ISCTE Business School
Instituto Universitário de Lisboa

MERGERS AND ACQUISITIONS: CAUSES AND CONSEQUENCES

Search for market dominance

Bruno Alexandre Lopes dos Santos

Project submitted as partial requirement for the conferral of

Master of Science in Business Administration

Supervisor:

Professor Doutor Pedro Manuel de Sousa Leite Inácio, ISCTE Business School, Finance Departmant

April 2010

Resumo (Português)

A temática das *fusões e aquisições* surge como um ponto marcante no desenvolvimento empresarial dos EUA, que rapidamente se transformou numa referência na criação de valor empresarial por todo o mundo.

O caso da indústria do aço dá ênfase a esta temática, visto ser um processo de combinação de empresas num sector bastante disperso quer a jusante como a montante que deu origem a uma empresa dominante.

A emergência da economia chinesa juntamente com a conjuntura mundial levaram os dois maiores players desta indústria a um processo de combinação, contudo este não foi um processo simples. A abordagem hostil por parte da Mittal Steel não agradou aos dirigentes da Arcelor SA que deste logo puseram em prática um conjunto de *medidas defensivas* as quais, após elevarem a alavancagem financeira da empresa adquirida, forçaram a revisão (em alta) da oferta.

Assim, após uma forte pressão exercida pelos accionistas o processo consumou-se e as *sinergias* expectáveis, através da projecção dos *cash flows futuros*, anunciam um futuro favorável ao crescimento da ArcelorMittal.

Contudo, embora algumas *sinergias* já tenham sido alcançadas, o futuro económico e político está mais incerto que nunca , pelo que os *cash flows futuros* não podem ser assumidos como garantidos. Não sendo possível à ArcelorMittal descurar os aspectos de mudança na sua envolvente, de governação empresarial e de risco cambial.

Palavras-chave:

Fusões e aquisições, Medidas defensivas, Sinergias, Cash flows futuros

Classificação JEL:

L610 - Metals and Metal Products; Cement; Glass; Ceramics

G340 - Mergers; Acquisitions; Restructuring; Voting; Proxy Contests

Abstract (English)

Mergers and acquisitions marked a turning point in the economic development of U.S economy, which quickly became a worldwide reference on value creation.

In 2006, on a dispersed industry, either at upstream or downstream levels (steel industry) a strong example of a consolidation process took place creating a dominant player.

Emergency of the Chinese economy added to the perspectives of a financial crisis made the two largest steel players to enter on a combination process, process which was far from simple. The hostile take-over bid launched by Mittal Steel did not please Arcelor SA Board of Directors which implemented some *defensive measures* in order to avoid the possibility of being acquired by its main rival and, on more practical terms, leading to the increase of the offered price. Due to the forced price revision the deal was consummated.

According to the expected *synergies* expectable, by projecting *future cash flows*, there are positive predictions for the future of ArcelorMittal.

However, nowadays the economic and political future is more uncertain than ever and, although some *synergies* have already been achieved, the future cash flows can not be taken as granted. Some aspects such as the market changes, corporate governance and currency exchange risk can not be forgotten by ArcelorMittal group.

Key words:

Mergers and acquisitions, Defensive measures, Synergies, Future cash flows,

JEL Classification:

L610 - Metals and Metal Products; Cement; Glass; Ceramics

G340 - Mergers; Acquisitions; Restructuring; Voting; Proxy Contests

Executive Summary (Sumário Executivo)

Desde os primórdios, a criação de valor e construção de uma riqueza sustentável constituem o principal objectivo da gestão de empresas, devendo esta metodologia ser transmitida através de toda a hierarquia.

Com vista a aprofundar a temática anteriormente referida, o autor procurou encontrar um caso de estudo recente que tivesse revolucionado uma determinada indústria. Neste âmbito destacou-se o caso da indústria do aço protagonizado pelas duas maiores empresas do sector (Arcelor SA e Mittal Steel) que remonta a 2006 e que promoveu a consolidação de uma indústria bastante dispersa tanto nas operações a jusante como a montante.

A Mittal Steel foi constituída em 2004 através da aquisição da LNM Holdings N.V por parte da Ispat International N.V fusionada com a International Steel group Inc. Era, em 2005, o maior produtor de aço a nível de quantidade, tendo as suas vendas dispersas pelo mundo e a transformação da matéria-prima centrada em zonas *"low cost"*tais como o Brasil e a Europa de Leste.

A Arcelor SA foi constituída através da fusão de três empresas: a Espanhola Arcelania, a Francesa Usinor e a Luxemburguesa Arbed. O volume de vendas da Arcelor SA focava-se principalmente na Europa (71% das vendas).

Embora fosse o principal produtor de aço a nível de quantidade, a Mittal Steel, apresentava em 2005 um volume de vendas de 28,132 milhões de dólares enquanto a Arcelor SA, segunda maior, apresenta um volume de vendas de 38,438 milhões de dólares. Embora as linhas de produtos de ambas as empresas fossem idênticas, o valor acrescentado pela Arcelor SA nos seus produtos era bastante superior.

Contudo, em 2005, a indústria do aço entrava numa fase crítica, causada principalmente pela emergência de algumas empresas Asiáticas, principalmente chinesas que fizeram a China passar de um exportador para um importador de matérias-primas, controlando os preços das diversas *commodities*. Situação à qual os grandes "*players"* não poderão estar expostos, surgindo nesta sequência a proposta de *takeover* da Mittal Steel.

Esta tentativa de tomada hostil não foi bem recebida pelo "*Board of Directors"* da Arcelor que desde logo tomaram diversas medidas defensivas. As quais começaram por ser uma

crítica ao CEO e Chairman da Mittal Steel (Mr Mittal), mas rapidamente se transformaram em acções que alavancaram o nível de passivo financeiro da empresa (aquisição da Dofasco e a distribuição de dividendos elevados) passando pela tentativa de uma fusão *"amigável"* com os Russos da Severstal SA. Medidas que culminaram numa proposta de aquisição das próprias acções, que caso a proposta da Mittal Steel não tivesse sucesso iria promover uma elevada *alavancagem* financeira. Contudo a combinação ArcelorMittal tornar-se-ia uma realidade a 25 de Junho de 2006 impedindo tal medida.

Desta forma já dispondo dos relatórios referentes à empresa fusionada de 2007 e 2008, o autor procedeu à projecção dos restantes *cash flows* futuros, utilizando a metodologia do FCFF (Free Cash Flow for the Firm) baseando-se num crescimento das vendas e outros custos (excepto os custo das vendas) de 20% em 2009, 15% em 2010, 7.5% em 2011, 5% em 2012 e 3% nos seguintes anos. Quanto ao custo das vendas o crescimento considerado foi de 15% em 2009, 10% em 2010, 5% em 2011 e de 3% nos anos seguintes. Sendo assumido para o efeito uma taxa de crescimento do activo económico (*invested capital*) anual de 3%.

Face à necessidade de actualização dos *cash flows* encontrados procurou-se determinar um custo médio do capital (WACC) que reflectisse o equilíbrio entre passivo e activo existente na ArcelorMittal. Cruzando alguns pressupostos extraídos de algumas bases financeiras como a Bloomberg ou o Damodaran com os relatórios de contas da empresa. Foi assumida uma taxa de juro sem risco (OT's a 10 anos dos Estados Unidos da América) assim como um prémio de risco de mercado (Rm-Rf) de 5.5% *"Damodaran assumption"*. Quanto ao risco do sector (βu) foi considerado o do aço geral (Steel general) ajustado devido ao valor demasiado elevado provocado pela conjuntura actual. Quanto aos *"relatório e contas"* de 2006 a 2008 da ArcelorMittal foram retirados: taxa média de imposto, *net debt*, custos financeiros, capitalização bolsista (valor do *equity*) e o custo da ívida financeira (que não poderia ser inferior à taxa de juro sem risco utilizada na análise).

Assumindo uma perpetuidade de 3% após o ano 2018, estipulou-se um *entreprise value* de 672,739 milhões de dólares.

Contudo com vista a avaliar as sinergias geradas pela combinação destas duas empresas, assumiu-se a criação de uma empresa fictícia *Summed company* (empresa soma) reflectindo a soma dos resultados de ambas as empresas se estas continuassem a operar independentemente. Os pressupostos assumidos foram em tudo idênticos aos anteriormente descritos, com excepção das

taxas de crescimento que se situariam nos 3% ao invés do crescimento das vendas e seu custo apresentado na hipótese anterior. Quanto à formulação do WACC este também apresentaria algumas diferenças pois ponderaria o *entreprise value* de cada uma das empresas. Extraindo-se desta análise conjunta um valor de 166,718 milhões de dólares.

Assim foram calculadas sinergias futuras de 423,521 milhões de dólares. Contudo emergia a questão: qual a fonte destas sinergias?

Com vista à resolução desta questão o autor resolveu separar as sinergias em três grupos: sinergias de crescimento (incremento das vendas), sinergias operacionais (redução nos custos de produção) e sinergias financeiras (diminuição do factor de actualização).

Obteve-se desta forma a seguinte distribuição percentual das sinergias: crescimento 57.8%, operacionais 4.9% e financeiras de 37.4%.

Embora os valores apresentados sejam aliciantes, o futuro é incerto e as sinergias não são garantidas. A actual instabilidade económica e política coloca inúmeros pontos de interrogação relativamente ao futuro da economia global. Situação que adicionada à possibilidade de um *downgrade* no rating, ao risco cambial e ao domínio da família Mittal nas decisões da empresa, poderá promover um impacto devastador na ArcelorMittal.

Embora algumas sinergias já tenham sido alcançadas, após uma integração *"amigável"*, a ArcelorMittal ainda se encontra num processo de recuperação do investimento efectuado, não se devendo descurar os aspectos relativos à governação empresarial, mudança na envolvente ou alterações nas taxas de câmbio sob pena de cair numa situação de *default* financeiro.

