INTERNATIONAL CORPORATE RELATIONS
Strategic Alliance and M&A
The Case of Honda, Rover and BMW

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ABSTRACT

The primary objective of the dissertation is to compare and contrast two strategies of international corporate relations; "strategic alliances" and "mergers and acquisitions". The focus would be on Honda, Rover and BMW which exhibited characteristics, strengths and weaknesses of both "strategic alliances" and "mergers and acquisitions". The thesis will also demonstrate how the BMW deal caused instability and thus made the alliance vulnerable. When companies like Honda, Rover and BMW adopt either a strategic alliance or a merger and an acquisition, they tend to have uniform objectives. Entrance to new markets, development of new products and improvement of organisational structures should be a company's ultimate goal. On the contrary the Honda-Rover alliance did not last long as it was broken by the acquisition of Rover by BMW. The theoretical approaches to both strategic alliance and merger and acquisition adopted by the car companies contrasted each other. Strategic alliances are characterised by friendly and safer approaches, which usually delays a company from achieving its objective. At times mergers and acquisitions can be subjected to a hostile environment, which can easily be overcome by the company's willingness to expand its productive capacity. Due to its long-term nature, a strategic alliance tends to distort corporate goals. Lack of formal contract between companies is likely to destabilise the alliance. On the other hand, a merger and an acquisition incurs financial risks, which can create complex and conflicting objectives for the company.

Chapter One

Introduction

1.1 Overview

In the present business world, "strategic alliance" and "mergers and acquisitions" are common strategies, and, particularly in the motor industry, those strategies are being chosen as rational and effective strategies. Historically, "mergers and acquisitions" have been very popular because it is the quickest way to achieve a company's objectives. In the motor industry, many automobile producers who were inefficient have been absorbed by larger and stronger companies in the form of mergers or acquisitions. However, as the market has become globally oriented and the level of uncertainty has increased, strategic alliances have been formed to reduce costs and risks, as well as to improve management.

Nevertheless, it can not be said that a strategic alliance is always an adequate strategy. It has also some disadvantages and mergers or acquisitions can be appropriate strategies in some situation. The case of Honda-Rover-BMW is the case which brought out the weaknesses of a strategic alliance, and the unilateral and forcible characteristics of a merger and an acquisition, and which emphasised difficulties of managing international corporate relation.

1.2 Aim and Objectives

The main aim of the research is to compare and contrast characteristics of strategic alliances and of mergers and acquisitions, and to examine when a company is motivated to form a strategic alliance and why a company decided to choose a merger or an acquisition, on the basis of the Honda-Rover-BMW case. In addition, the objectives of the Honda-Rover-BMW case are, firstly, to clarify how those strategies affected to each other, why Honda and Rover needed to form a strategic alliance, why Honda did not or could not acquire Rover and why BMW acquired Rover, and, secondly, to evaluate an effectiveness of both "strategic alliances" and "mergers and acquisitions" in the Honda-Rover-BMW case from the theoretical perspective.

1.3 Structure

This dissertation, which is completed on the basis of aim and objectives above, is divided into six chapters. The structure is as follows.

Chapter one comprises the overview of the research, aim and objectives, and the structure of this dissertation. In addition, the methodology of the research and the limitations which were inevitable in the process of the research are mentioned.

In chapter two, the main features of "strategic alliances" and "mergers and acquisitions" are looked at from the theoretical perspective. The first half of the chapter focuses on "strategic alliances" and examines the reasons why a company approaches this strategy, its advantages and disadvantages, and factors for a successful strategic alliance. Similarly, the second half concentrates on "mergers and acquisitions" and explores how it has been defined, what motivation there is for choosing a merger or an acquisition, and the strengths and weaknesses of the merger and acquisition..

In chapter three, the practical aspects of "strategic alliances" in the automobile industry are mainly discussed by using the case of the international corporate relations between Honda and Rover. The reason for the alliance and its effect to the both companies are also described.

In chapter four, the features of "mergers and acquisitions" in BMW-Rover trade are studied and the reasons why BMW decided to acquire Rover, and why British Aerospace (BAe) wanted to dispose of its motor vehicle business, are both considered. Moreover, the effect of BMW's acquisition on Honda-Rover is argued from both Honda's and Rover's perspective.

In chapter five, the strengths and problems of the strategic alliance between Honda and Rover are firstly analysed by consulting strategic alliance theories. Secondly, the acquisition between BMW and Rover are also assessed from the theoretical point of view.

In chapter six, in conclusion, the whole chapter is reviewed and then recommendations to Honda, Rover and BMW are also made.

1.4 Methodology

Theoretical parts of this dissertation were based mostly on books which were written by scholars who have researched particularly on strategic alliances and mergers and acquisitions in a strategic management. Recent periodicals and journals about both strategies were also referred to. Regarding the Honda-Rover-BMW case, the financial situation which seems to have directly affected motivation for their decisions was researched through the annual report of each company and world automobile data books, and other details of relation between companies were examined through articles of newspapers, journals and periodicals between 1994 and 1995. Furthermore, direct research to Rover, which was in the centre of the case, was done by asking questions about the Honda-Rover alliance and BMW acquisition to the staff working at Rover in Oxford.

1.5 Limitations

Considering the nature of the automobile industry which is continuously changing, what is maintained and suggested regarding the Honda, Rover and BMW relation in this dissertation may not be necessarily appropriate for the current situation. Moreover, about evaluation, it should be noted that a "theory" is just a "theory". Theories in business tend not to fit real situations. Therefore, in this dissertation, there may be some contradictions between theories and the Honda-Rover-BMW practice.

Chapter Two

"Strategic Alliance" and "Merger and Acquisition" Theoretical View

In the alliance business, nothing is forever.
Financial Times 25 February 1994

The importance of a strategic alliance has increased since organisations started to operate on a global level and market complexity has increased due to decreasing boundaries between countries. Similarly, mergers and acquisitions are also regarded as effective strategies when a company enters a new business or a new market.

In this chapter, the different characteristics of both strategies are mainly focused on from the theoretical perspective. Firstly, the effectiveness and problems of a strategic alliance will be evaluated. Secondly, the reasons of a merger's popularity and less popular aspects will be described. Finally, differences of purpose and attitude towards both strategies between countries will be looked at by using the example of Japan and Western countries.

2.1 Strategic Alliance

2.1.1 Definition

It seems that "Strategic Alliance" and "Joint Venture" are forms of corporate collaboration. However, both can be clearly separated in terms of their different characteristics. Historically, joint ventures have been defined as new business entities that are owned by two or more firms that share resources and skills. (Pekar and Allio, 1994) That is, owners hold an equity, share decision-making responsibility for the management and the benefit or loss resulting from the joint venture. Lynch (1993) also defined joint ventures as that they are formalised alliances uniting two or more separate organisations and resulting in; 1) the creation of a new separate business entity; 2) the allocation of ownership, operational responsibilities, and financial risks and rewards to each sponsor, while preserving their separate identities/autonomy; and 3) staffing by a separate management team. On the other hand, strategic alliances are defined as the most simple and basic alliances. According to Lynch (1993), strategic alliances are informal business relations characterised by; 1) tight operation linkage, such as cross-training, product development co-ordination, long-term contents based on quality, not just price; 2) mutual vested interest in each other's future; 3) long-term strategic orientation; 4) top-rank support; frequency of contract at top and middle levels; 5) reciprocal relationship sharing strengths, information, and mutual advantages; 6) co-ordinative management styles organised around collaboration, not hierarchical power. Pekar and Allio (1994) pointed out that firms are increasingly co-operating through non-equity ventures and this new

Figure 2.1 Types of and motives for strategic alliances

	LOOSE (MARKET) RELATIONSHIPS	**CONTRACTUAL RELATIONSHIPS**	**FORMALISED OWNERSHIP/RELATIONSHIP**	**FORMAL INTEGRATION**
FORMS OF ALLIANCE	**Networks Opportunistic alliances**	**Subcontracting Licences and franchises**	**Consortia Joint ventures**	**Acquisition and mergers**
INFLUENCES Asset management	Assets do not need joint management	Asset management can be isolated	Assets need to be jointly managed	
Asset separability	Assets cannot be separated	Asset/skills can be separated		Assets cannot be separated
Asset appropriability	High risk of assets being appropriated	Low risk of assets being appropriated		High risk of asset appropriated

(Source : Johnson and Scholes, Exploring Corporate Strategy, 1984, p238)

approach is rapidly becoming the key to success in fast-evolving industries such as electronic component technology, computer hardware and soft-ware, environment, drugs and medicine, financial services and robotics. In Figure 2.1, Johnson and Scholes (1984) summarised types of and motives for strategic alliances.

Such non-equity co-operative agreements which are technology swaps, R&D exchanges, manufacturer-supplier relationship, and distribution and marketing support have been common practice in the business world for a long time. In addition, it seemed that these relationships tended not to be crucial and were unlikely to drastically affect a company's competitive position in an industry. However, currently, these strategic alliances have become important in order to secure, maintain and reinforce a company's competitive advantage because of industry and technology revolution and the blurring of national and competitive boundaries. Thus, it has become an essential factor for a company to form a strategic alliance with other companies in order to survive or to establish a further competitive edge in a changeable, transitional and dynamic market situation.

2.1.2 Why Strategic Alliance ?

Environmental change

The business environment has dramatically changed since the recession because of the oil crisis in 1970s. Demand for many products and services has stagnated and the markets that showed high growth rate have started to shrink. Hence, competition in many markets has got keener and companies have been compelled to seek a way to maintain their market share and competitive position in a low growth or declining demand situation. However, in a stagnating market, it has been difficult to establish distinctive advantages against competitors and it has depended greatly on a company's ability whether or not it can protect its business from competitive offence and can deter competition from aggressive acts.

