distribution activities	100
59.13/2	Video distribution activities	100
59.14	Motion picture projection activities	100
58.21	Publishing of computer games	100
62.01/1	Ready-made interactive leisure and entertainment software development	100
59.11/3	Television programme production activities	100
59.13/3	Television programme distribution activities	100
60.1	Radio broadcasting	100
60.2	Television programming and broadcasting activities	100
58.11	Book publishing	100
58.13	Publishing of newspapers	100
58.14	Publishing of journals and periodicals	100
58.19	Other publishing activities	100
18.11	Printing of newspapers	100
18.129	Other printing (not labels)	100

SIC	Description	Proportion of SIC (%)
18.13	Pre press and media services	100
63.91	News agency activities	100
91.01	Libraries and archive activities	100
58.29	Other software publishing	100
62.01/2	Business and domestic software development	100
62.02	Computer consultancy activities	100
85.52	Cultural Education	100
90.03	Artistic creation	70
16.29	Manufacture of other wood products	30
23.41	Manufacture of ceramic household and ornamental articles	35
23.49	Manufacture of other ceramic products	35
23.13	Manufacture of hollow glass	15
23.19	Manufacture of other glass	15
13	Manufacture of textiles	25
14	Manufacture of wearing apparel	20
15	Manufacture of leather and related products	20
74.1	Specialised design activities	25
74.1	Specialised design activities	75
59.12	Motion picture, video and television programme post-production activities	25
59.12	Motion picture, video and television programme post-production activities	75
90.03	Artistic creation	30

SIC 59.12 is partly under Film & Video (25%) and Radio & TV (75%)

SIC 74.1 is partly under Fashion & Textiles (25%) and Design (75%)

SIC 90.03 is partly under Visual Art (70%) and Writing and Publishing (30%)