Acknowledgments

I would like to thank to every person who had been involved, directly or indirectly, on my thesis development. Since the persons who supported my development as a person, such as Professor Clementina Barroso and Professor António Gomes Mota, professors from the financial department of ISCTE business school, to all of my friends and family. I would like also to acknowledge all and every person which gave me strengths to go forward and to develop this thesis mainly my family and some person who can be considered as so.

But my special gratefulness is to my supervisor/coordinator Professor Pedro Manuel de Sousa Leite Inácio which, since the first moment, supported my thesis, closely followed its evolution, always available understanding and questioning my theories. Thank you!

Index of tables

Table 1 – Gains on main M&A theories

Table 2 – Premiums payment methodology

Table 3 – Expected synergies on main kinds of M&A

Table 4 – Main steel extractors & steel transformers (2008)

Table 5 – Medium price per tonne sold in Euros (2005)

Table 6 – ArcelorMittal kinds of synergies expected

Table 7 – ArcelorMittal D/E ratio

Index of graphs

Graph 1 – Williamson trade-off

Graph 2 – Onion diagram

Graph 3 –M&A Waves in U.S

Graph 4 – Steel prices evolutions

Graph 5 – Nickel prices evolution

Graph 6 – Zinc prices evolution

Graph 7 – Thermal Coal price $/ton

Graph 8 – Coking Coal price $/ton

Graph 9 – Iron ore price C/dmu

Graph 10 – Natural Gas $/1000m^3

Graph 11 – Steel scrap price $/ton

Graph 12 – Electricity price C/Kwh

Graph 13 – Chinese market power

Graph 14 – Steel production by zone (in tons)

Graph 15 – U.S and China steel consumption

Graph 16 – Steel demand (Index 2006 Q1=100)

Graph 17 – Arcelor's foundation

Graph 18 – Mittal Steel foundation

Graph 19 – Severstal denomination change

Graph 20 – Negotiations between Arcelor & Mittal

Graph 21 – Main advantage and disadvantage on increasing mining activities

Graph 22 – Demand for steel (China against Rest of world)

Graph 23 – ArcelorMittal flow chart

Índex

Resumo (Português) I
Abstract (English) II
Executive Summary (Sumário Executivo) III
Acknowledgments VI
Index of tables VII
Index of graphs VIII

CHAPTER I – Literature Review

1. Introduction 1
2. Mergers and acquisitions main differences 2
2.1. Acquisitions 2
2.2. Mergers 2
2.3. Legal and image issues 2
3. Global perspective over mergers and acquisitions 3
3.1. Reasons for a Regulated Politic on M&A 3
3.2. Regulation in North-America 4
3.3. Regulation in European Union 5
3.4. International Cooperation 6
4. Cost/benefit analysis on Mergers and acquisitions: 7
4.1. Jacquemin's approach 7
4.2. Williamson trade-off 9
5. Organizational/Corporate culture 11
5.1. Relevance for M&A valuation and success measurement 11
5.2. Cultures and subcultures 12
5.3. M&A in different cultures 14
5.3.1 The requested cultural leadership 14
5.3.2 Avoiding failure in cultural integration 14
6. Waves of Mergers and Acquisitions 15
1st cycle – Era horizontal mergers 16
2nd cycle – Era of vertical mergers 16
3rd cycle – M&A activity in the area of conglomerates 16
4th cycle – M&A activity on concentric mergers, hostile takeovers, LBO's and junk bonds 17

5th cycle: Cycle of cross-boarder mergers - Transnational and Transcontinental M&A 17
"6th cycle – Era of M&A in order to fight against globalization" 18
7. Main theories of M&A 18
7.1. Theory of economic performance and efficiency 18
7.1.1 Cost reductions 19
7.1.2 Resources rationalization 19
7.1.3 Acquisition of resources 20
7.1.4 Increasing market power 20
7.1.5 Acquisition and diffusion of new technology 20
7.1.6 Speculation 21
7.2. Agency theory 21
7.3. Hurbis theory 22
8. Premiums 23
8.1. Premiums calculation 23
8.2. Premium payment 24
9. Synergies 24
9.1. Growth synergies 25
9.2. Coalition synergies 25
9.3. Operational synergies 26
9.4. Financial synergies 26
9.5. SGA synergies 26
10. Kinds of mergers and acquisitions 27
10.1.Horizontal Mergers and acquisitions 27
10.2.Vertical mergers and acquisitions 28
10.3.Conglomerate mergers and acquisitions 28
10.4.Concentric mergers and acquisitions 29

CHAPTER II – ArcelorMittal SA Case Study

1. Introduction to the case study 30
2. Steel industry 31
2.1. The Chinese emergency 34
2.2. The Arcelor and Mittal reaction to the environmental changes 36
2.3. Differences between steel industry in United States and Europe 37
2.3.1. United States (U.S) 37

2.3.2. European Union (E.U) 38
3. Main players 39
3.1. Arcelor S.A 39
3.2. Mittal Steel 40
3.3. Severstal S.A 42
4. The Arcelor question 43
5. The process 45
5.1. Corporate Governance Critics (November/December 2006) 45
5.2. Dofasco acquisition (January 26th 2006) 46
5.3. First offer (January 27th 2006) 47
5.4. Payout measure – Getting back shareholders trust (February 16th 2006) 48
5.5. Self tender offer (May 12th 2006) 49
5.6. Improved offer (May 19th 2006) 50
5.7. Severstal Meaure (May 26th 2006) 50
5.8. Shareholders questions about defensive measures – the perspective change 52
5.9. Third offer (June 25th 2006) 53
6. Future cash flows estimation 55
6.1. Enterprise value 55
6.2. Synergies 58
7. The Risks Associated with ArcelorMittal Merger – "Future Fears" 59
7.1. The integration problem in ArcelorMittal's growth 59
7.2. Independency on upstream operations – strength or a weakness 59
7.3. Geographical risk 60
7.4. People risk 61
7.5. Downgrade risk 62
7.6. Foreign Exchange risks 63
7.7. Capital Expenditures risk 63
7.8. Dominant shareholder risk 64
7.9. ArcelorMittal distribution process risk 64
7.10. Political risk 65
7.10.1. Associated with sales 65
7.10.2. Associated with resources requirements 65
7.11. Efficient integration risk 66
7.12. Assets held for sale 66

7.13.Steel industry 66
8. Conclusions 68
Bibliography 71
-Books & Monographs 71
-Press & scientific publications 72
-Thesis 74
-Websites 75

Exhibits

1. Exhbith regulations 76
1.1. Clayton's Act 76
1.2. Rule No 4064/89 of 21 December 1989 86
2. Exhibit top steel transformers by output 114
3. Exhibit main steel transformers financial data (2005) 115
4. Exhibit Arcelor financial data (2003-2005) 116
5. Exhbit Mittal financial data (2003-2005) 117
6. Exhibit Arcelor + Mittal financial data (2003-2005) 118
7. Exhibit Mittal offer evolution 119
8. Exhibit premiums 122
9. Exhibit mining risks associated with ArcelorMittal 123
10. Exhibit number of employees by segment 125
11. Exhibit ArcelorMittal financial data (2006* - 2008) 126
12. Exhibit Wacc assumptions 127
13. Exhibit Wacc calculation 129
14. Exhibit Arcelor + Mittal future cash flows (projection) 131
15. Exhibit ArcelorMittal future cash flows (projection) 132
16. Exhibit ArcelorMittal incremental cash flows (projection) 133
17. Exhibit Synergies 134

Para os que caminharam comigo: Mãe, Pai, coordenador e avós

"To the ones that walked with me: Mum, Dad, coordinator and grandparents"

CHAPTER I – Literature Review

1. Introduction

Creating value and building a sustainable wealth have been the main objectives of business management, which should be spread through all organizational stakeholders and not just centred in management.

Mergers and acquisitions where firstly identified as a turning point in the development of U.S This growth process, quickly became standard in business value creation standards through the world, allowing not only a simple increase on shareholder's value but, in some occasions, by offering value over the sum of the merged companies, generating *synergies*[1].

This method of organizational development has great significance not only in financial but also in strategic terms. M&A require a profound organizational reorganization by targeting all the organizational stakeholders from members or shareholders, taking care of customers, suppliers, financial and economic regulators not forgetting all the political powers involved.

Organizational change promoted by these growing methods may have different motivations, from achieving a better market position to efficiency improvements. Due to all potential benefits, acquired companies often agree to be purchased knowing that they would not survive alone. This *"win-win"* should be the basis for successful M&A activity.

In the following essay, the researcher will discuss M&A emphasizing his analysis on one of the main objectives of mergers and acquisitions: the pursuing of market hegemony.

After this introduction the author will present a chapter with a literature review on M&A, followed by a second chapter where the ArcelorMittal case is discussed. On a final stage some conclusion will be extracted.

[1] Gains related with the companies together generating higher results than the sum of both parts, being the equation "2+2=5" (Ansoff Igor) the special alchemy of a merger or an acquisition; in another words, the key principle behind buying a company is to create shareholder value over and above that of the sum of the two companies.

2. Mergers and acquisitions main differences

2.1. Acquisitions

Although both constitute a combination of two or more companies, mergers and acquisitions are different issues which sometimes were incorrectly identified as synonymous.

An acquisition is a process where a company acquires[2] a part or the totality of another's capital, such process can be suggested on a:

- *"hostile basis"* – not desired by the target and usually facing strong barriers imposed by the acquired company
- *"friendly way"* – although it can not be totally desired, faces insufficient barriers to its development

However, this is not a linear division. On business activity, an acquisition which starts on a friendly basis can end on a real *"arm wrestling"*.

2.2. Mergers

On the other hand a merger happens when two firms voluntary agree to go forward as a single new company rather than remain separately owned and operated.

After the merger process the overall company can remain with the name and judicial constitution of one of the merged companies or promote a *merger of equals*[3].