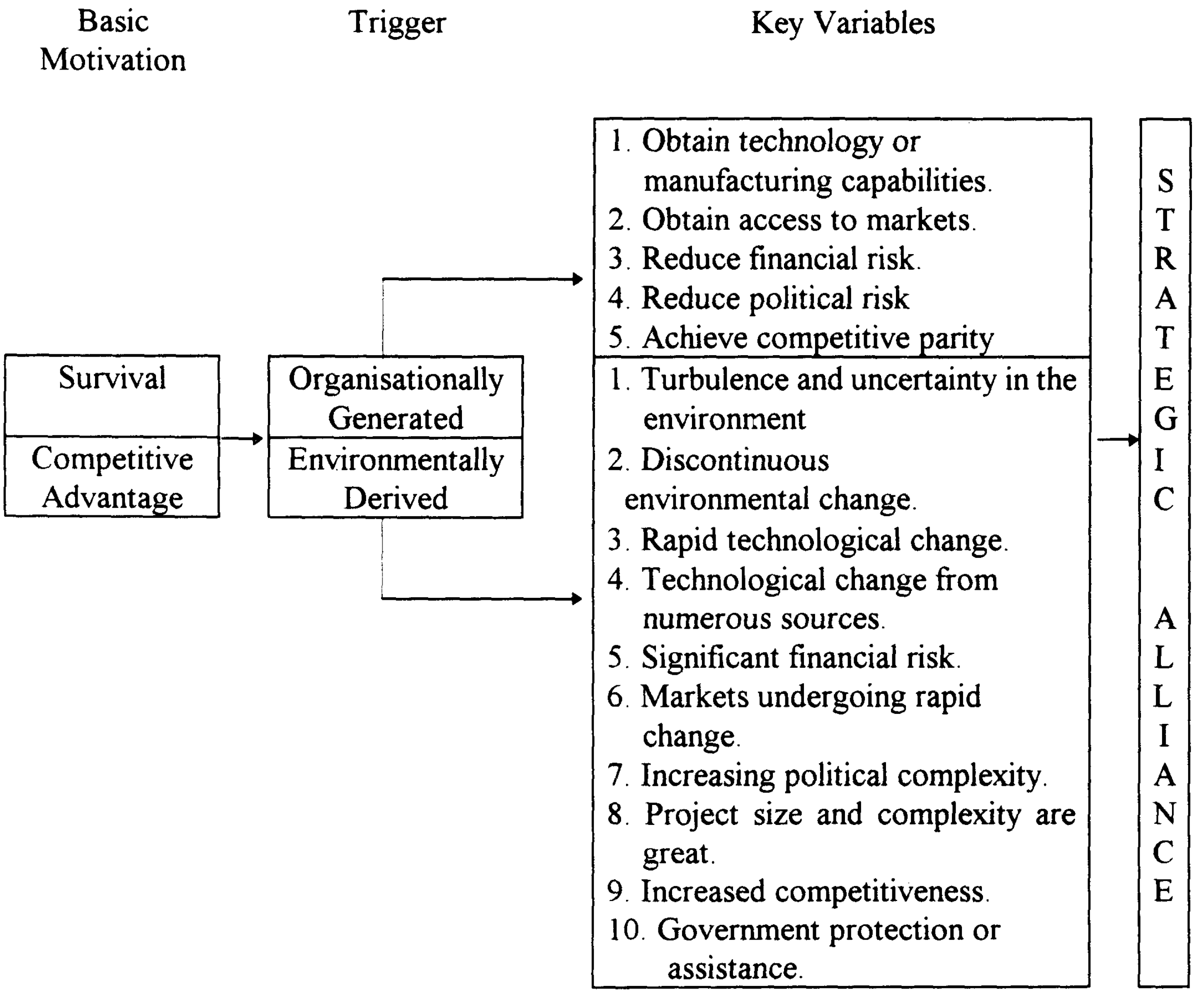
In addition to sluggish market growth, the costs for maintaining business have increased dramatically. James et al. (1985) identified three factors which lead to increase of costs; 1) the heavy expenditure required to develop and bring to market new technologies, processes and products; 2) the growth in and complexity of regulatory compliance; and 3) the need to compete on a world-wide basis and the increased marketing costs associated with competing in a mature market have combined to increase business expenses. Furthermore, business has been moving from a domestic market to a global one. Rapid development of new technology has made it easy for companies to exchange information and to transport products and services internationally. Hence, companies have moved to seek new markets abroad in order to acquire new sources of growth outside a mature home market and to reduce costs for R&D by maximising their business opportunities.

Emergence of global strategic alliance

Many companies started to look at strategic alliances as a crucial factor for future survival since their business was expanded internationally. It can be said that the main purposes for companies to form strategic alliances with others are to enter new markets to learn new skills, and to share risks and resources. In general, local situation and start-up costs in new markets are considerable barriers to successful market penetration. These barriers can be reduced by obtaining local knowledge and using local supply and distribution channels through an alliance with local companies. Similarly, the company can easily gain access to its partners' technology and operations skills such as product development, marketing and production system. It is also significant to shorten development spans and reduce costs for R&D which is normally time consuming and expensive. Moreover, by using alliance strategies, companies can offset some of the high investment costs and greater risk when the companies enter new markets or when they develop new products.

Murray and Mahon (1993) identified alliances that occurred in response to two underlying motivations: a 'defensive' instinct *to survive* or an 'offensive' desire *to achieve competitive advantage*. As can be seen from Figure 2.2, strategic alliance is triggered by either internal, external or both factors on the basis of two types of basic motivations. It can be seen that internal factors which encourage strategic alliance are lack of technology or manufacturing capability of a company, quick and easy market access and reduction of financial and political risk in local operation, while external factors are increase of uncertainty and fluctuating market situation in the environment, rapid and various technological changes, complexity of political matters in the local market, increase of size and complexity of project, and intensification of global competition. Moreover, James et al. (1985) clarified the most widely used alliance strategies. (Figure 2.3) They also maintained that, in business, the partners generally seek to combine financial, marketing,

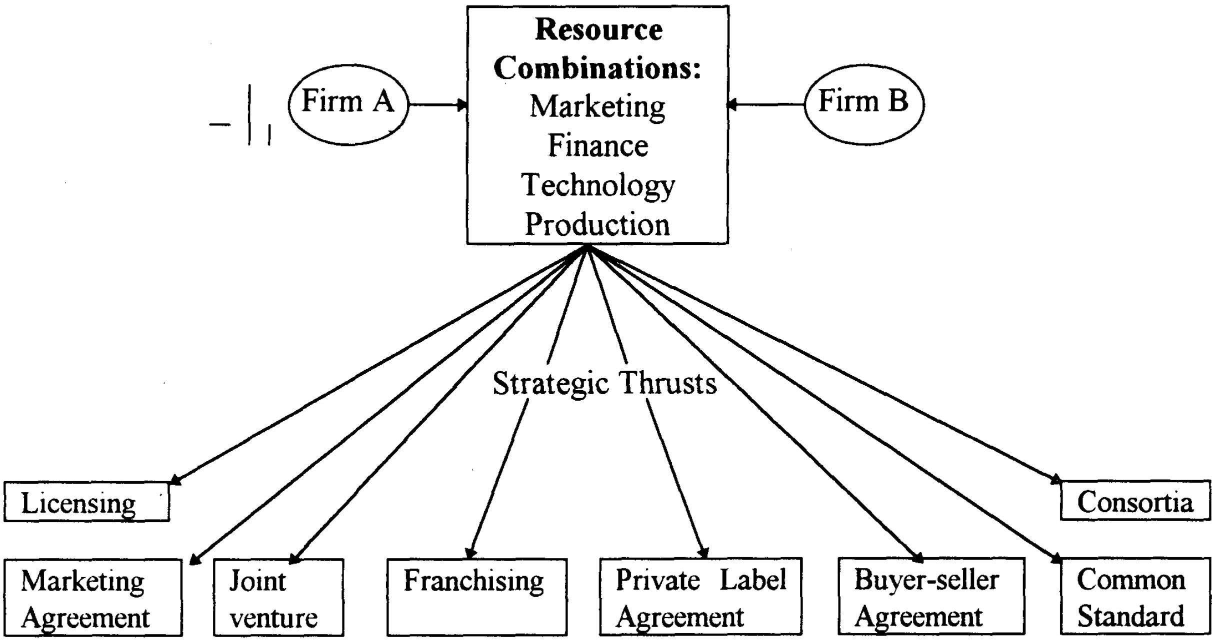
Figure 2.2 The reasons for forming strategic alliance



(Source : Long Range Planning, Vol. 26, 1993, p104)

production or technological resources in such a way as to serve the common objective of increasing market share. Thus, as can be seen from the description above, it seems that a strategic alliance is not just a simple contract to share management with others, but an important corporate relation for global companies to maximise their opportunity and to establish or reinforce competitive advantage in keener global competition, and that alliance arrangements between companies has been diversified since their business moved from domestic to international.

Figure 2.3 Basic Alliance Strategies



(Source : Long Range Planning, Vol. 18, No. 3, 1985, p77)

2.1.3 Advantages

Many competitive advantages for using strategic alliances in an international operation are recognised. Murray et al. (1993) identified three advantages; 1) size, 2) access and 3) control of options. Firstly, size advantage means that a company can easily obtain an advantage of economies of scales by increasing its capacity through the alliance, although it takes time to achieve it, and long term agreement between companies is normally required. Secondly, access advantages are independent of size and centre on the control of access to resources or customers, and this access can be based on superior "know-how" and ability, control of inputs or suppliers, and limits of entry to particular markets. Finally, regarding control of options, restriction on a competitor's option can take place in public policy, where corporations can influence legislation and regulation to their specific advantage. In Europe, where there are many onerous regulations on non-European firms, it might be a great advantage for non-European firms to form an alliance with European firms in terms of trading opportunity as they can avoid some regulations through its European partner.

Additionally, Nanda and Williamson (1995) identified two other advantages of strategic alliances. One advantage is that stakeholders stay engaged and committed at least during the alliance. It might be very dangerous for a company to sell a division in order to restructure its organisation for future survival. The reasons are that, firstly, skilled or high-calibre employees who belong to the division might leave for other opportunities as they may think their position will not be secure. Secondly, the limited possibility of future product enhancements, and the danger of being burdened with leftover inventory may discourage customers and retailers to purchases its products or services as technical support may not be provided. Thirdly, suppliers who consider termination of relationship may tighten their credit terms and relax their delivery and service standard. Fourthly, investors might withdraw their shares in the company as they feel that the business may decline. Thus, it is seen that the sudden taking of a decision will probably lead to serious problems for a company. To avoid these problems, the company can form a strategic alliance with another company. In doing so, the company may reinforce its core division, by obtaining partner's technologies or management skills, while it can dispose of another division by transferring it gradually to the partner. In addition, employees can learn new technology or skills and therefore they can easily move to other divisions. Customers, retailers and suppliers can also shift promptly to the partner's products or services, and to the distribution channel and supply chain. Investors tend to remain at the company as they believe that the company will be stable during the alliance and expect further growth after the alliance.

The other advantage Nanda and Williamson pointed out is that the unknown becomes known. When a business becomes globally based, a company is required to extend its operation and marketing abroad and has to face local business environment where such regulations and trade procedures are ambiguous. However, a strategic alliance allows the company to obtain an understanding of the business at its local site that is inaccessible to an outsider. In addition, the company is able to assess the true value of such intangible assets as brands, distribution networks, people, and systems. More importantly, the company is able to make key decisions quickly and efficiently on brand promotion, plant establishment and supplier rationalisation, and therefore considerable risks might be reduced by the partners help. These might be significant when the company will do business independently at the local site in the future.

2.1.4 Disadvantages

In spite of the fact that a strategic alliance leads to many advantages to a company, international alliances are often described as an inherently unstable organisational form. (Beamish and Inkpen, 1995) The life of a strategic alliance is normally rather short because it is vulnerable to market or technology change. It lasts only about six to eight years. A company forms an alliance with others in order to gain local knowledge, production skills or technology. However, when the company acquired its partner's strengths or when the partner's strengths became less useful because of sudden technology development or unexpected market change, the alliance tends to be terminated. Figure 2.4 shows types of a strategic alliance and current strategic alliances can be categorised in type A, which is "large firm - large firm" collaboration at international level, and in type D, which is "large firm - small firm" collaboration. In the case of type D, a small firm is generally in a weak position, while a large firm can take

Figure 2.4 Strategic Alliance Matrix

	Large Firm - Large Firm	Large Firm - Small Firm
National	A	B
Global	C	D

(Source : Nakamoto, Kokusaiteki Soshikikankei ni tsuite, 1996, p2)

advantage to control its weaker partner. Therefore, a large firm seems to unilaterally terminate the alliance when it thinks there is nothing to learn from its partner, even though the partner has not received sufficient benefit from the alliance. Ohmae (1989) stated that the problem of an international alliance is a large company behaves as it everywhere often does. That is, the large company ties up a small company and dose not allow it to expand its business into the areas which the large company wants to keep for itself. Thus, although relationships between companies on the basis of a strategic alliance seems to be equal, power relations between a large firm and a small one might be considerably different. Ohmae also stated that even if a company thinks that an alliance is going well and expects it will also go well in the future, its partner may not think that today's partner is the best or the most suitable tomorrow when technology, market or customers' needs are changed. Killing (1982) supported this argument that a manager will require the partner's managerial expertise, say, technology or market-related matters for a few years but will soon learn enough so that such help is no longer needed. Thus, forming a strategic alliance may not mean that both companies get equal benefit from it and, particularly, weaker companies tend to be still weak after an alliance.

