Seat No.: ________ Enrolment No.___________

GUJARAT TECHNOLOGICAL UNIVERSITY

MBA - SEMESTER– IV EXAMINATION – WINTER 2020

Subject Code:1549321 Date:04/01/2021

Subject Name:Specialization-Finance_Mergers & Acquisitions (M&A)

Time:02:00 PM TO 04.00 PM Total Marks: 47

Instructions:

1. **Attempt any THREE questions from Q1 to Q6.**
2. **Q7 is compulsory.**
3. **Make suitable assumptions wherever necessary.**
4. **Figures to the right indicate full marks.**

Q.1 Explain the terms.

Q.1(A) Explain the terms. **06**

1. Insider Trading
2. Equity Carve Out
3. Synergy

Q.1(B) Explain the terms. **06**

4. ESOPs
5. Take Over
6. Joint Ventures

Q.2	(a)	Explain Corporate Restructuring and Forms of restructuring Business Firms.	06
	(b)	Discuss Horizontal, Vertical and Conglomarate mergers with suitable examples.	06
Q.3	(a)	What are the major factors influencing cross boarder M&A Activity? Discuss	06
	(b)	Discuss Causes and motives for sell offs and divestitures.	06
Q.4	(a)	List down various theories of M&A explain in detail Differential Managerial theory and Hubris Hypothesis.	06
	(b)	Distinguish Spin-off from split up. Give examples.	06
Q.5	(a)	Write a note on JV as one form of restructuring business.	06
	(b)	Explain Going Private and leveraged Buy outs in detail.	06
Q.6	(a)	Synergy is the ability of a merged company to create more shareholder value than standalone entity. Discuss types and sources of synergy.	06
	(b)	What are the advantages & disadvantages of ESOP?	06

Q.7 **Marriot's Bondholder's taken for a spin (or for a ride?)**

In 1993 Marriott Corporation (MC) carried out a spinoff of its hotel management business to shareholders. In 1992, MC had revenues of $8.7bn and operating profits Di $496m. The group consisted of two broad categories of businesses — the lodging management group including hotels that contributed 52% of group revenues and 68% of operating profits, and contract services catering and facilities management, airport and highway concessions that accounted for the rest. With two-thirds of its operating profit from lodgings related businesses, MC was generally viewed as a hotel company.

MC pursued ambitious growth and profitability objectives in the hotel business through a strategy of developing and then selling hotels while retaining the right to manage them. Management separated from the ownership of these properties, required smaller capital to fund growth but also reduced the volatility of cash flows. This low volatility allowed MG management to maintain high levels of debt. MC's operating profit increased yearly from 1986 to 1989 in both lodging management and contract services group. However, in 1990-91 recession hit the, hotel occupancy rates and profits. The contract service businesses also suffered. MC had built up a large portfolio of hotel properties that were difficult to sell in the recession. It replaced high-risk senior debt with lower-risk subordinated debt against the background of falling credit rating of its debt.
Under the spinoff plan announced in October 1992, the lodging management, catering and other service businesses were to be spun off into Marriott International (MI). The parent, renamed Host Marriott (Host) retained ownership of the hotel and real estate interests. MI, under a long-term contract with Host, would manage the hotel properties. The Marriott family would continue to oversee all of the businesses and the senior management of MC would be split between MI and Host.

MC argued that the spinoff would benefit shareholders by

- allowing MI to exploit its growth opportunities in the management business;
- allowing the capital markets to value MI more accurately because of better financial information;
- Giving shareholders better investment options between a high-growth management company and a capital-intensive company with strong cash flow and long-term capital appreciation.

The initial spinoff proposal allocated most of MC's long-term debt to Host. When compared with the level of assets and operating cash flow, this allocation made Host vastly more risky than MT as shown below. This sparked considerable resistance from creditors who felt their debt was being put at high risk since most of it was being assigned to cyclical property business and very little to the management business with more stable cash flow. The interest cover ratio shows higher risk clearly. Such an allocation reduces the default risk faced by the shareholders and increases it for creditors, thereby transferring some of the corporate value from creditors to shareholders.

Assests/Liabilities	MC	First Proposal		Final proposal	
		MI	Host	MI	Host
Total Assets	6333	2360	4620	3017	3888
Proprietary & equipment	3672	360	3310	772	2689
Current Liabilities	1189	1130	210	1280	394
Long Term debt	2891	20	2870	899	2313
EBITDA/ Int.Expenses	2.6	20.3	1.3	6.5	1.8

Given the storm of protest from creditors and their Class action suits, MC revised the spin off proposal and reallocated more debt to the management business. This mitigated the additional risk faced by the creditors. MC was forced to accept several conditions, such as repurchase of debt, stricter covenants, higher coupon rate on new debt, etc. to the benefit of creditors. The revised spinoff plan was implemented.

Robert Parrino estimated the market-adjusted bondholder loss at $195m and industry adjusted shareholder gains at $81m, Thus the spinoff caused a $114m decline in the total value of these securities from spinoff announcement to distribution. The spinoff failed to create shareholder value in the period surrounding the spin off and destroyed the bondholder value. What could be the reasons for this? There are several direct and indirect costs to a spinoff— direct transaction costs, loss of ability to offset Host's losses with MI’s profits and thereby save on corporation tax, the increased coupon on new debt, value of warrants issued to creditors, duplication of accounting and financial systems, higher costs of new security issues, etc.

The Marriott family continued to maintain control over the entire firm. The spinoff limited the potential losses to Marriott family from any default on debt. The separation improved the management business's debt capacity and this would allow the family to pursue growth in this business aggressively without losing control.

Q.7 (a) Why did Marriott decide to go for a spinoff? 5.5

(b) What is the initial structure of the spinoff? Why MC was required to change it? 5.5

OR

Q.7 (a) Is there a conflict of interests in spinoffs among various stakeholders? 5.5

(b) How were these resolved in the Marriott case? 5.5

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