2.3. Legal and image issues

When one company acquires another, it allows the acquired firm to proclaim the action as a merger. Such action happens mainly because being bought tends to show negative connotations. Presenting the deal as a merger has the propensity to make the takeover process more pleasant. Sometimes, when both CEO's agree that joining together is in the interest of both

[2] Takes over

[3] Merger which creates a company with a different designation and different juridical constitution, where companies stocks are surrendered and new company stock is issued in its place; for example the merger between Daimler-Benz and Chrysler ceased to exists, creating DaimlerChrysler, and the merger between Arcelor SA and Mittal Steel which created ArcelorMittal SA

companies, it is possible to *"hide"* an acquisition. But when the deal is made on a *hostile* basis the process is always regarded and transmitted to the market as an acquisition.

3. Global perspective over mergers and acquisitions

Mergers and acquisitions in different countries and juridical systems

M&A can be experienced in just one country/juridical system or can involve, simultaneously, different juridical systems. This last approach was named as transnational mergers.

Due to its global impact, transnational mergers have recently become a crucial worry for governments. Although governments tried to find some answers to the problems emerged from this kind of mergers, the objective has not been fully achieved.

3.1. Reasons for a Regulated Politic on M&A

Mergers and acquisitions may contribute to the increase in competitiveness for firms operating in a global market. However, powerful companies in the market can promote a decrease on social welfare[4]. At this stage international regulation guidelines became essential in order to solve the problems arising from those companies *dominant* behaviour.

First effective idealization over transnational activity was defined based on two main issues:

- Transiting all benefits for social welfare
- Preventing and counteracting any anti-competitive behaviour

Complementing such theory, Neumann (1990) stated that these competition *guidelines* can be applied on two approaches:

- *Constructive – "assuming social welfare as the main objective"* being regulation just a way of replacing the market, when it is not managing resources efficiently or is not maximizing social welfare

[4] Through prices monopolization or even controlling competitors

- *Evolutionist – "based on Schumpeter's market vision"* being competition a dynamic process which generates technical progress[5] and the main objective of regulation is to build an institutional and economic environment which allows innovation, by eliminating barriers to new entrants

Adopting a *constructive* or an *evolutionist* analysis, the main purpose should always be promoting efficiency increases on resources usage.

3.2. Regulation in North-America

U.S first step on market regulation of market competition was given in 1890 with *Sherman's Act* promulgation.

Sherman Act constitutes the first "protection" of companies and consumers against dominant player's emergency[6].

Defending the free competition principle, this act stated that *"every person who shall monopolize, or attempt to monopolize, or conspire with any other person or persons, to monopolize any part of the trade or commerce among several states, or with foreign nations, shall be deemed guilty of a felony"* although never referencing M&A, this was the first regulation against the possibility of social welfare reduction caused by firms concentration.

The act which first emphasised mergers and acquisitions was Clayton's Act (1914). Approved by *Federal Trade Commission* (FTC) stated that *"no corporation engaged in commerce shall directly acquire the whole or any part of the stock or other share capital of another's also engaged in commerce (…) where (…) the effect of such acquisition may be substantially to lessen competition"* which can be seen also in *annex 1.1 – Clayton's Act*. After its promulgation the Act, together with Anti-trust division of U.S. tribunal of justice, started to be responsible for the detection of any illegal mergers or acquisitions.

In 1976 another step was given with the *Hard-Scott-Rodino Antitrust Improvements Act*, where legislation about M&A in U.S starts to concern the principle of *notification*[7] in order to control large industrial concentrations.

[5] Neumann (1990) *"Efficient process are discovered and new markets are creating by competing enterprises"*

[6] Denominated as trusts

[7] Where companies had to notify their M&A activity to anti-trust division

Evolution along the years had been constant and in 1968 the U.S justice department had promulgated the *Merger Guidelines*[8]. Although *Guidelines* were not a law, they brought transparency to control process.

3.3. Regulation in European Union

Rome agreement does not concern any article related to M&A. Before the 80's M&A activity in the European Union was ruled by the 81º and 82º articles, which do not emphasise M&A issues.

Regulation over M&A was just implemented in the end of 50's when the U.S had already half century of experience. This new regulation had got together different countries rules in order to shrink, the possibility of negative impacts on global market integration.

As the effective market realization in 1992, was expected to promote M&A exponential growth, additional legislation was needed. Leading to regulation number 4064/89 which concerns, between others:

- Real communitarian application [nº1, 2 and 3 of 1st article]
- Promotion on efficiency issues – an organization can have a technological process without penalizing the consumer surplus [number 1, b) 2nd article]
- Defining a concept where the consumer surplus was near one – being unacceptable to sacrifice the consumer surplus
- Application of strong restriction on M&A which tend to establish or reinforce a dominant market position [number 3 of 2nd article]

As can be seen in the *annex 1.2 – rule number 4064/89of 21 December 1989*, major part of guidelines was common to U.S Guidelines with specificities of a common market and not a common country.

[8] being reviewed in 1982, 1984, 1992 and 1997

3.4. International Cooperation

Internal application of regulations early described ignored the external/global effect of M&A. The existence of international cooperation and coordination proved to be essential as a way to obtain cross-border mergers which promote an increase on social welfare. Three main options in order to apply an efficient management over cross-boarder were suggested:

- *Bilateral cooperation* – reconciling the positions of different regulation authorities
- Creation of competition rules framework for M&A – based on a global regulator such as WTO[9]
- *Multilateral cooperation* – with the existence of a worldwide supranational authority

Although to achieve an efficient regulation *multilateral cooperation* should be the applied methodology on cross-boarder M&A regulation, *bilateral cooperation* was the more utilized coordination method.

In order to promote a better transnational cooperation some contracts were signed between EU, Canada, Japan and U.S[10] in order to promote a *multilateral* framework.

WTO, as expected, was presented as the promoter of this framework, its principal objective was to harmonize the market and avoid anti-competitive behaviour. Five years after the signing of the first pact (1991), a huge step was given with the creation of the "*Working group on the Interactions between Trade and Competition Policy*". This group identified two anti-competitive practices:

- Practices which impact on more than one market - with the essential multilateral cooperation in these circumstances where the existence of several authorities with different perspectives can generate several conflicts
- Practices which impact on distinct markets than its home market - there are problems in obtaining and processing information from the other markets, where legislation and regulation can be very closed

[9] World Trade Organization

[10] Pact of 1991 and 1998 are the mostly known

The conclusion extracted was that, given the lack of communication between different countries, *bilateral cooperation* can not be sufficient by itself according to WTO a *multilateral cooperation* agreement is needed including, between others:

- Principles and rules on a national level – competition policy and regulation on different countries
- Set of rules for anti-competitive practices – transnational rules
- Framework for cooperation provisions, aiming to identify and report anti-competitive practices with substantial effects on international trade
- Mechanism for conflict resolution

Not only domestic but, more than ever, transnational M&A can have negative impact on social welfare strategy and market performance (as will be seen on the *topic 4.2.).*

Such issues become more complex when the frame of analysis changed from a closed economy to an open economy. As the economy is becoming more global than ever, generate of inefficient situations caused by the lack of information tends to increase.

Although *bilateral cooperation* has been successful, some innovation is required, imposing the need of a *multinational cooperation*.

4. Cost/benefit analysis on Mergers and acquisitions:

4.1. Jacquemin's approach

As in all business terms, the main question on mergers and acquisitions consist of a success or failure analysis: do these decisions create or destroy value instead?

Following Jacquemin's (1990) perspective, benefits associated with mergers can be from two kinds:

- Cost reduction in terms of production and/or transaction
- Management efficiency gains

The same author refers that benefits provided by cost reductions in terms of production and/or transaction can be achieved by economies of scale[11] or economies of scope[12].

Both can be achieved with an increase on the rationalization of production and management, motivated by the merger process. Mergers process can be faced as a way to solve inefficiencies, as a company with a lower cost structure tends to increase its market share.

Although m*arginal costs* tend to decrease, on M&A activity arises the problem of *transaction costs*. But such costs can also be eliminated or internalized through a merging process, mainly on a vertical merger. Coase's approach (1937) stated that *"a firm will tend to grow until the costs of organizing an extra transaction within the firm become equal to the costs of carrying out the same transaction by means of an exchange on the open market"*. It is being positive to internalize activities when the market costs are higher than processing such activities inside the organizational structure.

Jacquemin's theory also added that benefits associated with management efficiency gains on mergers can be the solution for *agency problems*[13] as will be seen in the topic 7.2.

However, M&A can also have negative impact on customer prices, rival companies and even on merged companies. One example of a negative impact on merged companies can be given by *diseconomies of scale*[14].

Although issues such as *diseconomies of scale* can be relevant for economic analysis, the main cost referred by economic theories is the one caused on costumer prices and rival companies by the market power increase of merged companies.

[11] Follow Jacquemin's approach (1990) economies of scale can be:

- Static – when result from increase on the production inputs, not changing any production condition
- Dynamic – when result from a learning process

[12] *"Related with efficiencies primarily associated with demand-side changes, such as increasing or decreasing the scope of marketing and distribution of different types"* (www.wikipedia.com)

[13] Eisenhardt (1989), *"Agency theory is directed at the ubiquitous agency relationship, in which (the principal) delegates work to another (the agent), who performs that work. Such problems can arise when: the desires or goals of the principal and agent conflict and or if it is difficult or expensive for the principal to verify what the agent is actually doing"* adapted by the author

[14] Diseconomies of scale took place when a companies achieve a dimension which become departmental communication and coordination difficult, losing flexibility on environmental changes adaptation

Such increases tend to boost industrial concentration levels as smaller players, avoiding bankruptcy situations, are acquired by dominant players. Highly concentrated industrial sectors tend to have players selling at higher prices, much higher than their marginal cost, promoting several inefficiencies such as:

- Limitation on the quantity of products placed
- Production costs, become less relevant, as they have a limited impact on results – if companies have higher production costs they simply increase their prices without any market penalization[15]

Thus, market concentration through M&A can, also lead to *price cartelization*[16]. On the other hand, a decreasing number of companies in the market imply a reduction on customer choice, being itself a cost, leading to a welfare loss.