Stafford (1994) pointed out two other problems concerning a strategic alliance. The first problem is that 'too much is expected too soon'. Companies who formed a strategic alliance tend to concentrate too much on short-term objectives and profit. However, specific knowledge or system such as Just-in-Time production system and *Kanban* system take a relatively long time to transfer and can not be achieved in the short term. Hence, concentration on short-term effect cripples long-term partner commitment. The second problem he suggested is that 'strategic goals between partners are ambiguous or conflict with each other'. It is rather difficult for companies to maintain one fixed corporate objective with their partners because of the continuous change of business environment. When its corporate objective becomes ambiguous, companies in an alliance start to have a different objective and, consequently, the vulnerability of the alliance increases. Thus, it can be said that a strategic alliance is very likely to collapse if a company fails to assess other companies and choose a right partner, and to share a consistent objective with the partner.

2.1.5 Factors for a Successful Strategic Alliance

In many cases, an alliance really means an eventual transfer of ownership. (Bleeke and Ernst, 1995) It is said that the median span for alliance is only about seven years, and nearly 80% of them ultimately terminate in a sale by one of the partners. Although a company may not expect that it will buy its partner or will be bought by the partner, it will probably be critical to consider whether or not an alliance might lead to a sale. The reasons are that such evaluation may help a company prevent disastrous partnerships and unanticipated sales of important business, help managers select corporate partners that can advance their organisation's long-term strategic plan, and help reveal opportunities in which an alliance may be used as a low-risk, low-cost option on a future acquisition. (Bleeke and Ernst, 1995)

Before forming an alliance, a company should consider the following three points in order to make an alliance successful. Firstly, initial strengths and weaknesses of the company and its partners should be identified. For example, it might be crucial to know which partners' strength may relatively affect the project, which partners may possess an advantage on the customers that will be targeted by the project and which partners may contribute most on the project in terms of investment. Understanding these factors might enable the company to know which partner will lead the alliance and will be an eventual owner. Secondly, it should be considered how strengths change over time. For example, a change of market and technology may lead to a shift of power relations. Bleeke and Ernst (1995) pointed out that although product and technology provider have most power at the beginning of an alliance, unless those products and technologies are proprietary and unique, power usually shifts to the party that controls distribution channels and customers. Clarifying each partner's role in the alliance may make the alliance go smoothly. Thirdly, possible competitive conflict should be anticipated. When direct competitors whose products and geographic position overlap try to form an alliance, conflict is inevitable. The conflict can be minimised when each partner brings distinctive qualities such as different geography, products and functional positions. Thus, a company should choose each potential partner carefully and assess whether their products or services will compete with its own ones in the same market in future. By understanding it, partners in the alliance may be able to avoid competing with each other and losing effectiveness of the alliance.

In addition, Brouthers et al. (1995) observed there are four considerations for successful international strategic alliances, which can be called The Four Cs of Strategic Alliances. (Figure 2.5) According to the four Cs, strategic alliances should be utilised when:

Figure 2.5 The 4 Cs of successful international strategic alliance

(Source : Long Range Planning, Vol. 28, No.3, p19)

1) *complementary skills* are offered by the partners;
2) *cooperative cultures* exist between the firms;
3) the firm has *compatible goals*; and
4) *commensurate levels of risk* are involved.

'Complementary skills' means that when a company chooses partners, it should consider not only the size of the financial contribution to the alliance, but also the skills, technologies and markets that the partners belong to. Both alliance partners should contribute equally and depend on each other. Moreover, both should create a formidable competitive advantage which can not be achieve independently. Murray and Mahon (1993) also agreed that both should receive mutual (but not necessarily equal) benefit from the alliance. Second, 'cooperative culture' means that both partners should recognise cultural difference when the alliance is formed between companies from different countries. Both should not try to control the alliance, but should possess a mutual sense of trust. Therefore, it might be accurate to say that strategic alliances work better when there is only a small difference in the size of both companies, if both companies are from different cultural background. Third, 'compatible goals' means that both companies' strategic goals should be achieved in a cooperative way. Lack of goal compatibility may create a climate in which the alliance will not succeed. Similarly, Murray and Mahon (1993) said that the existence of strategically significant goals is essential for success of strategic alliances and the benefit to be achieved should outweigh those derived from other means/actions. Fourth, 'commensurate level of risk' means that both should share risks equally for the alliance and its equality should be maintained. If one company obtains more from the alliance than its partners do, risks will no longer be in balance and the alliance may become unstable.

Thus, a company which plans to form a strategic alliance with others should carefully assess its own strengths and its partners' strengths and should evaluate the feasibility of the alliance from the long term perspective. Furthermore, 'alliance partners should note that alliances survive only as long as each company regards the other as its best partner and therefore each must take what steps it can to ensure that the other continues to need it'. (Financial times, 25 February, 1994)

2.2 Merger and Acquisition

2.2.1 Definition

When companies seek growth strategies, they choose one from a number of tactical options such as mergers or acquisitions, joint ventures, and internal product or business development. Mergers and acquisitions are often chosen as an efficient growth strategy. Porter (1986) observed that, through the mid-1980s, the annual number of mergers was around 2,500 and it is continuously increasing.

Although merger and acquisition both are sometimes considered as one and the same thing, Rue and Holland (1989) defined each separately. Their definitions are as follows:

> "An *acquisition* occurs when one company purchases the assets of another and absorbs them into its own operation. A *merger* occurs when two or more companies combine into one company. In an acquisition one company clearly acquires another ; in a merger neither participant acquires the other, but rather both companies merge together, combining operations."
>
> (Rue and Holland, 1989, p47)

Likewise, Wheelen and Hunger (1983) defined that "a *merger* is a transaction involving two or more corporations in which stock is exchanged, but from which only one corporation survives" and that "an *acquisition* is the purchase of a corporation that is completely absorbed as an operating subsidiary or division of the acquiring corporation." They also mentioned that mergers are usually between firms of somewhat similar size and are usually "friendly", while acquisitions are usually between firms of different sizes and can be either "friendly" or "unfriendly".

However, most managers might define simply both merger and acquisition as the most quickest way to enter the new market and the most effective way to avoid or eliminate many barriers to entry like patents, costly promotions, and organisational uncertainty from the strategic perspective. Furthermore, some may believe that merger and acquisition are a better strategy than an internal growth strategy when a company tries to enter into new, unrelated businesses. Thus, it can be seen that merger and acquisition are not just a way to make a company bigger, but a significant strategy when a company firms its competitive position in the existing market and diversifies its business into new markets.

Figure 2.6 Type of merger

Type of merger	Advantages	Disadvantages
Absorption of a competitor	Reduces competition	Emerges organisational conflict
Absorption of a vertically related organisation	Reduces uncertainty among organisation vertically related to each other	Increases costs and dependency on a single industry
Absorption of an organisation operating in another area	Reduces dependence on one area	Increases uncertainty and risk

2.2.2 Why Merger ans Acquisition ?

According to Pfeffer (cited in Quinn et al., 1988), there are three reasons an organisation may seek merger; which are, first, to reduce competition by absorbing an important competitor organisation; second, to manage interdependence with either sources of input or purchasers of output by absorbing them; and third, to diversify operations and thereby lessen dependence on the present organisations with which it exchanges. (Figure 2.6) Similarly, Rue and Holland (1989) stated that the reason for merging with or acquiring another company includes improving or maintaining competitive position in a particular business in order to enter new markets or acquire new products rapidly, to improve financial position, or to avoid a takeover. In the case of the merger between Natinale Nedeland, the insurance company, and NMB Postbank, they reached the agreement to merge in order to keep up with rapid changes of financial services. In financial services, customers are becoming more demanding, financial institutions are competing more vigorously for customers, and they are also looking ahead to the challenge and opportunities of the single European market. Moreover, the demands of customers are becoming more complex and more international. Facing these facts, they thought it was quite difficult for a single organisation to satisfy those customers and to maintain its competitive position in the dynamic market. Hence, they found many advantages and values for a merger rather than staying alone and agreed that it is essential to establish a bigger and stronger organisation, with a clear identity of purpose and a scale and range of resources that can answer customers' needs, not only in Holland but in Europe and beyond, and can continue to grow through the 1990s. Thus, it can be said that many companies are attracted by "merger and acquisition" because it enables them to accomplish strategic objectives quickly and effectively. At the same time, it tends to attract executives who enjoy the challenge of negotiation and deal-making. (Rue and Holland, 1989)

2.2.3 Advantages

Although it is said that a merger includes high risk and most companies have failed to manage it, sometimes it is an appropriate strategy and a successful merger brings a company considerable advantages against its competitors. These advantages can be divided into two, external advantage and internal advantage.

Regarding external advantages, a merger makes it easier for a company to enter new markets or new business, or to improve its competitive position in existing businesses. An acquiring company can double its size and also quickly obtain technology, and the supply and distribution chain of an acquired company. Hence, an acquiring company can easily enter the market where an acquired company has served. More importantly, an acquiring company may be able to achieve economies of scales and it will be a great advantage for an acquiring company not only in the existing market but also in the new market it will enter.

Internal advantages which are observed by Harrison (1987) are 1) increase in earning, 2) reduction of dependence on one area, 3) investment of excess cash and 4) improvement of management. Firstly, an acquiring company can increase its sales and earning by acquiring, particularly, a company which has a strong record of earning growth and therefore earning per share will be improved. Secondly, if a company's business is highly cyclical and is easily influenced by seasonal factors or power of customers or suppliers, diversification by merger may reduce risk in the case of shrinkage of the market the company involves in, and give an opportunity for further growth. Thirdly, in a mature market, it becomes difficult to find the way to profitably invest excess cash and a company will become inefficient because its rate of turnover is increasing. However, development of a new business by merger may reduce cash accumulated in the company as new investment will be required for it and, consequently, rate of turnover will improve and the company will, therefore, become efficient. Finally, a merger may improve management. Lubatkin (cited in Rue and Holland, 1989) stated that two operating units can be run more efficiently (i.e., with lower costs) and/or more effectively (i.e., with a more appropriate allocation of scarce resources given environmental constraints) together than apart. Thus, the effective use of merger may be crucial for improvement of a company's competitive position and its growth in the future.

2.2.4 Disacvantages

The major disadvantage of a merger is financial risk. When a company merges with another company, its costs for acquisition are extreme in spite of the fact that it is not guaranteed whether or not the company will develop after the merger. Harrison (1987) described the financial risk of merger.

> "Interest expenses are only one part of the cost of new debt that is usually necessary to finance a large merger. New debt increases the leverage of the marginal firms, thus increasing financial risk. In periods of industrial or economic decline, high financial leverage increases the probability of default and/or bankruptcy." (Harrison, 1987, p79)

Although the acquiring of suppliers or customers group may reinforce vertical integration of a company and reduce the company's uncertainty by bringing critical contingencies within the boundaries of the organisation, it is said that strong vertical integration leads to high costs and creates a larger organisation which is increasingly tied to a single industry. (Quinn et al., 1988:326) On the contrary, while absorption of a company operating in another area will probably give an opportunity for the acquiring company to diversify its business into a new industry, it does not reduce the company's uncertainty, but increase its operational risk. Moreover, acquisition of a competitor seems to be a good way to reduce competition, but it tends to cause strong conflict between organisations because of the difference of each corporate culture and it is, therefore, very difficult for the acquiring company to transfer its management style to the acquired one.

