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PROFILES OF INDUSTRIAL CONSOLIDATION: MERGER & ACQUISITION ACTIVITIES IN THE EUROPEAN ENERGY MARKETS

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Overview

In the past and as well as currently, Merger & Acquisitions (M&A) activities follow long term cycles and depend strongly on the equivalent status of the corresponding sector.² Acquisition rumors of p. e. Scottish Power through E.ON or Gas Natural raiding Endesa at this moment reflect the expectations of a further M&A wave – this is the fire to the markets' imagination and generates a mentality and behavior of auctioneer.³

Since the first M&A activities in the late 18th century when Exxon, formerly known as Rockefeller's Standard Oil Trust, successively acquired the US American Oil Market and reached nearly 90% of market share, the research area of the industrial growth development of economy and business has been of great interest.

„Industry segments that are consolidating reflect diminished competition as a result of there being fewer companies operating in that segment. Consolidation is typically driven by a change in regulatory or market forces and is manifested by many companies deciding to discontinue operations, merge, or acquire, hence lessening the number of players.“⁴

Since then, the energy sector is in a permanent process of consolidation, but the recent liberalization of the global energy markets in the late 20th century brought additional momentum to the M&A activities. One major reason was the combination of liberalization with the privatization of the industry in various countries, the large IPO's of EDF and GDF in France being a striking example.⁵ A first, overwhelming observation is that within the European Union the speed of liberalization and privatization was very different within the member states. In addition, the foundational status of the industry differed, in countries such as UK till 1990 and France till 2005, due to the dominance of national super monopolies in the supply side of the market in electricity and gas. But also in overseas countries, especially the Americas, the same processes had begun, as we all know producing different results.

The question in this context is whether the global electricity and gas sector achieved a current condition of industrial consolidation or whether the hitherto existing drivers of the consolidation activities can further drive their forces again within the next years. Furthermore, this analysis will offer a retrospective and historical view and an analysis of past M&A patterns and already completed processes of industrial consolidation. Therefore, a comparison of the

² Petz, M., Maier, K.-D. (2005): Konsolidierung folgt langfristigen Mustern. Munich: Tag & Nacht Verlag, TAM Nr. 19, p. 2

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⁴ op. cit. Clemente, M. N.; Greenspan, D. S. (1998): Winning at Mergers and Acquisitions – The Guide to Market-Focused Planning and Integration. New York: John Wiley & Sons, Inc.

⁵ Petz, M., Maier, K.-D., Oswald, K. (2005): Industriekonsolidierungsmuster europäischer Energiewirtschaften im Vergleich. Vienna: 4th International Energy Congress (IEWT 2005) at Vienna University of Technology, February, 16th 2005

activities regarding the energy market liberalization of the most important European markets critical in understanding the shape and dynamic of this important sector.⁶

Methods

Although this theme has been an ongoing issue since the first documented trust, there has not been any one common database standard representing the industry deals. In contrary, the existing material has several failures in methodology or typology is not up-to-date or just is false. In some regions, no valid material out of one or few sources is available at all.

Furthermore, only single examinations are available, but not in linked databases. Now it is the first time the existing data material has been composed, collected and decoded. So a unique existing database that is up to date has been developed with all documented trusts and M&A relevant activities within the electricity and gas sector of these countries for the period from 1991 to 2005.

In sum, during this period 1,039 transactions were identified in which more than 2,700 participants were directly involved as contract partners. As several companies are legal entities of combinates and are controlled by their mother companies, in total a quantity of about 1,250 autonomous firms and combinates took independent action in the M&A market. The value of transaction in Europe is available from 1991 to 2005 in 210 cases of the 819 transactions and amounts in total about billion 200 Euros.

As a result, we followed a stepwise approach: data from Germany and UK was available from different, unconsolidated sources, but for some merger or takeovers at least systematically counted by the cartel authorities. As additionally both countries now follow a similar market liberalization model, this offered an opportunity to start here and to show results on a short term basis.

Selected Research Findings

In Great Britain the consolidation strongly accelerated compared to Germany. One of the reasons is clearly the more restrictive cartel policy especially in Germany, but also the introduction of the new regulator. Currently, on the European level, there emerges a conflict between the Spanish Ministry of Economics and the European Merger and Monopoly Commission. If these differences contribute to a common solution of an EU standard for trust control remains as a question mark.

During the past two years in Germany the consolidation in the electricity and gas sector hardly ranged: Other reasons are in post merger integrations and corporate restructuring efforts of the German players. These issues have to be approached before further M&A activities can go ahead. The focus of the M&A activities in Great Britain mainly was set to the upstream (power generation) area.

Since then about 58% of the electricity and gas companies in Germany were target of transactions. There about 34% of those companies have been taken over. Especially, in the year 2004 the consolidation propelled in Great Britain to a consolidation grade of 79% as a transaction object.

Thus a similar development of density in both regarded markets is discovered, admittedly starting from different starting positions.

Although the quantity of the M&A activities were reduced from 46 transactions in 2004 to 16 transactions in 2005 to a level of 1994, a further internationalisation of the German utilities

⁶ Maier, K.-D., Petz, M., Schellenberg, T.(2004): Neue Studie untersucht M&A-Aktivitäten in Deutschland und Großbritannien. Eschborn: Dow Jones News (vwd) GmbH, vwd:energy-weekly, Nr. 51. p. 7-12

can be observed. In 2004 E.ON acquired the Hungarian gas business of MOL for EUR 2.1 billions. Also in 2005 E.ON was the most active German utility, when they acquired Caledonian Gas Field for about EUR 690 million.

In fact, the process of consolidation accelerated in Great Britain as well as the volume of transactions increased to EUR 18 billion. Here especially the EUR 8.6 billion National Grid Transco transportation and downstream business spin-offs have to be mentioned.

From a strategic point of view these acquisitions are the execution of an already directed country or sector strategies. E.ON continued its penetration strategy in Eastern Europe and laboured successively for the expansion in the gas business. Similar situation is true for Thuega, systematically implementing its country strategy in Italy, whilst the acquisition of the EnBW in Austria has some kind of a stand-alone character.

Selected Conclusion

1. The prognosticated dying of municipal utilities – that communal companies disappear in their existence - has not come true in a hard sense. But brisk acquisition behaviour of the integrated energy companies purchasing shares of city works and regional utilities can be observed. As result the archetype of the independent municipal/regional utility becomes increasingly rare.
2. The mature UK market shows that capital intensive and utilisation intensive industry tends towards oligopoly structures across several evolutionary phases. Main drivers are as follows: economies of scale and scope and economies of density.
3. The consolidation in Germany will be advanced through operational and strategic alliances on the level of regional municipal utilities within this and next year. In contrary to general assumption, the domestic consolidation will be continued by international finance investors did not prove valid, but will be continued by domestic companies in scopes of strategic alliances.
4. For the strategies of the energy companies the theory of ANSOFF seems to be evidence. Namely, product diversification is rarely applied, but more common are regional market penetration strategies and market expansion.