4.2. Williamson trade-off

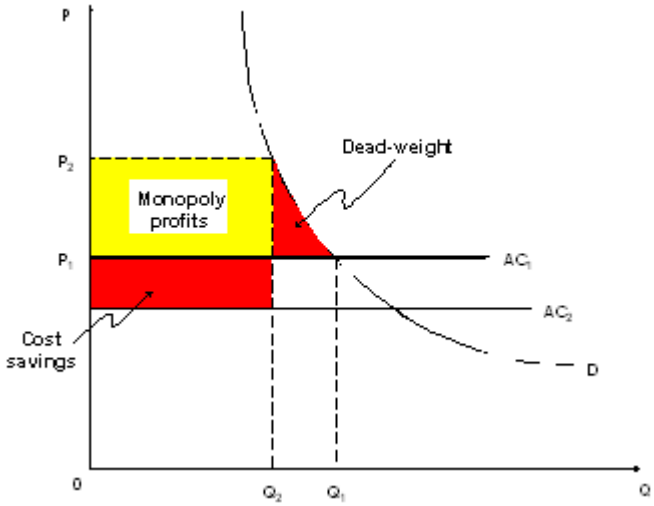
The author that developed the deepest study over welfare issues was Williamson, basing his theory on welfare determination promoted by an increase on market power (caused by M&A processes).

Williamson had developed a linear function where, assuming stable costs at a certain production level, tries to determine under what conditions the net effect of a merger on welfare is positive.

[15] Also called market monopolization

[16] Sullivan and Sheffrin (2003), *"Formal prices agreement among competing firms"*

Williamson theory is described in the following graph:



Graph 1 – Williamson trade-off
Source: http://www.med.govt.nz/

The graph shows that:

- An increase on market power is reflected in the increase of the equilibrium price from P_1 to P_2 and retrenchment of supplied quantities from Q_1 to Q_2; As a result of this change, consumer surplus decreases, however such decrease is not entirely appropriated by the supplier:
    - While *"monopoly profits"* area represents a transfer of surplus from consumer to producer;
    - *"Deadweight"* area symbolizes an effective loss in social welfare
- Decrease in average production costs from AC_1 to AC_2, associated with economies of scale promote efficiency gains, which result on a social welfare improvement represented by *"cost-savings"*

Williamson's theory stated that the net effect of a merger on social welfare will just be positive if:

"Cost-savings" > "Dead-weight"

It is important to refer that Williamson's model did not consider any difference between producer and consumer surpluses. Defending that *"total welfare"* is calculated through the sum of both surpluses. However, in his perspective, the balance between efficiency gains and consumer surplus reduction can not be forgotten. Defending that higher Q_1/Q_2 ratio require a higher cost reduction in order to keep a positive impact on social welfare.

5. Organizational/Corporate culture

5.1. Relevance for M&A valuation and success measurement

The relation between *corporate culture*[17] and organizational effectiveness attracted an increasing interest through the years, reaching a climax in the 80's. At that time corporate culture became a crucial subject due to the influence of *organizational values*[18] in organizational results.

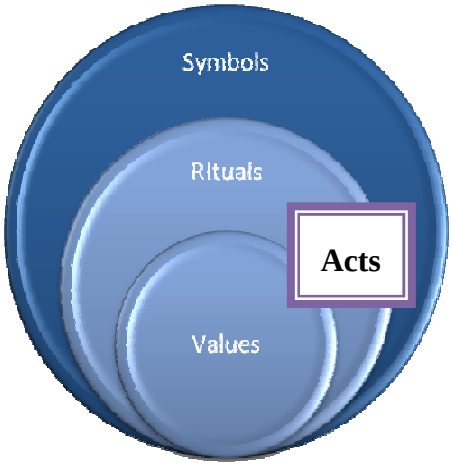
On the 80's Hofstede (1980) and Ouchi's Theory Z (1981) were the first theories directly related w *corporate culture*.

Hofstede defended the existence of five cultural dimensions which restricted cultural behaviour:

- *Power distance* – expected differences between power levels (proximity/distance to the leader)
- *Uncertainty avoidance* – capacity to accept environmental uncertainty
- *Individualism/Collectivism* – acting as a group or as an individual
- *Masculinity level* – male societies are traditionally ruled by competitiveness, ambition and material possession, being female societies the reverse
- *Short/long term orientation* – time horizon orientation

[17] Montana and Charnov (2008), *"Sum of values, customs, traditions and meanings that make a company become unique (...) corporate culture is often stated as the character of an organization since it embodies the vision of the company's founders (...) corporate culture influences ethical standards within a corporation, as well as managerial behavior"*

[18] Beliefs and ideas about what kinds of goals members of an organization should pursue, concerning also all organizational behavior standards



Graph 2 – Onion diagram

Source: Hofstede (1994) page 9 [Adapted by author]

If values are more connected with the moral and ethical codes, being a determinant factor of what people think that *"should be done"*, rituals and symbols reflect what people think *"is or is not true"*.

"Onion diagram" defended that acts/attitudes link values with symbols and rituals. In Hofstede's perspective what defines the employee's acts and attitudes is a conjugation between values, rituals and symbols transmitted not only through *corporate culture*, but also by their own culture.

Theory Z developed by *Ouchi*, also called *"Japanese Management style"*, was focused on employees loyalty to the company. *Ouchi* defended that companies should provide a welfare increase for any employee, in his perspective:

"High Employees Satisfaction = Productivity Increase"

5.2. Cultures and subcultures

It is common to identify organizations with one *corporate culture*, which is generally the culture of top management. On real business life cultural homogeneity is not verified, as several sub-cultures can be found that compete with the top management culture.

Working teams can also create their own habits and peculiar interactions which may lead to tensions within organizational structure disturbing the whole system. In this perspective, Roger Harrison (1972) and, on the 80's, Charles Handy (1985) stated that *corporate culture* can be adapted within different departments.

Roger Harrison and Charles Handy described four ways to link organizational structure to *corporate culture*:

- *Power culture* – concentration of power on a few
- *Role Culture* – power derives from hierarchical position
- *Task Culture* – power derives from expertise
- *Personal Culture* – all individuals believe themselves as superiors to the organization

Charles Handy defended that *Personal Culture* frequently makes organizational structure hard to manage.

Another contribution was brought by Edgar H. Schein (1985) that described *corporate culture* as *"a pattern of shared basic assumptions that the group learned as it solved its problems of external adaptation and internal integration, that has worked well enough to be considered valid and, therefore, to be taught to new members as the correct way to perceive, think, and feel in relation to those problems"* developing a standpoint observation which characterized three cognitive levels:

- First level includes *artifacts*[19], facilities and offices, the way company employees interact with organization outsiders, slogans or "jokes" which characterize organizational environment
- Second level concerns *organizational values*, which tend to be studied trough interviewing processes
- Third level is where organization's *tacit assumptions*[20] are placed; its existence is usually consciously unknown by the membership; being an element, usually, not investigated due to its complexity level

According to Schein's model miss understanding cultural norms can strongly compromise organizational future, meaning that the first and second levels can not be totally applied without the third[21].

[19] Organizational attributes that can be seen, felt and heard by an "amateur" observer

[20] Culture elements that are unseen and not cognitively identified on daily interactions between organizational member, but are present and strongly implemented in the company

5.3. M&A in different cultures

5.3.1 The requested cultural leadership

As it was previously justified *"different cultures within organizations are frequently appointed as one of the main reasons for the failure of integration processes"*.

On M&A processes each organization has its own culture which tends to clash when brought together due to *cultural differences*[22].

The main way to solve such differences is through the imposition of a strong cultural leadership. Organizational leaders should also be cultural leaders making possible the change from the two old cultures into a *"unified"* new culture. A common culture should concern:

- *Culture innovation*, through recognition of cultural differences, creating a new culture which replaces the previous cultures, and a
- *Culture maintenance* by reconciling old cultures in the new "unified" culture

5.3.2 Avoiding failure in cultural integration

If it is possible to find a dominant culture within an organization, it is understandable that M&A increase these features and cause culture shock on different levels of the merged organization.

Sometimes such shocks are expected and anticipated by cultural *due diligence*. The main problem arises when those cultural aspects are overlooked and undervalued, and cultural shock appears after the signing of the contract with all its potential hazards.

Failure to link strategic vision to process objectives may jeopardize organizational operations. *Due diligence*[23] is essential to avoid such errors on mergers or acquisitions evaluation process.

[21] Such situation leads, for example, to increasing difficulty for newcomers to assimilate organizational culture also explaining the change failure

[22] Which generate lack of identity, communication problems, and inter-group conflicts

[23] Process which allows an individual evaluation process, due to the specificity of M&A operations *"each merger is a different merger and each company is a different company"*

The basic function of *due diligence* on M&A context is to evaluate responsibilities, results and risks associated with each decision.