Considering these advantages and disadvantages, it seems that a merger might offer great benefits to the acquiring company, but it can be very expensive and can cause more problems than it solves. Rue and Holland (1989) stated that a successful merger requires a strategic rationale, careful evaluation and analysis of potential candidate, negotiation of price and other transaction details, and a transaction plan. Furthermore, Harrison (1987) suggested that a merger should usually be considered as a last resort when all of the strategic alternatives have been exhausted.

Chapter Three

The Strategic Alliance in the Automobile Industry Honda and Rover

Alliances are held together by fear, not by love.
Harold Macmillan (1959)

The strategic alliance between Honda and Rover lasted 15 years since the relationship started in 1979. In the motor industry, it was unusual that the equal relationship between car companies lasted so long time without divorce or merger.

This chapter explores why a strategic alliance was formed between Honda and Rover and how it affected each company. Then, the reasons why Honda and Rover agreed to form an alliance, the company's situation at the time and the effect of the alliance on both companies will be mainly focused.

3.1 Historical View of the Joint Business-Rover and Honda

The relationship between Honda and Rover started on 27th December 1979. After the oil crisis, British motor industry, which failed to rationalise its production and management, was continuing to decline and British Leyland (BL), which was the only British automaker, faced keen competition with foreign producers such as American, European and Japanese. Hence, BL desperately needed a partnership in order to improve its low productivity and increase development costs for new products. BL sought the way not in Europe, but in Far-East, Japan, and set up a joint business with Honda. Honda was already well-known for its development of its high-efficient engine and it shared with other Japanese companies a more advanced approach to manufacturing technology, while also improving its expertise in areas like suspension and body engineering. (Bhaskar, 1988:61) Thus, this joint business with Honda was meaningful for British Leyland, who lacked sophisticated technology and rationalised manufacturing.

History of the collaboration between Honda and Rover is as follows.

1979	May	Rover/Honda collaboration agreement.
	December	Agreement to build Honda Ballade as Triumph Acclaim at Cowley.
1981	July	First Acclaims sold in the UK.
1983	April	Rover 800 joint development agreement.
1984	April	Rover 800 joint production agreement.
	June	First Rover 200 series sold in the UK.
1985	February	Honda UK Manufacturing(HUM) set up.
1986	July	First Rover 800 series sold in the UK.
	October	First Legend sold in the UK.
1988	August	Rover sold to British Aerospace.
1989	July	Outline of cross shareholding agreed.
	August	Rover 200 production starts in the UK.
	October	Honda Motor Europe set up in the UK.
1990	April	Cross shareholding deal signed
1991	November	New wide-ranging memorandum of understanding signed.
1992	October	HUM starts European production of Accord.
1993	January	Rover 600 production starts at Cowley.
	June	Sales deal for Rover 4WD vehicle in Japan.
	November	Honda Crossover/Land Rover Discovery sales start.

1994 January BAe sells Rover stake to BMW.

(Source : The Guardian, 22 February 1994)

3.2 Purpose and Benefit from the Rover's perspective

In the situation of the business depression of BL, Honda's approach for joint venture was a great opportunity for the company. There were some reasons why British Leyland did not want to form an alliance with a European or American company. Firstly, there was an opportunity for British Leyland to associate with Renault, but it did not materialise. Renault was very attractive not only in its well-structured operations, but also in its development of advanced models. However, Michael Edwarde, who was a Chief Executive Officer of BL, thought after the meeting with Renault that its strongly nationalistic attitude would eventually leave BL no more than a British satellite of a French firm and Renault was not willing to market BL's cars to other EEC countries. (Edwarde, 1983:189) Therefore, he thought that collaboration with Renault would not lead to a favourable outcome for BL. Secondly, the association with GM was also not realised. When the managing director of Vauxhall in the UK, which is a subsidiary of GM, asked about the plan "Gemini", which was the plan to exchange British Leyland's production capacity for GM engineering resources, Edwarde was very attracted by the plan. However, the fact that this plan was not supported by GM headquarters was detected and the plan collapsed. After the collapse, Edwarde stated that BL would not form an alliance with European car producers.

> "There would be problems within Europe because it is difficult to collaborate with a direct competitor in what is one big market. The dangers of a link with a multinational - even if it were interested - would be that BL would become an offshore assembly operation."
>
> (Edwarde : cited in Pilkington, 1996:73)

Thus, the emergence of Honda as a partner seemed preferable for BL to reshape its organisation. Edwarde (1983:194) also stated that Honda's size, their engineering skill, their remarkable track record, and a number of other key factors, made Honda the most desirable partner.

Pilkington (1996:73) pointed out five main factors which led Rover to the collaboration; first, political pressures in the form of EU trade barriers and the UK government's dwindling financial support for Rover; the second, Rover's lack of capital following its record of failure; the third, the lack of design and organisational capability in Rover following the formation and subsequent rationalisation of BL; the fourth, the consumer perceptions of Rover products which demanded a fresh approach to design; and finally, the threat of Japanese manufacturers arriving in the UK market, which meant it

Table 3.1 Comparison of Rover and Honda at the Start of the Relationship

Fact of Organisation	Honda	BL
Model range complexity	2	16
Number of Plants	2	30
Engineering strength	Power train	Interior/Suspension
Ownership	Shareholders	Government
Model strengths	Small Sector	Executive Sector
Other business interests	Motor cycle	Trucks, buses, four-wheel drive car
Management style	Practical/technical	Bureaucratic/historical

(Source : Transforming Rover : Renewal Against the odds 1981-1994, p74)

could not survive as a car producer. Pilkington (1996:72) also pointed out the necessity for collaboration for BL in 1980. He maintained that the relationship with another company was the only way to revitalise its product range quickly and cheaply and to cope with the rapidly waning enthusiasm of the British government for any further support for the company.

Although BL and Honda were both car manufacturers, there were some differences between them. (See Table 3.1 for the summery of the comparison) Firstly, BL's model range was 16, whilst Honda's was just 2. Secondly, BL had 30 plants which seemed excessive, whilst Honda had only 2 plants, but they were similar and more rationalised. Thirdly, BL was owned by the government, but Honda was a privatised company. Finally, Honda's other production was the motor cycle and BL's was tracks, buses and a four-wheel drive car. Considering these points it can be said that both could not be a direct competitor with each other. Moreover, as some similarities, firstly, both were free of complex collaborative commitments and ,secondly, were leaders in front-wheel-drive car and they could, therefore, carry research and development jointly in terms of technology. (Edwarde, 1983:194)

Although Honda and Rover seemingly took a form of joint development, Rover was highly dependent on Honda. In 1984, Rover bought the production equipment from Honda and, since Honda built an assembly plant at Honda of UK Manufacturing (HUM) in Swindon in 1990, Rover's dependency on Honda's product and production technology was getting stronger. Furthermore, during early 1990s, Rover started to adopt Japanese personnel system and before it started production for new model, 600 series, at Cowley plant, it dispatched its engineers and floor managers to the Honda's plant in America for training. (Yuzawa et al., 1996:181)

Thus, in the 1990s, collaboration with Honda was significant and meaningful for Rover to overcome the depression of the company and reconstruct the British motor industry. Rhys (1994) also stated that Rover has learned so much from Honda about efficient, long-term links with suppliers, factory operation, people management and building cars properly.

3.3 Purpose and Benefit from the Honda's perspective

Purpose for the collaboration

Although it has been described above how important it was for Rover to collaborate with Honda during the 1980s, from Honda's perspective, this collaboration was not so important as the European market was not very significant for it compared to Japan and North America. In addition, Honda had concentrated during the 1970s and 1980s on promotion in the US market rather than in the European one (See Table 3.2) and it was only ranked fifth among other Japanese car producers in Europe. (Mair, 1994:226)

Considering these facts, it can be seen why Honda did not want to build an assembly plant as it had in the US. As Honda did not seem keen on promotion in Europe, it probably wanted to avoid investing a large amount of money for building an assemble plant and a suitable supply base. Therefore, the collaborative business with Rover was also favourable for Honda and was a greater chance to enter the European car market immediately.

However, it should be noted that Honda was not looking at the UK market, but the German, even though its manufacturing was located in the UK. According to Mair (1994), Honda engineers view Mercedes, BMW, Audi, and Porsche as its target in terms of product quality and product concepts and the central Honda R&D subsidiary in Europe is, therefore, located at Frankfurt in Germany, not at Swindon in the UK. He also pointed out that this is the reason why Honda's first British-produced Accord models were left-hand-drive, exported straight to Germany.

Benefit from the collaboration

It can be said that the main advantage for Honda from the collaboration was to gain access to the European market easily through an indirect route at a time of highly restrictive import controls. Unlike Toyota and Nissan who built an assembly plant in Europe and invested a large amount of money for the European operation, Honda could build cars in the Rover's plant and promote them with minimum costs.

There were some other advantages of the collaboration for Honda. Firstly, it could gain design expertise in the previously European-led quality and executive cars sectors and also in the particular field of suspension technology. (Pilkington. 1994:83) Secondly, in addition to the sales of the cars, it also provided variety of components like an engine and a gearbox for the Rover's products. Therefore, it could increase the profit not only from the sales of the cars, but also from the sales of the components. Thirdly, it could learn about the characteristic of European suppliers and also educate them to be a suitable

Table 3.2 Honda's European Sales are Minor Compared to Sales in Japan and North America (1990)

Market	Honda, sales, Y bn, % in brackets	Honda sales, units, % in brackets	Honda's share of market (%)
Japan	1,110 (32)	669,000 (35)	8.7
North America	1,849 (53)	952,000 (50)	6.2*
Europe	370 (11)	173,000 (9)	1.2**
Others	146 (4)	121,000 (6)	
Total	3,476 (100)	1,915,000 (100)	

Notes : * United States
** Western Europe
Sales figure in first two columns for the fiscal year April 1990 - March 1991, as Honda reports them. Europe is defined widely by Honda, referring to its regional marketing division.

(Source : Mair, A., Honda's Global Local Corporation, 1994:227)

suppliers for the Japanese operation. It was very important for Honda to establish a closer relationship with the suppliers before Honda's own European production began. It was also beneficial for the suppliers as they could improve their performance by learning about the Japanese supply system which seemed more sophisticated than the European one. Finally, Honda could learn how to do business in Europe. Mair (1994) stated that multiple linkage between Honda and Rover personnel over the decade have provided Honda with an ongoing lesson in how business is normally done in Europe. Thus, it can be seen that Rover was very important for Honda's European operation and Honda, who was a new car manufacturer, learned a great deal from Rover, who has a long history as a car manufacturer.

However, why did Honda choose Rover as a partner, not Renault, PSA or Fiat? The critical reason seems power relation between both companies. It was obvious that Honda was in a stronger position than Rover in terms of economy and Honda could, therefore, make Rover accept Honda's requests. If Honda had an alliance with a larger company, its business in Europe would have been restricted by the company. Therefore, Honda preferred a weaker company as a partner. Mair (1994) also said that Rover's very weakness made it an ideal partner for Honda.

