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To Our Clients:

Takeovers: An Update

The past year has seen the return of strategic acquisitions and, to a limited extent, the return of hostile tender offers.

Much of the acquisition activity has been concentrated in four areas --

- defense contractors
- healthcare
- financial services
- communications/media

In each area, there is a technological reason propelling the acquisition activity.

The sharp reductions in the defense budget have motivated the sale of defense businesses by conglomerates and the combination of defense companies to improve margins through synergy savings.

The pressure of the escalating costs of medical insurance and the prospect of the Clinton healthcare legislation underlie the merger activity in the healthcare industry.

The changes in regulation permitting multistate banking and the expansion of banks into the securities business and the mutual fund business, the large savings available from expense elimination from in-city combinations and the need to deal with portfolio and capital problems have been the reasons for the activity in financial services.

The coming of interactivity, the desire to combine software with hardware, the changes in regulation and the development of new technology are causing the rapid increase in acquisition activity in communications/media.

Adding to the acquisition activity has been the significant pressure from activist institutional shareholders on multi-industry companies to spin-off or sell underperforming divisions or divisions that sell at low price earnings multiples and are perceived (rightly or wrongly) as dragging down the market valuation of the remaining high multiple business.

The Paramount and Grumman situations show that strategic mergers -- even multibillion deals -- can generate the same type of competitive activity as the financially motivated takeovers of the 1980s. The same reasons that lead a company to compete for a strategic acquisition may result in an increase in initial hostile takeover attempts.

Further fueling the new takeover activity are the renewed availability of bank financing, the revival of common stock pooling mergers (particularly in financial services and healthcare), the markets' acceptance of junk bonds and derivatives as takeover currency, the markets' disregard of goodwill in communications/media acquisitions and the erroneous but widely held view in boardrooms that the poison-pill-just-say-no defense is no longer feasible.

The present takeover environment warrants reexamination of strategic plans, takeover response preparation and senior management and board of directors understanding of current legal and tactical thinking with respect to takeovers. Many companies have neglected takeover response preparation during the period of reduced activity since 1989. The events of the past year indicate a significant probability of increased acquisition activity and the expansion of takeovers into other industries.

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