Being essential:

- Knowledge of the business
- Strong skills/competencies to match that knowledge, supported by clear objectives added to common sense
- Flexibility and open mind to constantly raising new questions

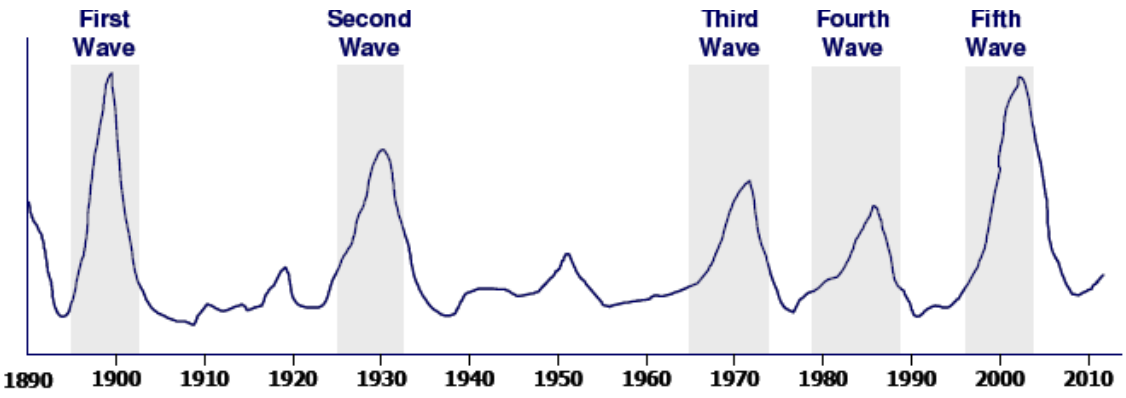
This analysis should always be focused on the cultural integration process.

6. Waves of Mergers and Acquisitions

Association with the environmental change

M&A cycles have not a specific starting or ending date, authors diverge when trying to point a date for the start of a new M&A cycle. By the other way ending dates are generally pointed as coincident with wars or financial disasters.

Cycles produce different effects depending on the political and economic space in which they took place. Analysing American's (U.S.) economy, historians and economists refer 5 waves of mergers:



Graph 3 – M&A waves in U.S.
Source: Paulo Bento (2004)

1st cycle – Era horizontal mergers

(1897 – 1904)

First M&A cycle was marked by a strong increase on horizontal mergers activity which created mainly steel, telephone, oil, mining, railroad and other giants of the manufacturing industry.

In this era some monopolies raised, followed by a deep transformation on economic and business structure, strongly associated with the installation of railways.

First cycle of M&A had slowed down with panics of 1904 and 1907, in association with the First World War and the creation of first anti-trust regulations.

2nd cycle – Era of vertical mergers

(1924 – 1929)

Second cycle promoted fundamental changes on economic structure, with consolidation of industries that were the subject of the first wave and also a significant increase on vertical integration processes.

This was the cycle where crucial developments in technology and manufacture took place, with the major automobile manufacturers reinforcing positions through new production processes [24]. The era of vertical mergers ended with 1929 "Crash" and "Great Depression".

3rd cycle – M&A activity in the area of conglomerates

(1950 – 1969)

Period in which the *"conglomerate concept"* raised in U.S. Assuming a visionary position, some of the major conglomerates, such as IT&T or Litton, were created.

In order to follow the market trend, some established companies accepted the concept and start a diversification process into new industries/areas.

Conglomerate stocks crashed in 1969 and the diversified companies never achieved the expected diversification benefits.

[24] Ford is one example with several improvements in the process

4th cycle – M&A activity on concentric mergers, hostile takeovers, LBO's and junk bonds

(1984 – 1989)

Cycle also named as the *"era of hostile takeovers*[25], characterized by a fierce bidding war for strategic positions.

In addition there was an increasing number of junk bond financing and a steadily increasing volume/size of *LBO's*[26].

After the 1987 stock market crash, U.S. corporate raiders had paused for a few months. The cycle ended with the collapse of the junk bond market in 1989/1990 added to the decreasing on savings and banks loans.

5th cycle: Cycle of cross-boarder mergers - Transnational and Transcontinental M&A

(1995 to …)

Cycle marked by deals with high transactional values named as "mega-deals"27 open space for uncommon processes "mergers of equals" (explained in the topic 2.2). Companies of unprecedented size and global sweep were created in this period28 on the assumption that size matters, boosting organizational market value.

The main problem is that high stock prices pressure companies to do "huge deals" to maintain heady trading multiples which, for some, were not supportable in the long run.

Fifth cycle was also the period of Millennium Bubble bursting and of great scandals, such as Enron, which promoted a revolution in all corporate governance issues.

For some authors this cycle is not ended yet, but for others, the collapse had started with the fall down of Internet stocks in 2000 followed by financing problems of telecoms, defending that a 6th cycle had already started.

---

[25] The first major-company hostile bid was made by Morgan Stanley on behalf of Inco, which *"opened the door"* for the major investment banks to make hostile takeover bids on behalf of raiders

[26] *"highly-leveraged transaction (HLT), or bootstrap transaction occurs when a financial sponsor acquires a controlling interest in a company's equity and where a significant percentage of the purchase price is financed through leverage borrowing"* (www.wikipedia.com)

[27] Nine of the ten largest deals in history, until 1995, took place in this period

[28] Chrysler and Daimler Benz, Exxon and Mobil, Boeing and McDonnell Douglas are examples

"6th cycle – Era of M&A in order to fight against globalization"

"(2003 to …)"

The stronger contradiction starts in the fifth cycle ended/sixth cycle start. In some authors opinion, after the first cycle ended, somewhere in 2001, the growth of merger activity between 2002 and 2006 (from USD1.2 trillion to USD 3.4 trillion) created a new M&A cycle.

Main factors which justify this growth were:

- Globalization
- Encouragement promoted by governments of some countries[29] to create some strong, internal and external, players
- Low financing costs availability and
- Tremendous growth of private equity funds with an increase in management-led buyouts.

"*The winds of globalization have forced businesses to target beyond their national borders for competitive advantage that is world wide in scale*" (http://www.lexuniverse.com – history of U.S M&A).

7. Main theories of M&A

In the last decades have been witnessing an increase amount on M&A activity. Between the main theories that justify such situations can be found:

- Economic performance and efficiency
- Conflict between decision makers and investors (agency theory)
- Hubris existence

7.1. Theory of economic performance and efficiency

Historically appointed as the main cause for business change, economic performance and efficiency theory defend that motivation for M&A procedure emergency is profit and company

[29] France and Italy are strong examples

value maximization, which is achieved through an efficient combination of two, or more, businesses.

Such efficient is reached when the expected value is greater than the sum of both parts *"2 +2 = 5"* (Ansoff, Igor).

$$V_{(A+B)} > V_A + V_B$$

Meaning that Companies together have an higher value than companies summed

Between the latest theories six causes can which promote this additional value can be found: cost reductions, resources rationalization, increased market power, acquisition of resources, acquisition of new technology and speculation.

7.1.1 Cost reductions

Cost reductions can occur on:

- Financial costs – arising from the existence of surplus funds on one company/business, which can be transferred to other businesses, internally financing its investment needs
- Operational costs – M&A can create economies of scale or scope (as it was explained on the topic 4.1) which can also promote a more efficient usage of human and technological resources, plant, equipments, materials and other inputs leading to a cost reductions.

7.1.2 Resources rationalization

Usually associated with optimized usage of available resources after a business combination, joint production will tend to reduce costs. If in the joint company there is one production facility able to fit all production requirements at a lower *marginal cost*, the merger process will tend to *"close down"* all remaining plants rationalizing the production resources.

However, economies of scale are more frequent in the distribution area, where a large supply chain with a broader coverage allows for lower distribution costs.

7.1.3 Acquisition of resources

An acquisition or a merger allows to the acquirer control over the acquired company resources. Expressing, following Porter's idea (1980) *"a fast way of organic growth"* inside or outside country boundaries.

Acquisition of resources through *cross-border*[30] M&A tends to be, nowadays, critical for business development when trying to access new markets or even reinforce its presence. M&A allows the elimination/reduction of lack of experience and knowledge in new markets.

7.1.4 Increasing market power

Increases on market power after M&A processes, due to the increase on market share, promote the improvement of organizational power over customers, suppliers, staff and other stakeholders putting higher barriers to new entrants. As it was explained in the topic 6 on the first U.S M&A cycles was common a fast achievement of *monopolistic* positions. With the emergency of some antitrust rules such processes become more controlled.

More recently, with the impact of the financial crisis, M&A process was referred as one way to avoid small organizations insolvency, being acquired by major industry players contributes to an increasing market power of the *merged company*.

7.1.5 Acquisition and diffusion of new technology

In order to stay competitive, players need to be on top of technological developments and business applications, M&A process assumes in such circumstances a crucial position. With the acquisition of other players, organizations can maintain or even develop their competitive edge[31].

Acquisitions allow spreading knowledge through combined companies, which could speed up the objectives achievement, seen as impossible without the combination.

[30] Outside country boundaries

[31] *Google Inc* example *"one acquisition per week"*

7.1.6 Speculation

Speculative actions are associated not only with different performance expectations and with relative position on industry sectors, but also take into account behavioural perspectives of organizational managers[32] - Different managers build different organization structures.

In the recent past, due to high economic fluctuation, an elevated level of speculation processes took place with a strong increase on *opportunistic acquisitions*[33].

7.2. Agency theory

Conflict between shareholders and managers

Agency theory described by Jensen-Meckling (1976), argued that *"managers should act as agents of shareholders (…) trying to avoid situations where there is a conflict of interests between decision makers and company owners"* Jensen-Mecklin named such problems as *agency problems*.

Stating that managers promote organizational growth and constantly efficiency improvements was the way to achieve their desired power and other rewards.

In this issue of efficiency level some measures can become a *"conflict point"*. Taking as an example the investment of surplus funds from operations[34] although it allows the financing of new projects, shareholders, worried about short-term dividends would strongly oppose to such decision creating *agency problem*s.

In such cases the solution appointed by Jensen's theory was that managers should distribute the surplus (FCFF) to shareholders through extraordinary surplus or acquire own shares (boosting market shares value).

In Agency theory, M&A was appointed as one radical solution, applied in order to restore the required efficiency and harmony of interests between shareholders, managers and all stakeholders.

[32] Different managers create different companies

[33] Short term acquisitions aimed to selling at higher prices, not following any economic reasoning

[34] Free Cash Flow to the Firm

7.3. Hurbis theory

According to Roll (1986) ideology managers make mistakes on *"target companies"* evaluation.