Chapter Four

Merger and Acquisision in the Automobile Industry BMW and Rover

We are, after all, all business man.
BMW Chairman (1994)

"Merger and Acquisition (M&A)" is a common occurrence in the current business world. In the motor industry, many car companies have merged with larger companies since the industry appeared. In 1994, BMW merged with Rover, which was the last British-owned major car producer, and this deal surprised not only Honda but also other car producers all over the world. This deal was so sudden and negotiation was completed between BMW and BAe ignoring Rover and its closest partner, Honda.

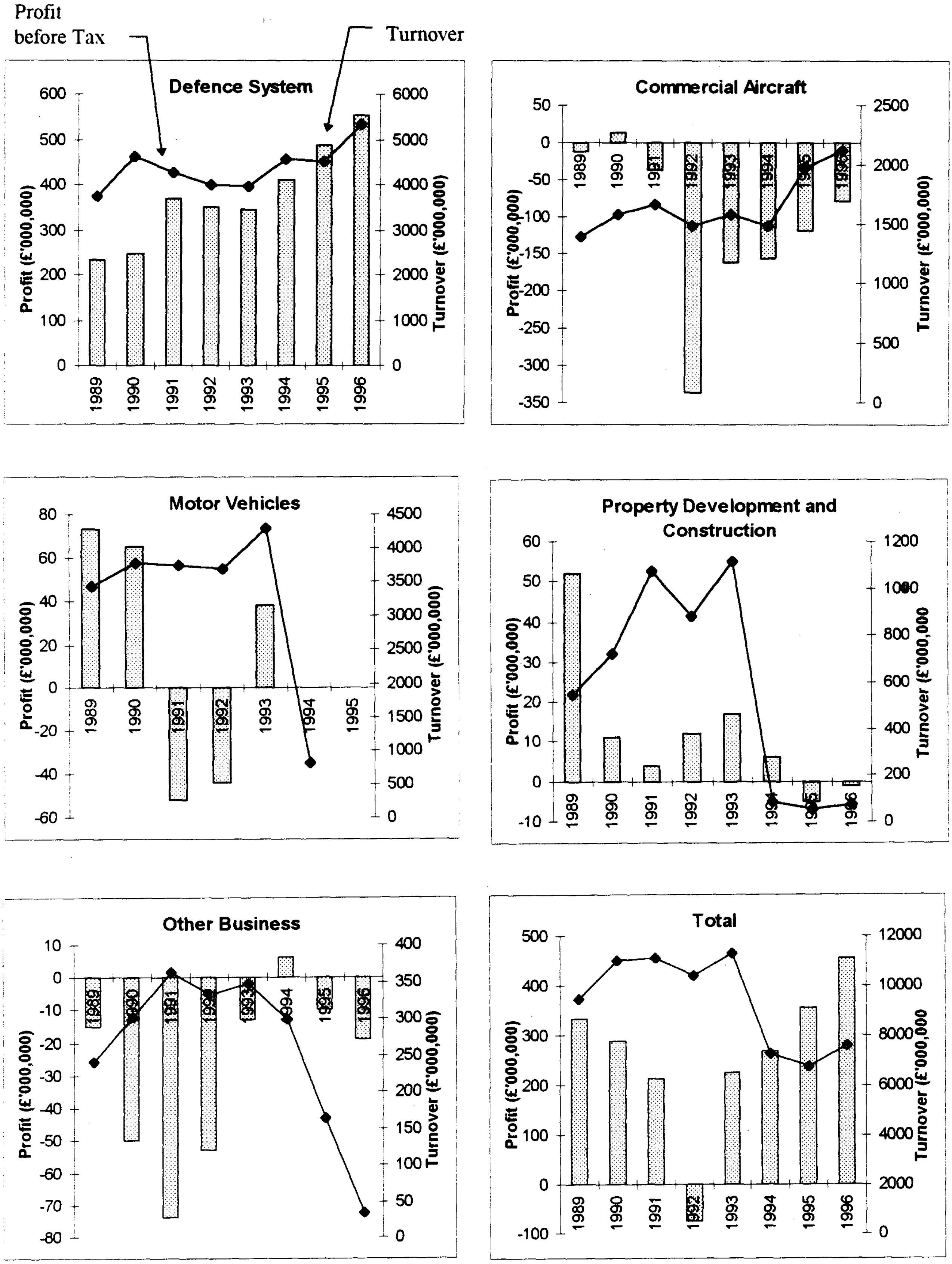
This chapter looks mainly at M&A between BMW and Rover and how it affected Honda, who had a strategic alliance with Rover for 15 years. BAe's financial situation, which led the disposal of Rover, BMW's purpose and benefit from the takeover, and Honda's reaction towards the BMW deal will be also discussed.

4.1 Situation of British Aerospace

In January 1994, Rover, the last UK-owned volume car company, was sold to BMW by British Aerospace (BAe). BAe did not inform Honda, Rover's partner for fifteen years, about BMW's action and did not tell the workers working for Rover. It surprised not only Honda and workers in Rover, but also other car producers in the world as it was so sudden. What was the reason BAe sold Rover? Why did not BAe sell Rover to its partner, Honda?

Firstly, regarding the financial condition of BAe, it can be seen from Figure 4.1, there are many businesses in the BAe and most of them have not been profitable. From the early 1990s, its profit started to decline substantially and its income statement showed a loss of £75 million in 1992. Particularly, the Commercial Aircraft business has made losses since 1991. Thus, it can be said that one of reasons to sell Rover was to ease its own short-term financing problems. Secondly, BAe stated that the decision to sell Rover was part of BAe's strategy. According to Andy Wrathall, spokesman for BAe, BAe is putting more emphasis on prime contracting defence business and the value-added nature of the business is improving, despite a declining market. (Financial Times, 1 March 1994) Additionally, increasing competition in aerospace and defence industry seemed to compel BAe to dispose of its automotive subsidiary. Hence, BAe needed a company who could buy Rover immediately and BMW was the one who could deal. Finally, the reason why BAe did not sell to Honda is that Honda did not want to take 100% share of Rover as it

Figure 4.1 Turnover and Profit before Tax of British Aerospace



was the last British-owned car producer and Honda wanted to leave Rover as a "British" car producer, not "Japanese". Therefore, although BAe asked several times Honda to take 100% of Rover's share, Honda refused its offer.

Thus, there were several reasons for BAe to dispose of Rover. However, it should be noted that Rover is turning out to be a profitable company since the collaboration with Honda started. Moreover, the UK car market was the only one which showed growth in the European car market in 1993. (Table 4.1) Considering this point, it seems that BAe only cared about short-term profit, but not long-term profit. Brummer (1994) commented that the tough situation for BAe would not be improved so easily, even though it received £800 million from the sales of Rover, because of the following reasons. Firstly, its defence business remain under threat from budgetary cuts around the world; secondly, its missile business is under permanent siege from General Electric Company (GEC); thirdly, sharing the costs of its regional jets' business with Taiwan has been foiled; fourthly, it remains only a minor factor in the civil aviation market; and finally, all of these businesses require huge amounts of research and development capital to keep them technologically ahead. (Financial Times, 17 January 1994) He also argued that it would have been better from the long term perspective to sell off defence and aviation business and retain Rover with its better market prospects.

It can be seen from the discussion above that BAe's decision was not sensible considering the future growth of its business. Moreover, its unilateral decision, ignoring Honda, may cause serious problems to Anglo-Japanese ties.

4.2 BMW's Purpose and Benefit for the Acquisition of Rover

Purpose

As can be seen from Table 4.1, West European car producers suffered steep annual declines in the European market. Production has been reduced drastically and car production has declined to result in losses of tens of thousands of jobs. (Financial Times, 17 January 1994) Particularly, luxury car specialists such as Mercedes-Benz and BMW, who have been produced only large and luxury cars, have faced the crisis of extreme market shrinkage in the luxury car segment and of a decline of larger car sales. Therefore, these companies had to expand their product range in order to survive in keen competition. Mercedes-Benz has already decided to produce its own compact car, A-class, which targets the small car segment rather than the luxury car segment. Moreover, it planned to produce the Mercedes M-class off-roader, which is a smaller and four-wheel drive car, for the Recreational Vehicle (RV) segment, which includes minivans, sport/utilities (SUVs) and station wagons. BMW decided to maintain its product range without any expansion. Instead, BMW acquired Rover and compact, small, medium and four-wheel drive car segments are concentrated on by Rover and larger and luxury car segments are concentrated on by BMW. In doing so, BMW can maintain its luxury brand image and also save a large amount of money for costs of new car development. Mr. Pischetsrieder, BMW management board chairman, stated that BMW will not build a small car for sale

Table 4.1 West European New Car Registration January-December 1993

	Volume (Unit)	Volume Change (%)	Share (%) Jan - Dec 93	Share (%) Jan - Dec 92
TOTAL MARKET	11,449,000	-15.2	100.0	100.0
MANUFACTURERS:				
Volkswagen group	1,888,000	-20.1	16.5	17.5
-Volkswagen	1,245,000	-20.5	10.9	11.6
-Audi	318,000	-23.2	2.8	3.1
-Seat	273,000	-17.4	2.4	2.4
-Skoda*	51,000	-0.1	0.4	0.4
General Motors****	1,493,000	-11.4	13.0	12.5
-Opel/Vauxhall	1,436,000	-11.0	12.5	12.0
-Saab**	42,000	-18.1	0.4	0.4
PSA Peugeot Citroen	1,402,000	-14.7	12.2	12.2
-Peugeot	848,000	-14.9	7.4	7.4
-Citroen	554,000	-14.3	4.8	4.8
Ford*****	1,315,000	-13.4	11.5	11.3
-Ford Europe	1,304,000	-13.5	11.4	11.2
-Jaguar	11,000	+1.2	0.1	0.1
Fiat********	10272,000	-20.6	11.1	11.9
-Fiat	955,000	-19.9	8.3	8.8
-Lancia	179,000	-22.4	1.6	1.7
-Alfa Romeo	125,000	-24.7	1.1	1.2
Renault*****	1,201,000	-16.2	10.5	10.6
Nissan	397,000	-9.5	3.5	3.2
BMW	370,000	-16.4	3.2	3.3
Rover	**361,000**	**+8.9**	**3.2**	**2.5**
Mercedes-Benz	354,000	-13.5	3.1	3.0
Toyota	318,000	-5.8	2.8	2.5
Mazda	194,000	-28.0	1.7	2.0
Volvo*****	171,000	-14.7	1.5	1.5
Honda***	162,000	-7.8	1.4	1.3
Mitsubishi	140,000	-13.1	1.2	1.2
Total Japanese	1,388,000	-12.9	12.1	11.8
Markets :				
Germany	3,192,000	-18.8	27.9	29.1
Italy	1,890,000	-20.4	16.5	17.6
United Kingdom	**1,778,000**	**+11.6**	**15.5**	**11.8**
France	1,721,000	-18.3	15.0	15.6
Spain	744,000	-24.1	6.5	7.3

* VW holds 31 per cent and management control of Skoda.

**** Include cars imported from US and sold in Western Europe.

** GM holds 50 per cent and management control of Saab Automobile.

***** Renault and Volvo are linked through minority cross-shareholdings.

******** Fiat group includes Lancia, Alfa Romeo, Innocenti, Ferrari and Maserati.

*** Honda holds a 20 per cent stake in Rover vehicle operations.

(Source : Financial Times, 17 January, 1994) under the BMW badge and Rover in the UK and the Rover brand will become its centre for small car development. In addition, he said that a small BMW would not comply with the brand core BMW image, that it has worked 20 years to achieve. (Financial Times, 1 February 1994) Therefore, BMW criticises Mercedes-Benz's decision to widen its product range to "downmarket" and asserts that Mercedes-Benz may not be able to keep its brand image as a luxury/executive car producer. It seems that this is the one of reasons for BMW to acquire Rover.

