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To Our Clients:

Takeovers are Back

Just three months after the October market crash, takeover activity has come back as strong as ever. The revival spans the entire spectrum of takeover activity from highly leveraged bustups to multibillion dollar cash bids by major companies. Combination tender offer and proxy fight takeovers have reappeared and so has the pacman defense. In addition to the revival of old takeover strategies, new ground is being broken in hostile takeovers. This is what is happening:

Foreign money; cheap dollars. The $4.3 billion bid by Hoffman La Roche for Sterling Drug and the $4.2 billion bid by British American Tobacco for Farmers Group show the attraction of prominent American companies for foreign companies able to take advantage of the 50% reduction since 1985 in the value of the dollar. We can expect much more of this.

Highly leveraged bustups. Last year Campeau took over Allied Stores in a $3.4 billion highly leveraged transaction financed by a bridge loan that was refunded with junk bonds. Following the takeover, Campeau embarked on a bustup of Allied selling off major parts. The $4.2 billion Federated Department Stores bid announced by Campeau this week is a close parallel of the Allied bid.

Hostile bid in the same community. Emhart and Stanadyne are both prominent members of the Hartford business community with many business and social overlaps. Rarely, if ever, has one such company made a hostile bid for another. Yet Emhart made a $.6 billion bid for Stanadyne evidencing the breakdown of the last remaining cultural barriers to hostile takeovers.

High tech takeovers. The heavy dependence on people, the high-price earning ratios, large amounts of good will and rapid product obsolescence have restricted high tech mergers and even more so hostile bids for high tech companies. The $.4 billion bid by Prime Computer for Computervision portends a new field for hostile bids.

Proxy fights. The E II threat of a proxy fight for American Brands (to which there is a pacman response) and the Bank of New York's intention to combine its hostile bid for Irving Bank with a proxy fight to remove the Irving Bank board of directors show the potency of proxy fights in this era of institutional ownership.

Junk bonds and other takeover financing. The junk bond market is not what it was before the crash. However, it is still there and is giving signs of reviving. Bilzerian got the financing for his $1 billion takeover of Singer and NEOAX has made a $.5 billion bid for IU International on the basis of a Drexel highly confident letter. Bridge loans are still available and bank financing is more available than ever before.

New players. Several of the major commercial banks have become significant factors in advising on takeovers. The Hoffman La Roche bid for Sterling marked the entry of J.P. Morgan as an advisor to a hostile bidder. Sterling alleged that Morgan's role in advising Hoffman breached a fifty-year relationship between Morgan and Sterling and belied an extensive advertising campaign promoting Morgan's relationship approach to merger advisory services. Hoffman started its tender offer at $72, then unilaterally raised to $76 and then again to $81, only to lose to an $89.50 white knight bid by Kodak. While the Hoffman bid was flawed by bad pricing and bad tactics, it brought home the new role of the Morgan bank.

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There does not appear to be much to slow this resurgence of takeover activity. Meaningful federal legislation is at best a remote possibility. The new Delaware takeover law is totally ineffective against the type of bids we are currently experiencing and despite all the loud objections by Boone Pickens, will not slow takeover activity. The only effective protection against abusive takeover tactics is the second-generation poison pill now starting to be adopted by major companies.

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