When acquiring a company listed on the stock market, the offer, due to market efficiency, should concern a conjugation between:

- Acquired company value – given by the market through market capitalization
- *A Premium*[35] – justified by the *incremental cash flows* the merged company is expected to generate

Roll's theory emphasis the mistake made by managers evaluation on *premiums* definition, which are driven to pay a higher price[36] being *"infected by Hubris"*.

Hubris existence lead acquirer managers to reduce requested *due diligence* tasks. *Hubris* in the case of takeovers can be associated with "auctions", the higher the competition, higher the premium.

The main problem become visible after the takeover, when synergies gains are not sufficient to cover the excessive premium paid. Such insufficiency is named as "winners curse"[37].

	Acquirer benefits	Acquired benefits	Total gains
Economic Performance and Efficiency	+	+	+
Agency Theory	-	0 or +	-
Hubris	-	+	0

+ Positive gains - Negative gains 0 Null gains

Table 1 – Gains on main M&A theories
Source: Berkovich-Narayanan (1993)

Following Berkovich-Narayanan (1993) M&A processes motivated by economic performance and efficiency improvements should create a positive impact even on the acquirer or acquired organizations.

[35] Difference between the offer value and the market value

[36] Roll (1986) *"bidding firms infected by hubris simply pay to much for their targets"*

[37] Defended by John Von Neumann and Oskar Morgenstern (1944)

But such results do not held for M&A motivated either by *Agency theory*, an acquisition motivated by lack of trust between managers and shareholders, or infected with *Hubris*, which became *"problematic when there is more than one potential bidder"* Robinson (2003).

8. Premiums

8.1. Premiums calculation

On mergers and acquisitions evaluation process some discrepancies can arise. Sometimes evaluation just focus on *"positive results"*, but such results may not be enough to cover the *cost of capital*. Analysis based on *accounting* results or on *value creation*[38] may lead to different conclusions.

This evaluation process tends to be facilitated not only by the knowledge in advance of some strength's generated by the combination, but also by the previous knowledge of future obstacles. Rodriguez in 2003 stated that *"in order to reduce disparities, some information should be worked in advance, before the final signing of the contract"* it is also relevant to study the value creation which *"should be taken into account not only the characteristics of tangible and intangible assets but also its influence on ultimate success"*.

Questions about valuation processes often lead to paid premiums to being questioned as one obstacle to combinations success. High premiums may represent an excessive force demonstration, but constitute an incentive for the acquired company being, at the same time, a potential synergies indicator.

In order to predict the future synergies it is essential to know if the acquisition was made on a *hostile* or *friendly basis.*

[38] EVA (economic value added) or CFROI (cash flow return on investment) are examples of financial instruments more used

8.2. Premium payment

Being acquisitions an investment, payment method will also produce future effects. Usually represented by only one, or a combination, between the two following payment methods:

- *In cash* – where the acquirer issues funds, which may exist within the company or must be obtained externally
- *By shares* – situation where the acquirer issue shares that are distributed to the acquired company shareholders; since there is no need for the use of funds, there is no increase in the financial risk of the new entity

However, considering future financial risks, it is important to take into account the fact that in a *cash payment* the shareholders leave risks exclusively on the purchasing company, when the *shares payment* is applied, the future risks are shared among all shareholders involved (acquirer and acquired).

	Acquirer responsibility	Acquired responsibility	*"Corporate involvement"*
Cash Payment	+	-	Only Acquirer
Shares Payment	+	+	Acquirer & Acquired

Table 2 – Premiums payment methodology
Source: Author

9. Synergies

Decision takers on mergers, acquisitions and other alliances have to know which resources, skills and other assets can be the source of *"value creation"*. Through an individual evaluation of each situation, as each asset have its own characteristics. Such evaluations can be generalized or not.

One of the main difficulties on *synergies* evaluation comes from the fact that after making an acquisition assuming future synergies, it become difficult to measure what would be the performance, after the change, without the combination.

Although *synergies* classification had been in constant evolution along the years, the author continues to prefer Chatterjee (1986) theory, distinguishing five main kinds of synergies:

- *Growth synergies*
- *Collusion/Coalition synergies*
- *Operational synergies*
- *Financial synergies*
- *SGA*[39] *synergies*

9.1. Growth synergies

Transformations on the 5th M&A cycle lead to the consolidation of some industries mainly based on the theory *"big is better"*. The main problem is that such kind of process forces firms to operate on high activity levels, putting higher pressure on investments.

Fifth wave characteristic goes aligned with *growth synergies* theory, believing that dimension gains are not only achieved by joining two or more companies. To reach an effective gain it is necessary to have an appropriate combination and the merged company must have the requested skills to produce new goods and services or improve the existent ones, penetrating and developing a sustainable growth on markets, accessing new information and new technologies.

Success on mergers and acquisitions is only achieved when combined companies take full advantage of skills and competencies of each other. However, this is only achievable when process attributes are adequately safeguarded being the *due diligence* processes the first step to achieve the desired results.

9.2. Coalition synergies

Coalition synergies are often associated with price agreements that, in some cases may be considered illegal. While *growth synergies* tend to occur on horizontal mergers and acquisitions, *collusion synergies* can occur in horizontal and vertical mergers within the same industry or sector.

[39] Selling, general and administrative expenses

9.3. Operational synergies

Operational Synergy is a concept used to describe the state of an organization when the people and processes work together, while maintaining competitiveness, to expand the ability to deliver products and services to its customers. It is the result of a disciplined process that enables integration of more than one organization skills and capabilities in a way that makes it possible to produce outstanding results consistently.

Operational Synergies occur when organization's diverse skills and capabilities are fully integrated allowing efficiencies in the supply, production or distribution.

As a result there will be:

- Cost reductions[40] or quality increases – *Direct synergies*
- Ability to change prices – *Indirect synergies*

9.4. Financial synergies

This kind of synergy can lead to a reduction of the cost on capital, through acquisition of companies with low debt levels, which can lead to a diversification or restructuration process.

Financial synergies can also be associated with perfection or imperfection of capital markets. Although some authors defend that such kind of synergies do not exist, just focus their analysis on operational and growth synergies, various studies prove its existence (Chatterjee, 1986) particularly in acquirer companies with larger debt levels, since their access to capital markets is more difficult and expensive.

9.5. SGA synergies

A SGA synergy refers to the opportunity of a combined corporate entity to reduce or eliminate expenses on business management, usually associated with the elimination of duplicate costs on general and administrative expenses[41].

[40] Economies of scale or economies of scope

[41] Where, between others, can be included: marketing expenses, payroll costs (salaries, commissions, travel expenses)

10.Kinds of mergers and acquisitions

Development and characterization of mergers and acquisitions

Caring about business structures, different business combinations promote different mergers. Developing a historical analysis, fours different kinds of mergers/acquisitions which depend on the level that is occupied by merged companies on the value chain can be appointed:

- *Horizontal* – companies in the same business or value chain level, in this situation a merger brings some resources overlap
- *Vertical* – companies positioned on complementary activities (different levels of the value chain)
- *Conglomerate* – acquirer and acquired companies are present on different businesses within one sector or are placed in different economic sectors
- *Concentric* - companies are located in different business units but related by the market or by the technology

10.1. Horizontal Mergers and acquisitions

Horizontal M&A are characterized by the combination of companies which operate on the same sector of the same industry and wish to form a larger organization, usually aspiring to:

- Efficiency increases on production and distribution – the main objective is to promote increases in economies of scale and scope, with a general reduction of costs – *focus on cost synergies*
- Increased market power through growth expectations – allow merged company to grow on existing markets as well as on new markets, products, brands and competencies – *focus on synergies by income or profit, or coalition synergies*
- Improved usage of resources – sell surplus assets, as well as promote an optimized combination of resources (tangible, intangible and human) – *focus on cost synergies*

Horizontal mergers can also be promoted by inefficient management of the target company, this basis of the agency theory, can also be associated with other kinds of M&A but does not always lead to value creation.

The reasoning behind the most successful horizontal mergers and acquisitions has been the combination between aspirations/synergies earlier described.

10.2. Vertical mergers and acquisitions

Characterized by mergers or acquisitions between companies operating in the same industry, but positioned in different stages of the value chain.

Between the main reasons and expectations which justify vertical mergers or acquisitions can be found:

- Technological efficiency increases
- Reduction or elimination of research, advertising, communication, production coordination and other transactional costs
- Improvement in inventories management (more efficient within a single entity, decreasing market dependency)
- Uncertainty avoidance on cyclical aspects on demand and by this way a reduction on market dependency
- Acting in stages with higher value added

Vertical integrations tend to promote a decrease on *"upstream supply"* dependency. Lead, in some cases, to a competitive advantage based on a dominant position over an essential industrial resource.

10.3. Conglomerate mergers and acquisitions

Conglomerates or conglomerated companies became popular on the 60's, characterized as *"multi-businesses"* organizations or *holdings*[42] with management over a range of non-related activities.

Conglomerates promote a business diversification, through acquisitions rather than based on organic growth. Requiring different research skills, engineering process and sales technique to promote an efficient manage of companies positioned in different industries.

[42] A company that owns enough voting stock in another firm to control management and operations by influencing or electing its board of directors, also called parent company (www.investorwords.com)

There are two main kinds of conglomerates distinguished:

- Financial or financial control
- Operational, strategic or administrative

While financial conglomerates are exclusively focus on the exploration of *financial synergies*. Operational, strategic or administrative conglomerates explore *operational synergies* additionally to financial synergies.

Conglomerates promote the sharing of knowledge and resources between business units, as a source of competitive advantage. But, in conglomerate integrations, *"bad buying decisions"* can put the whole organization at risk.

10.4. Concentric mergers and acquisitions

Concentric integration processes consist on agreements between companies positioned in different sectors but with common markets or processes/technologies used.