The other reason for the acquisition might be to enter the RV market which is rapidly growing, particularly in the US and Japan through Land Rover. In the US, 38 new vehicles including those with major changes were introduced in 1996 and 14 of them were pick ups, vans or SUVs. (Ward's Automotive Yearbook, 1996:128) In Japan, RV market continued to grow rapidly in 1995 and RVs accounted for 272,000 units, marketing a 24% jump from 1994 and 4.7% market share increase to 28.8%. (Ward's Automotive Yearbook, 1996:64) Therefore, BMW can expect great sales expansion of Land Rover four-wheel drive vehicle in the US and Japan.

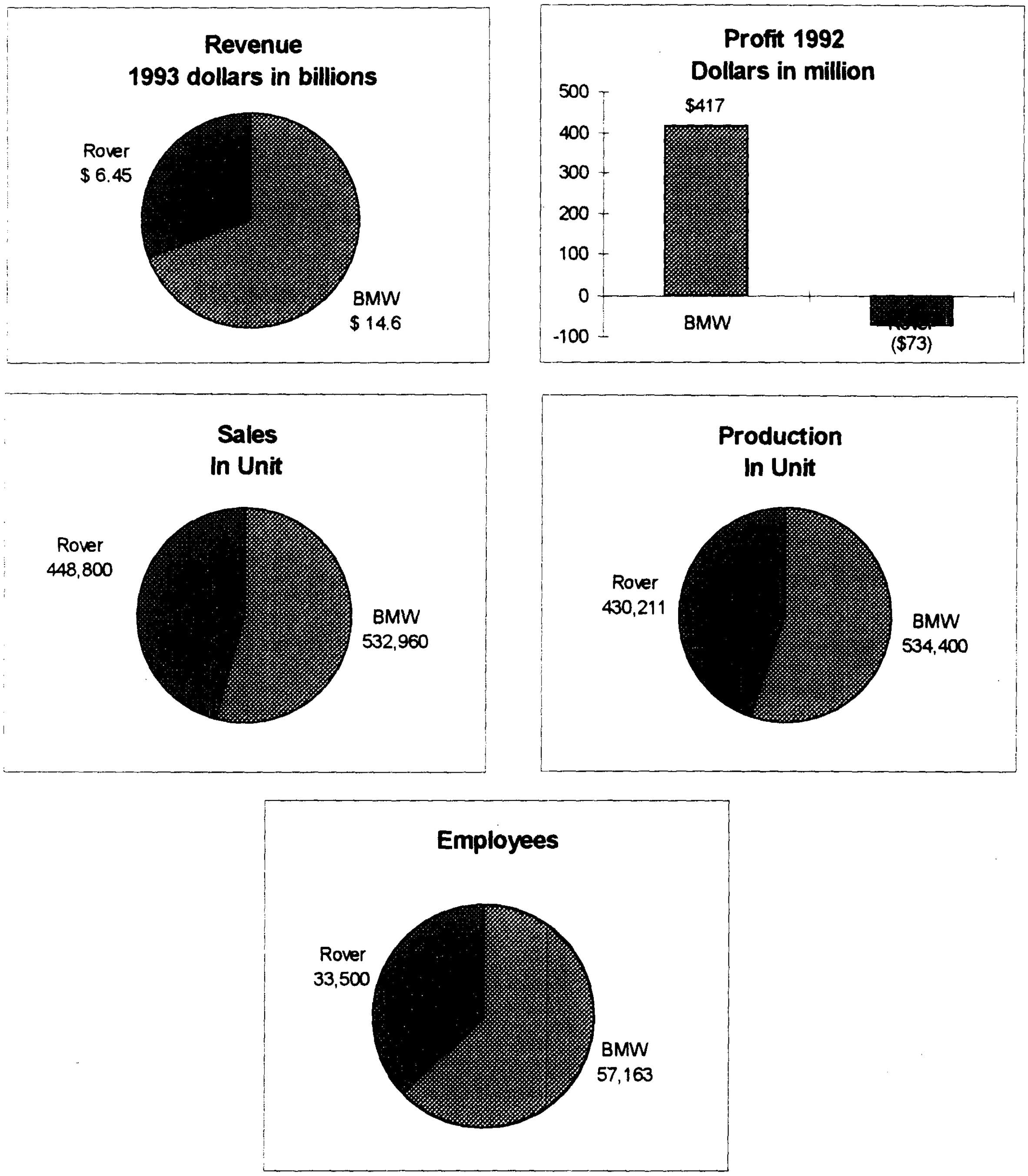
<u>Benefit</u>

The biggest advantage BMW gained from the acquisition against its rival, Mercedes-Benz, might be costs for development of a small-sized car and RV. It will probably be very costly to produce a new concept car and time consuming, although Mercedes-Benz has decided to expand its business to the downmarket. In addition, it might be dangerous for a luxury/executive car producer to enter the downmarket as they may have to compete with their competitors with price and may damage their luxury image in consequence of price competition. Furthermore, it seems essential for the companies in the "downmarket" to achieve low cost production by the economies of scales as they have to provide sufficient numbers of cars cheaply. Therefore, it might be very difficult for the luxury car producers who have not acquired economies of scales to compete with mass producers. Thus, Mercedes-Benz, who will promote its own small car and RV, may have to deal with these problems in the future.

Unlike Mercedes-Benz, BMW quickly entered the small-sized car and RV market by acquiring Rover. BMW almost doubled in size overnight (Figure 4.2) and became Europe's seventh-biggest automaker, with sales of some 1 million cars and trucks a year. (Automotive News, 7 February 1994) As a direct effect of the acquisition, firstly, BMW could expand its product range from the present 4 models to 14 models including Land Rover. (See Table 4.2) Hence, it became a "full line" producer, which makes a full range of cars from mini and super-minis to large executive cars, without lowering its brand image as a luxury/executive car producer. Secondly, expansion of capacity may lead to economies of scale, although they will not be achieved in short term. If it is achieved, it will be a great competitive advantage for BMW against its competitors not only in the small/medium car market, but also in the large/luxury car market. Thirdly, BMW can easily gain access to front-wheel-drive technology Rover has developed. All of BMWs are rear-wheel-drive and therefore acquiring front-wheel-drive technology will probably give some distinctive advantage on a new and existing product development. Fourthly,

Figure 4.2 The New, bigger BMW

How the combined BMW/Rover measures up
in terms of performance in 1992.



(Source : Automotive News, 7 February, 1994)

Table 4.2 BMW and Rover Automobile Range in 1994

	BMW	Rover
Luxury Large	BMW 7 series	-
Large	BMW 5 series	Rover 800
Middle	BMW 3 series	Rover 400/600
Small	-	Rover 200
Compact	-	Rover 100, Mini
Luxury Sports	BMW 8 series	-
Compact Sports	-	MG
Sporty/Utility	-	Defender, Discovery, Range Rover

acquisition of Land-Rover may offer great benefit to BMW. The sales of Land Rover have been steadily increasing. In 1993, it produced approximately 71,000 vehicles and it was the biggest production figure in its history. (Business Age, 1 March 1994) Moreover, recent continuous market expansion for RVs in the US and Japan might stimulate its sales growth. Finally, BMW may be interested in the production of BMWs in the UK as production costs in the UK are relatively cheap compared with Germany. Although BMW maintained that no BMWs would be produced in the UK, there is a capacity to produce BMWs in the Rover factory and BMW might shift its production to the UK if competition gets keener in the future.

Thus, it seems that BMW gained much benefit from the acquisition of Rover. However, there are also some problems BMW has to deal with. Firstly, it might be over capacity for BMW to own several plants just in Europe, not in other regions, in terms of global strategy. Secondly, large investment for R&D and marketing on the Rover products might be needed in addition to the investment on BMWs. It might be costly from the long term perspective. Finally, it may be difficult for a specialist producer who targets normally the niche market to deal with several markets at once in terms of management. Hence, BMW might fail to compete with American and Japanese volume producers. The future success of BMW may depend on how quickly and how efficiently these problems can be solved.

4.3 Effect of the Acquisition on Rover

The takeover of Rover was decided between BMW and BAe without informing Rover about it in advance. It surprised all workers employed by Rover when they knew their owner had changed overnight. At the same time, they were worried about a large scale restructuring of Rover and the reduction of employment which often occurs. From the management perspective, this sudden takeover was also problematic. Rover has developed its products with Honda since the alliance started and has depended greatly on Honda's production system, technology and personnel skills. Even though the

Interview with staff at Rover company

"What did you think about Honda as a partner?"

Both answered that Honda was a very nice partner and helpful.

"Do you think Rover cars has become too "Japanese" in terms of design?

Both answered "no".

"What do you think about the merger by BMW?"

One answered it would be good for the future growth, while the other answered he was worried about Rover's future.

"What do you think about the collapse of relationship with Honda?"

One answered that Rover will be able to learn different technology and management skills from BMW, although it was a pity to finish the collaboration with Honda. However, the other answered that most models of Rovers have been developed with Honda and this collapse will, therefore, affect Rover's future product development.

"Merger often lead radical change of the organisation. Do you feel concern about a change that may happen certain employment prospects of Rover?"

One answered that Rover's employment would be secure as BMW would support Rover sufficiently, whilst the other answered Rover's employment would be unstable as it depended on the financial situation of BMW, although it would support Rover.

"How do you think sales of Rover car will be affected by the merger from the long term perspective?"

One answered it would increase under the BMW support, while the other answered it would decrease if Rover ceased collaborative product development with Honda.

"How do you think about British Aerospace(BAe)'s decision?"

Both thinks Rover was sold cheaply and BAe did not care about Rover's future, but their profit.

(Research at Cowley in Oxford : 30 July 1997) collaboration with Honda has not affected Rover's profits yet, its production has rationalised efficiently as compared with before. Hence, Rover expected Honda would be a key for further growth in the future and the collaboration would last longer. However, when BMW's takeover was realised, the collaboration with Honda was terminated and Rover's future became uncertain.

From the result of research above, which was made at the Rover factory, Cowley, in Oxford and which was answered by two staff working at Rover, it can be seen how employees of Rover feel about the takeover and the collapse of the alliance with Honda. Employees at Rover had a very good impression of Honda and they have been proud of Rovers as a "British" car, even though it has been said that Rovers became too "Japanese". Similarly, they showed a negative attitude to the BAe's decision. However, regarding BMW, it can be seen that there is some confusion among employees. Some might expect BMW will positively affect Rover, but some might believe that BMW will use Rover for its own strategy rather than Rover's growth.

It seems that there are no advantages for Rover in being acquired by BMW. However, Rover may also benefit from the takeover in the following points. Firstly, Rover will gain access to the technical and manufacturing support of BMW; a certainty of ownership and the opportunity to expand its product range through new product development. (Marketing Week, 4 February 1994) Secondly, BMW's strong reputation in the US might be an important factor for Rover to increase its sales in the US market. Wolfgung Reitzle, BMW's head of development, also stated that the access to the BMW dealer network will be a big, big advantage for Rover. (Automotive News, 7 February 1994) Thirdly, BMW's strong distribution network will probably help Rover to promote Land Rovers in the US and Europe. RVs/SUVs are very popular, particularly in the US and Japan, and Land Rover's sales are steadily increasing in Japan. However, it is seriously under-distributed in Europe and the US because of Rover's poor distribution network. Therefore, the efficient promotion of Land Rovers through BMW's distribution network may lead to a sales expansion of Land Rover in these countries. Thus, it can be said that Rover gains many advantages from the takeover as well as BMW and BMW will give Rover a significant competitive edge for intensifying global competition.

4.4 Reactio of Honda towards the Acquisition of Rover by BMW

Honda's reaction towards the acquisition was hostile. Honda was surprised and disappointed by the deal, because it took a long time for Honda to cultivate the kind of close inter-corporate ties across national boundaries and it did not expect the collaboration would be broken up so easily. Nobuhiko Kawamoto, Honda's chairman, criticised the BMW deal as "completely negating the long efforts between Honda and Rover . . . to make Rover a British company with its own brand identity". (The Independent on Sunday, 6 February 1994) More importantly, Honda is concerned about how much Honda's technology BMW gets through Rover. Honda and BMW are

Table 4.3 Rover and Honda : The Main Links

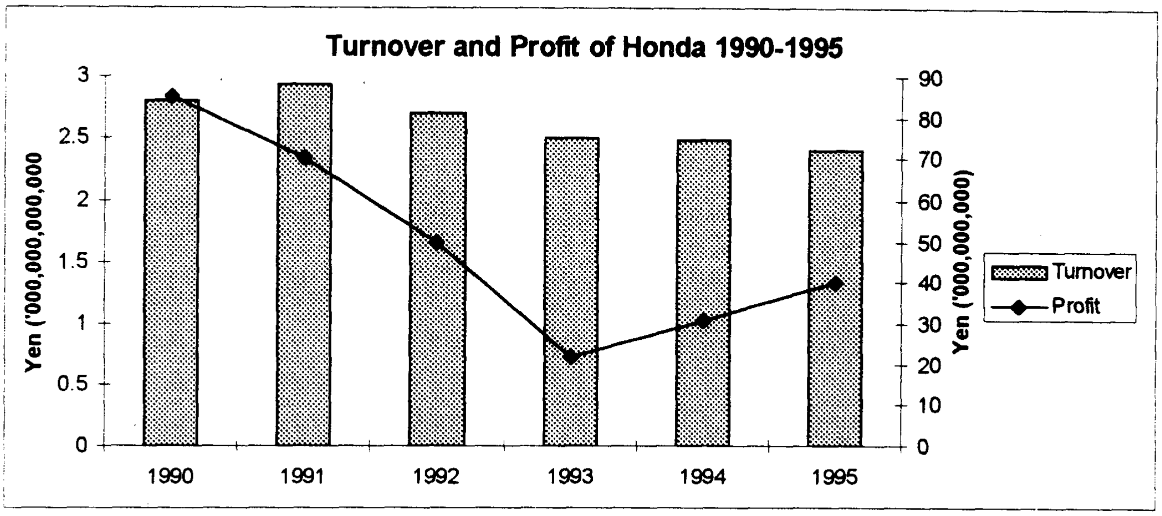
Type of agreement	Example	Status
Equity holdings	Honda has 20% stake in Rover Cars Rover has 20% stake in Honda (UK)	Honda selling to BMW BMW selling to Honda
Licensing	Honda car designing: Rover 200, 400, 600 and 800 Honda Component designs: eg Gearbox for 2-litre Rover engine Honda has supplied production equipment and technology to Rover for eg its 200, 400, and 600 models	Can be broken on 3-months notice; Honda to negotiate with BMW As above Rover able to maintain existing equipment
Component suppliers	Rover and Honda each sell the other about Pounds 400m-worth of car parts a year eg - Honda sells to Rover 1.6, 2.0, 2.3 and 2.7-litre engines; fascias for 600 models - Rover sells body panels to Honda for UK-made Accords Maintenance of common lists of parts specifications and suppliers	In many cases each party has to supply the other as long as the car model remains in production Disintegration of this relationship would quickly cause chaos on production lines
Vehicle sales	Rover makes Honda Concertos in Birmingham and supplies Land Rover Discoveries for sales as Honda Crossroads in Japan	Model sales likely to continue

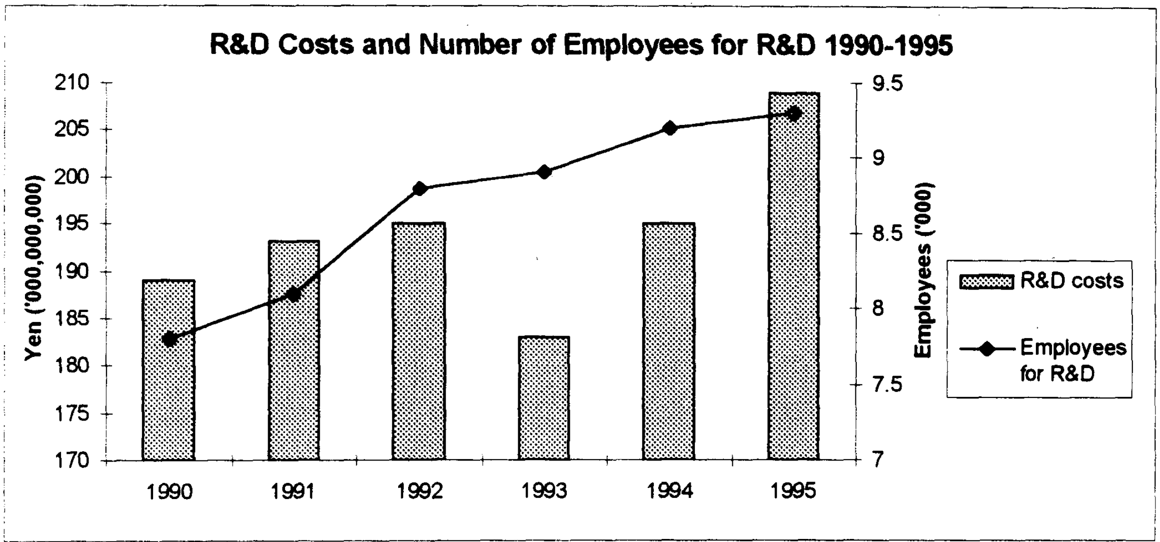
(Source : Financial Times, 22 February, 1994)

potentially direct competitors in the world auto market. Both have a similar history and have built their brand image on a high level of engineering and great performance in motor sport. Particularly, in the US, Honda has developed its separate luxury performance brand, Acura, and it directly competes with BMW. Hence, if BMW learns of Honda's engineering strength and of Japanese efficient production system through Rover, it will be a great advantage for BMW against Honda and will badly affect Honda's future survival.

Although Honda showed anger towards the BMW deal and seemed to break off collaboration with Rover, immediate annulment of the contract would also be problematic for Honda in terms of short term strategy. Honda have used panels produced by Rover

Figure 4.3 Change of Profit and R&D costs of Honda 1990-1995





(Source : Kokusaiteki Kigyoukankei ni Tsuite, 1996)

for the Honda Accord model and has no facilities of its own to produce those parts. It is said that it would take at least two years for Honda to install such capacity at its Swindon plant. Moreover, Honda has received approximately $600 million annually from the sales of components to Rover. Hence, Honda would have a financial problem if it pulled out. Because of these disadvantages, Honda could not terminate the collaboration immediately even though it was not willing to continue it. Table 4.3 shows the main links between Honda and Rover, and the state of the links after the takeover. However, Honda clearly states that it will maintain the collaboration till the contract is over, but in future it intends to create a more independent operation in Europe.

As was described, the reason why Honda did not acquire Rover was that Honda wanted to leave Rover as a "British" car producer. However, it is not the only reason. It seems that there are some internal reasons. Firstly, it should be noted that Honda is a distinctive company and it has strong policy on its management and has strong corporate culture in the organisation. Additionally, it is proud of its brand. Hence, it can be said that Honda was not willing to mix up Honda brand with Rover brand. Secondly, in terms of the financial situation of Honda, it could not afford to buy Rover at the time. As can be seen from Figure 4.3, Honda has invested a large amount of money in R&D, in spite of the fact that its profit has declined sharply because of shrinkage of the domestic market since the 1990s. In 1995, total amount of investment for R&D of Honda was 209 billion yen (£870 million) and this amount was almost equal to the amount BAe sold Rover at to BMW. (Nakamoto, 1996) Thirdly, Honda has also invested a large amount of money in its Asian operation. In 1996, Honda's annual production in Thailand exceeded 900 thousand units. Moreover, in the same year, it built a second plant in Thailand in order to produce its new Asian model, City, and reinforced its production in addition to its strong supply chain and distribution network in the Asian region. Thus, considering Honda's character, it was not feasible for Honda to control Rover and, considering its financial situation, it was very risky to hold 100% share of Rover at the time.

Chapter Five

Evaluation of International Corporate Relations in the Honda-Rover-BMW case

Needs change, and today's partner might not
be the best or the most suitable tomorrow.
Kenichi Ohmae (1989)

The Honda-Rover BMW case was a good example to compare and contrast differences of the strategic implication between "strategic alliance" and "merger and acquisition". It has been discussed that "strategic alliance" is long-term based and a 'friendly' strategy, while "merger and acquisition" is short-term based and an 'unfriendly' strategy. However, it depends on the situation whether or not which strategy is better to choose and both strategies have initial strengths and weaknesses.

The purpose of this chapter is to evaluate "strategic alliance" and "merger and acquisition" in the Honda-Rover-BMW relations. "Strategic alliance" in Honda-Rover relation will be, firstly, assessed by consulting the theoretical aspect, and then the evaluation of "merger and acquisition" in the BMW-Rover relation will be also made from the theoretical perspective.

5.1 The Honda-Rover Alliance

From the theoretical perspective, it can be said that the inter-company relationship between Honda and Rover was relatively stable and successful. Both formed an alliance in order to cope with keen competition in saturated motor vehicle markets and establishing stronger competitive position in the future by acquiring each other's strengths and complementing each other's weaknesses. It was meaningful for both to share costs and risks, because since the motor industry has shifted domestic operation to global, its trade environment has become complex and the level of uncertainty has increased. In addition, equity swap at a small percentage allowed both companies to maintain a friendly relationship for long time without a one-sided control. However, it should be noted that Honda and Rover each had a different motivation when they agreed to form the alliance. As described in Chapter 2, when companies consider an alliance, they are motivated by two different factors: *survival* and *competitive advantage*. In the Honda-Rover case, it seems that Rover approached an alliance on the basis of survival motivation, while Honda's decision was based on competitive advantage motivation. It seems obvious that Rover sought an alliance for survival considering the weakened British economic situation, emergence of foreign competitors such as Japanese and Americans and the insufficient production ability of Rover itself. On the contrary, it might be natural to assume that Honda was interested in an alliance from the competitive aspect as Honda had heightened its popularity not only in Japan but also in the US and Asia region, and it has aggressively competed with world major car producers.