The more common concentric combination is widely known as *"bank-assurance"* leading to M&A or other alliances between banks and insurance companies. In the recent years has emerged a new type of concentric combinations relating banks and telecommunications companies.

Combining the kinds of mergers and acquisitions with expectations about the five kinds of synergies described on the topic 9:

	Horizontal	Vertical	Concentric	Strategic conglomerates	Financial conglomerates
Growing	++	+	++	++	-
Operational	+	+	-	-	-
Coalition	++	++	+	+	-
Management	++	+	+	++	++
Financial	+	+	+	++	++

++ Main objective *+ Complementary objective* *- Not expected*

Table 3 – Expected synergies on main kinds of M&A
Source: Author

Can be concluded that financial and growing synergies are expected on almost all types of mergers or acquisitions, by the other way operational synergies are just expected on horizontal and vertical mergers.

CHAPTER II – ArcelorMittal SA Case Study

1. Introduction to the case study

The acquisition of Arcelor by Mittal presents, a recent (2006) and unusual merger process in one dispersed industry, at *upstream* and *downstream* levels, where the leader acquires its nearest competitor, searching for a hegemonic market power.

This consolidation process of the steel industry started at 27th January, 2006 when Mittal Steel initiated an historical acquisition pretending to create a giant steelmaker changing the route of this industry, decreasing Mittal's market dependency and creating a new industry leader with an increased bargaining power over stakeholders.

The unpredictability of Mittal's offer comes from the steel industry history, where the growth based on acquisition, was marked by a fierce bidding war between these two players. An example of this bidding war was Mittal Steel acquisition of Kryvorizhstal in October, 2005[43] after a fierce dispute with Arcelor which was fought back by Arcelor with Dofasco's acquisition on January 24th, 2006[44] after a dispute with Thyssenkrupp.

Dofasco's acquisition was one of the most efficient defensive measures executed by Arcelor S.A after the Mittal Steel takeover (first offer) announcement. The position occupied by both companies in the industry (leader and nearest competitor) and the defensive measures applied by Arcelor S.A (strongly supported by Spanish, French and Luxembourg governments) made this particular merger so unpredictable and unexpected.

Since the first offer at 27th January, 2006 the market saw continuous attacking and defensive measures of both parties which changed the expectations regarding the conclusion of the deal predictions for each side several times. But, after all, Mittal's offer ended up at June 25th, 2006, after two improved offers, as being considered as a *"good business opportunity"* by the same persons[45] that had considered it as *"completely unacceptable"* in the beginning of the year.

But, how was it possible to change this perception in such a short period of time? The present case study describes the factors which contributed to this huge change in Arcelor judgment about Mittal's offer. Other points that existed before the merger, such as defensive

[43] For USD4.8 billion

[44] for USD5.6 billion

[45] Arcelor CEO (Guy Dollé) and other main shareholders

actions in mergers and acquisitions, how can an industry analysis help to understand M&A trends, the expected synergies, shareholders structure and corporate governance issues before the merger are also assessed. This analysis intends to be useful in order to understand the post-merger position and the future challenges such as the effective realization of expected synergies, shareholders structure changes and corporate governance issues.

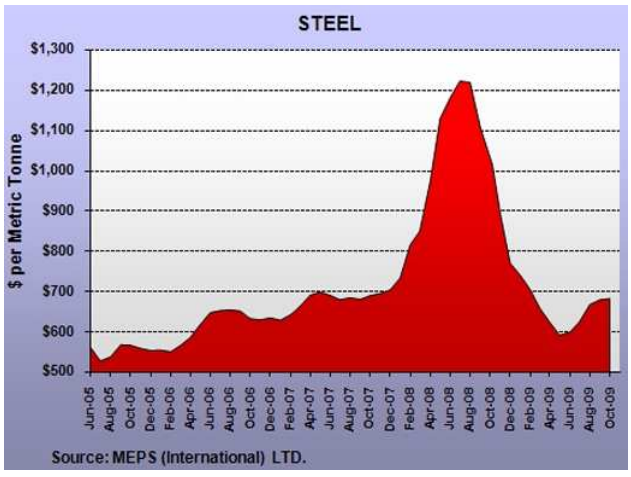
2. Steel industry

Steel industry was marked, since 2004, by a fierce fighting for the market leadership at upstream operations between Arcelor and Mittal.

Before Mittal's tender offer over Arcelor, steel industry was very fragmented in terms of market share, being highly cyclical and very competitive.

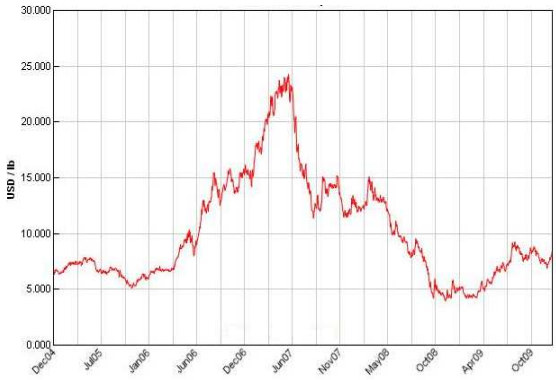
Facing such problem the industry entered on a consolidation phase where the smaller players, in order to avoid bankruptcy, started to be acquired by the larger ones. Stronger players at *downstream* operations emerged through this process, but at *upstream* operations the market dependency problem strongly remains.

The market dependency started to be seen as "*the main threat*" when the upward pressure on steel prices caused by the fast growth of steel products demand from China, India and other developing economies



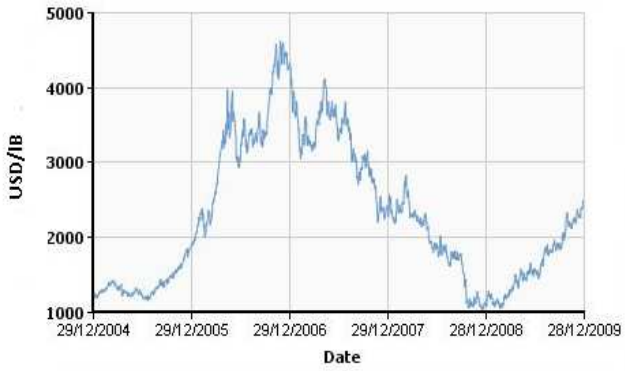
Graph 4 – Steel prices evolutions
Source: MEPS (International) LTD

The emergency of new players, a sharp rise in some commodities essential for the steel-making process (zinc or nickel) and a consolidation process in the mining industry are contributing to make the steel prices (final products) rise significantly.



Graph 5 – Nickel prices evolution

Source: www.kitcometals.com/charts/nickel_historical_large.html

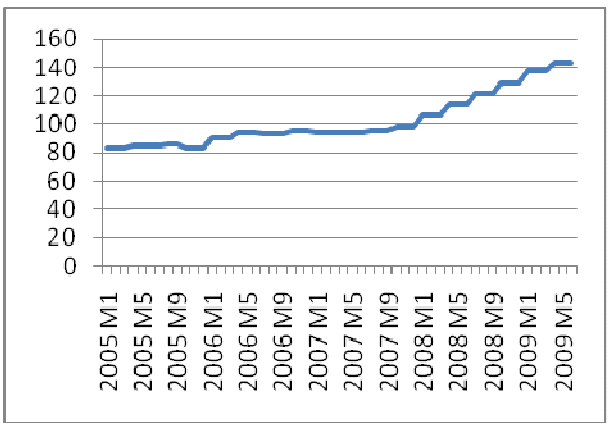


Graph 6 – Zinc prices evolution

Source: www.lmo.co.uk/zinc_graphs.asp

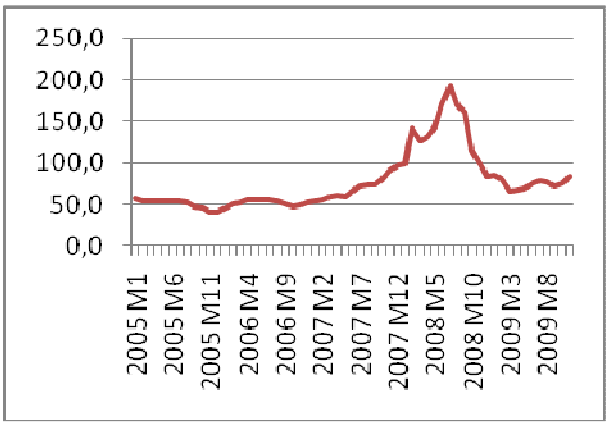
Analysing the market, since 2005, there is a general increase on prices of zinc and nickel, following the steel trend.