The reasons why the Honda-Rover strategic alliance was so successful can be explained by "Four Cs of successful international strategic alliance", which were described in Chapter 2. Firstly, complementary skills were offered by both companies. Honda mainly has offered its excellent engine and Japanese production skills, while Rover has offered local market knowledge and components for Honda cars. Secondly, although it seems that cooperative cultures did not exist between both companies, as Rover positively tried to absorb Japanese management style and personnel in order to improve its inefficient management, there were not serious cultural conflicts between them. It can be said that, in this alliance, Honda approached Rover with the attitude of a teacher, whilst Rover had the attitude of a student. According to Hamel et al. (1989), alliances seem to run most smoothly when one partner is intent on learning and the other is intent on avoidance - in essence, when one partner is willing to grow dependent on the other. Considering their argument, it can be explained why Honda-Rover relationship lasted for a relatively long time. Thirdly, both Honda and Rover had compatible goals, although those were not achieved because of the acquisition of Rover by BMW. The goals might have been restoration of the British motor industry and establishment of competitive advantages in the European market. Honda really respected the history, tradition and originality of the British motor industry and wanted to protect it, and therefore Honda was willing to help Rover. At the same time, Honda could also promote its cars into the European market, where customers' preference is varied and markets are complexly segmented, through Rover's knowledge about the European market. Likewise, Rover could also reinforce its competitive advantages in the domestic and the European market by acquiring Honda's efficient production system and improving quality and productivity through the alliance. Thus, it can be seen that both companies had compatible goals, which would not be achieved individually, but require cooperative devotions. Finally, it seems that there were commensurate levels of risk between both companies. Although it might have been a disadvantage for Honda to form an alliance with Rover, which was declining, Rover also had some kind of risk to form an alliance with Honda. The reason is that Honda was a Japanese company and there might have been considerable cultural differences between both companies and there was a danger that Honda might have controlled Rover and used it for its own benefit. Hence, the degree of uncertainty of forming an alliance with Honda seemed much higher than of forming an alliance with American or European companies. At the same time, both shared costs and risks equally for R&D and product development. Thus, applying the Honda-Rover alliance into Four Cs, it can be seen that Honda and Rover met the four factors of successful alliance sufficiently and the alliance, therefore, could last for 15 years without conflict.

Even though the Honda-Rover alliance looked so successful, it was terminated by the takeover of Rover by BMW. However, this takeover was not a solitary cause for termination. It has been said that, theoretically, a strategic alliance which is not protected by formal contracts is inherently unstable and its life span is usually six to eight years. The main problem that emerged between Honda and Rover might have been increase of ambiguity for the cooperative objectives between them. Though compatible goals existed, those were rather ambiguous and it seems that there were not specific objectives. Moreover, some problems can also be found in both Honda and Rover. Honda's problem was that it failed to think about the attitude towards business that Western companies have. In many cases, Western companies is likely to concentrate highly on short-term profit and shareholders wealth maximisation. BAe has the same attitude towards its business and it wanted to dispose of its motor vehicle division, which had been unprofitable. Hence, Honda should have considered BAe would probably sell Rover to another company. Furthermore, Honda just kept ignoring BAe's offer about the sale of Rover and did not prepare for the sudden termination of the alliance. Similarly, Rover depended highly on Honda and seemed reluctant to operate actively and to establish originality. Rover was also optimistic and did not anticipate termination of the alliance. Thus, the Honda-Rover alliance case showed that longer strategic alliance would reduce its significance and effectiveness.

5.2 The BMW-Rover Acquisition

The BMW's acquisition of Rover can be categorised in "absorption of a competitor" in a type of merger, which is explained in Chapter 2. Although the advantage of "absorption of competitor" strategy is to reduce competition, BMW will probably not enjoy its advantage. According to Quinn et al. (1988), the theoretical argument was that in industries with many competitors, the absorption of a single one did little to reduce competitive uncertainty. That is, absorption of a competitor in the market where many companies exist does not necessarily give a competitive advantage to the acquiring company. In the BMW case, Rover is its direct competitor and both companies have been targeting mainly the European market. Particularly in Europe, there are many motor vehicle producers and competition is rather intensive. Hence, BMW's acquisition strategy may not be able to lead reduction of the competition and give a strong competitive edge to BMW from the theoretical perspective. However, it should be noted that although both are direct competitors, each of them has targeted different customers and has established a distinctive brand image towards customers. Moreover, each of them has developed cars which have different feature and therefore their products do not overlap after the acquisition. Thus, it seems that BMW obtained greater advantages from the acquisition against its competitors, although intensity of competition remains the same.

The characteristic of BMW is a typical "Western" company considering the way of its business. BMW preferred having 100 % of share in Rover to forming an alliance with others because it can control Rover freely and can increase its equity immediately. In addition, although BMW has been a specialist for larger and luxury car segment, it wanted to enter small, medium and four-wheel-drive car markets where demand for those cars is dramatically increasing by the acquisition of Rover. From the strategic perspective, it can be said that the BMW's decision to acquire Rover is appropriate. The first reason is that it can obtain immediate benefit from the growing market. Although there is an internal growth strategy as an option which is less risky than an acquisition or a merger, this is time consuming and also problematic when a company does not have skills and technologies. Furthermore, even though a company wanted to enter a new market through internal growth, it may not be able to get a preferable return, because the market on which it targeted may be declining when it enters markets as markets and customers preference are rapidly changing. The second reason is that the acquisition allows BMW to concentrate on reinforcing its large and luxury cars and enable BMW to maintain its brand image. This can be a great advantage to its major competitors who are consuming time, money and technologies for developing their own small and four-wheel-drive cars. In terms of economies of scales, the acquisition strategy seems effective for BMW. An acquisition leads to capacity expansion and increased capacity enables it to achieve economies of scale. According to McGuigan et al. (1975), a plant with twice the capacity of another plant can be constructed for less than twice the cost of the smaller one. Hence, BMW might be able to implement low cost production. Additionally, McGuigan et al. Pointed out the large firm may be able to achieve a relatively greater degree of brand recognition and brand loyalty from its higher level of scales promotion expenditures over an extended period of time. Thus, BMW might be able to get an advantage of economies of scale not only in operation but also on marketing through the acquisition.

The acquisition brings BMW not only advantages, but disadvantages. As is said in the theoretical view merger, financial risk might be a major problem for BMW as well. The acquisition enabled BMW to double its size, revenue and sales in unit, but if economies are in recession, the market shrinks, or the project fails, the damage that BMW suffers will be enormous. At the same time, in order to maintain or reinforce both BMWs' and Rover's competitive positions in a saturated market, BMW should invest a large amount of money into product development and sales promotion continuously. In addition to the financial risk, BMW may also have a problem of integration. Johnson and Scholes (1984) stated that the overriding problem with acquisition lies in the ability to integrate the new company into the activities of the old and this often centres around difficulties of cultural fit. The risk of emergence of organisational conflict which is associated with absorption of a competitor is also mentioned in Chapter 2. Thus the BMW's acquisition strategy includes a danger that serious conflict between BMW and Rover might happen in the near future because of culture and management style differences.

Chapter Six

Conclusion

6.1 Overview

In this dissertation, the main characteristics, strengths and weaknesses of "strategic alliances" and of "mergers and acquisitions" have been described by focusing on the international corporate relations between Honda, Rover and BMW. It is generally accepted that, in the current business situation, a "strategic alliance" is likely to be a preferable way for most companies to strengthen their organisations and expand their business either domestically or internationally. It has been discussed that a strategic alliance has become very popular because it enables a company to reduce costs, risks and uncertainty through its partners' local knowledge, skills and technologies when it tries either to launch new products, to enter a new market or to diversify its business to an unrelated area. Moreover, it might be also the factor to support popularity of the strategic alliance that partners can concentrate on their business freely as the relationship between partners is not based on control by one large and strong company. From these advantages, many companies tend to be attracted and to form an alliance without serious strategic considerations. However many companies are likely to fail to consider the disadvantages involved. Because of the lack of formal contract between partners, a relationship tied by a strategic alliance is rather vulnerable and unlikely to last long time. Additionally, although many companies seek a strategic alliance in order to cope with a change of customers demand, market and environment, and technologies, these factors tend also to increase the vulnerability of the alliance. Even though partners set compatible goals on the long-term basis, these situation changes will probably spoil the goals and reduce the significance of the relationship. Therefore, when a strategic alliance is formed, it should be precisely planned and should be understood well by partners what strategic goals are, when those will be achieved, and when the alliance will be terminated.

It has been discussed that mergers and acquisitions are also on effective strategy for the expansion of a company's business as well as strategic alliances. In 1989s, the number of mergers and acquisitions was drastically increased, particularly in Western countries. Although immediate achievement of objectives and acquisition of control are the major attractiveness for a merger or an acquisition, it leads to considerable problems such as increase of financial risks, emergence of organisational conflicts and difficulty of management control. Hence, many organisations have failed to manage a merger or an acquisition and business commentators state that in many cases mergers and acquisitions are unlikely to be successful. Nevertheless, even now, those strategies are so popular among Western companies as those are still the quickest way to achieve short-term profit and shareholders wealth maximisation. It would be more accurate to say that the reason for the failure of mergers and acquisitions is that companies concentrate too much on short-term finance rather than long-term management strategy. That is, lack of strategic objectives tends to lead to unsuccessful mergers or acquisitions. Therefore, it can be suggested that a company which acquires or merges with another company should evaluate whether or not the acquisition or the merger will be strategically significant. In doing so, the company might be able to avoid disastrous failure and to maximise the benefit from the merger or the acquisition. Thus, comparing both strategies, it can be seen that a strategic alliance and a merger or an acquisition have completely different characteristic and different approach towards partners, but it might be more important to note that without clear and consistent strategic goals, both strategies can not be successful and are unlikely to last long.

The case of Honda-Rover-BMW clearly showed difference between strategic alliances and mergers and acquisitions and the difficulty of managing international corporate relations. It can be said that the Honda-Rover alliance was successful as they could meet factors for successful strategic alliances such as compatible goals, complementary skills, cooperative culture and commensurate risk. Nevertheless, this relation was easily broken by the sudden acquisition of Rover by BMW. This case proved that even though the alliance seems to go well, it is still unstable and vulnerable. Although BMW should have consulted with Honda before the acquisition, Honda was also too optimistic for the alliance. Honda failed to consider the vulnerability of a strategic alliance and the characteristics of Western companies. Moreover, Honda might have been able to avoid the disastrous separation by considering BAe's financial situation and its objectives. In spite of the fact that BAe asked Honda several times to buy Rover, Honda did not take it seriously and even did not reply. It can be said that this kind of attitude also caused termination of the alliance. On the contrary, BMW adopted a quick response to BAe's offer by acquiring Rover. However, it seems a rather poor strategy. Although BMW maintains that the strategic purpose for the acquisition of Rover is to enter new markets such as small car and four-wheel-drive car markets, it is still short-term and potential problems are enormous. If BMW wants to make the acquisition successful, it should have precise long-term objectives. Otherwise, it may loose competitiveness in the future or worse may result in the acquisition by its competitor. Thus, this case tells us that a strategic alliance and a merger or an acquisition can be a very effective strategy for a company whose business faces global competition, but those strategies always include some kind of problems which can easily spoil the relationship. Therefore, it is suggested that a company which approaches another should consider which alliance strategy is the most relevant for future operation, should evaluate which partner is the most suitable to establish future competitiveness and should clearly recognise principal strengths and weaknesses of its alliance strategy.

6.2 Recommendations

Honda

Honda is planning to reinforce its plant in UK in order to stay independent. However, it might be better for Honda to have a closer relationship with local suppliers or customer to reduce costs and risks in local operation, although it might not want to.

Rover

Rover may be able to strengthen its product quality through the acquisition. Suggestions for Rover are to improve its weakened management and to actively obtain BMW's strengths such as excellent product development skills and high standard technologies. Its world wide distribution channel can be useful to increase customers recognition for the Rover marquee.

BMW

BMW may be able to improve its large and luxury cars, while its competitors devote their time, technology and money to small or four-wheel-drive cars. However, BMW should invest a large amount of money into Rover's R&D. Lack of investment may reduce Rover's competitiveness in the market and, consequently, operations costs will increase and it may cause serious financial problems to BMW.

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