The same trend was verified on steel input costs:



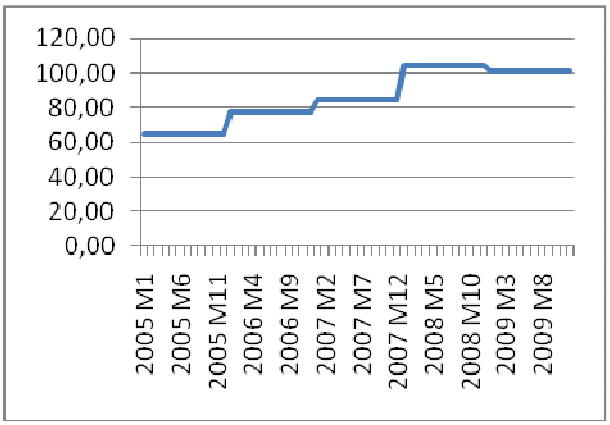
Graph 7 – Thermal Coal price $/ton

Source: www.steelonthenet.com/files/steel_costs.html



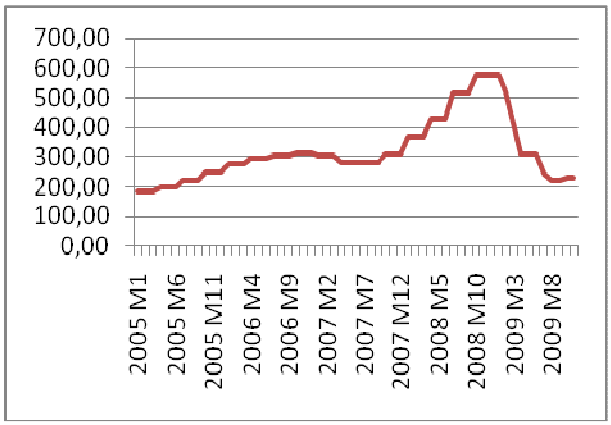
Graph 8 – Coking Coal price $/ton

Source:www.steelonthenet.com/files/steel_costs.html



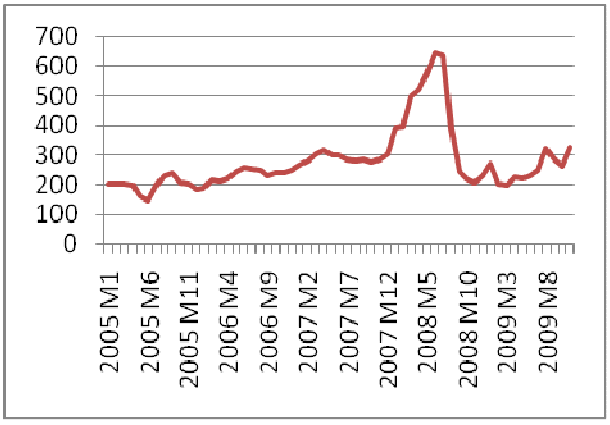
Graph 9 – Iron ore price C/dmu

Source: www.steelonthenet.com/files/steel_costs.html



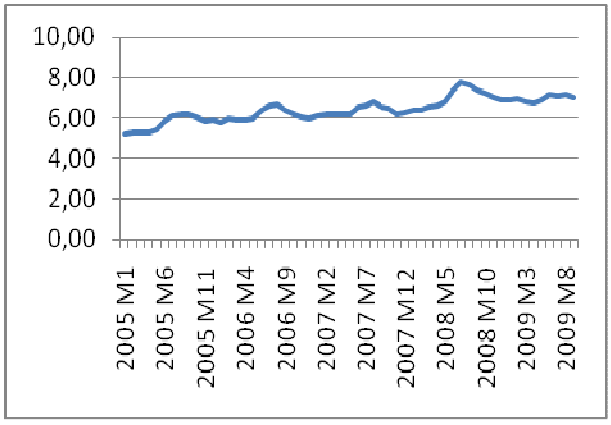
Graph 10 – Natural Gas $/1000m^3

Source: www.steelonthenet.com/files/steel_costs.html



Graph 11 – Steel scrap price $/ton

Source: hwww.steelonthenet.com/files/steel_costs.html



Graph 12 – Electricity price C/Kwh

Source: www.steelonthenet.com/files/steel_costs.html

Steel industry increased its degree of volatility, both in terms of earnings and of production output. Significant increases of some metals, energy and other inputs to the steel-making process had contributed to increase the volatility of steel prices.

Producers and consumers limited control on price made players face a huge disparity between demand and supply, mainly because of the increasing developing countries demand named as *"Asiatic steel demand"*.

But there are other factors which had strongly contributed to drive this trend, such as the global economic conditions with mainly the recession felt in the automobile, construction and other industrial products industries leading to a reduction of the demand for steel.

2.1. The Chinese emergency

Chinese increasing influence changed the steel market. High domestic demand for infrastructure ignited by the fast industrialization in the country had produced an oversupply at world's level of Chinese steel products.

This oversupply had promoted a consistent increase of input prices, starting to pressure the region's profitability and making the industry more cyclical. Consequentially, China has emerged as *"the key factor"* in the global steel market, linking the ups and downs of Chinese economy to the ups and downs of the steel industry.

After a fierce consolidation process, where the smaller players were acquired, although the first steep in the consolidation process had been given, due to the Chinese emergency steel producers remained highly dependent on Asiatic players.

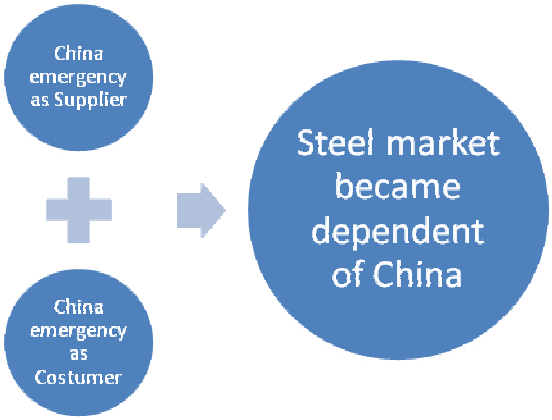
Country	Company	Steel Extraction in mmt(*)	Steel Transformation in mmt(*)	Steel Extraction - Steel Transformation	Self-Suficent
Luxembourg	ArcelorMittal	103,3	116,4	-13,1	No
Japan	Nippon Steel	37,5	35,7	1,8	Yes
China	Baosteel Group	35,4	28,6	6,8	Yes
South Korea	POSCO	34,7	31,1	3,6	Yes
China	Hebei Steel Group	33,3	22,8	10,5	Yes
Japan	JFE Holdings	33,0	34,0	-1,0	No
China	Wuhan Steel Group	27,7	20,2	7,5	Yes
India	Tata Steel (Corus Group)	24,4	26,6	-2,2	No
China	Jiangsu Shagang Group	23,3	22,9	0,4	Yes
US	U.S. Steel	23,2	21,5	1,7	Yes

Table 4 – Main steel extractors & steel transformers (2008)

Source: www.wikipedia.com [adapted by the author]

As can be analysed from the previous table, four Chinese players can be found among the Top 10 players in terms of steel extraction[46].

Since 2004, Chinese power over the market had become more intensive not only in terms of natural resources output, but also in terms of steel products, based on their main competitive advantage: the natural resources self-sufficiency.



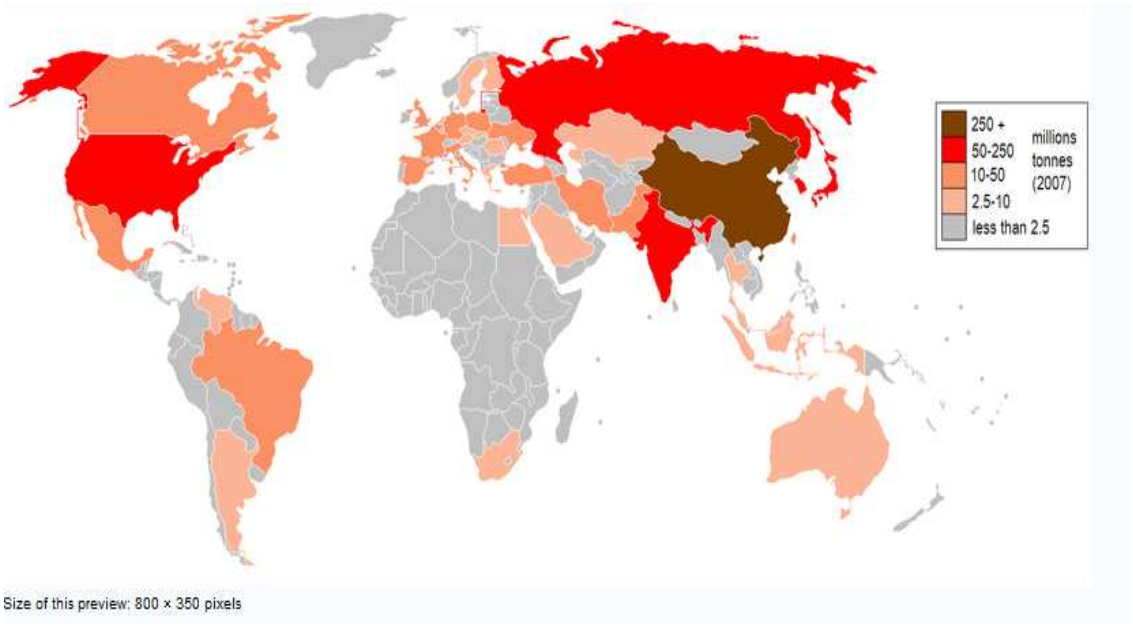
Graph 13 – Chinese market power
Source: Author

With the consolidation process, Chinese market passed from a *"large group of small firms"* to a *"restricted group of dominant players"*.

[46] *Upstream* operations

2.2. The Arcelor and Mittal reaction to the environmental changes

Facing the global increase on input costs, Mr Mittal stated that *"Something needs to be done on the steel industry"* defending that the major industry players should not be dependent on a highly volatile commodity strongly controlled by the Chinese players.



Graph 14 – Steel production by zone (in tons)
Source: www.wikipedia.com

To reduce market dependency a stronger player was needed, and the merger between the two major players started to be seen as the best solution to counteract the steel industry trend.

At that time there was a first proximity between Mittal and Arcelor CEOs when they admitted that steel industry's consolidation was *"the way through success in this fragmented industry"* (Mr Dollé Arcelor S.A CEO) and Arcelor's shareholders started to face Mittal's takeover as *"the solution to acquire a hegemonic position*" and to fight the high volatility of the steel prices.

Together Arcelor and Mittal would be able to produce more than 10 percent of the world global output, close to 100 million tones of steel, as can be seen on *annex 2 – top steel producers by output*. This would promote an increased pricing power and a decrease on industrial fragmentation. However the market dependency problem would not be completely solved.

The consolidation process would create a stronger and more competitive market leader, allowing a stronger impact on emerging markets, such as Brazil, China, India, Russia and Eastern

Europe[47]. This was an essential measure as these countries are increasing their demand for steel, the major steelmaking producers started to move to, or were already placed in those regions, looking for lower operational costs.

2.3. Differences between steel industry in United States and Europe

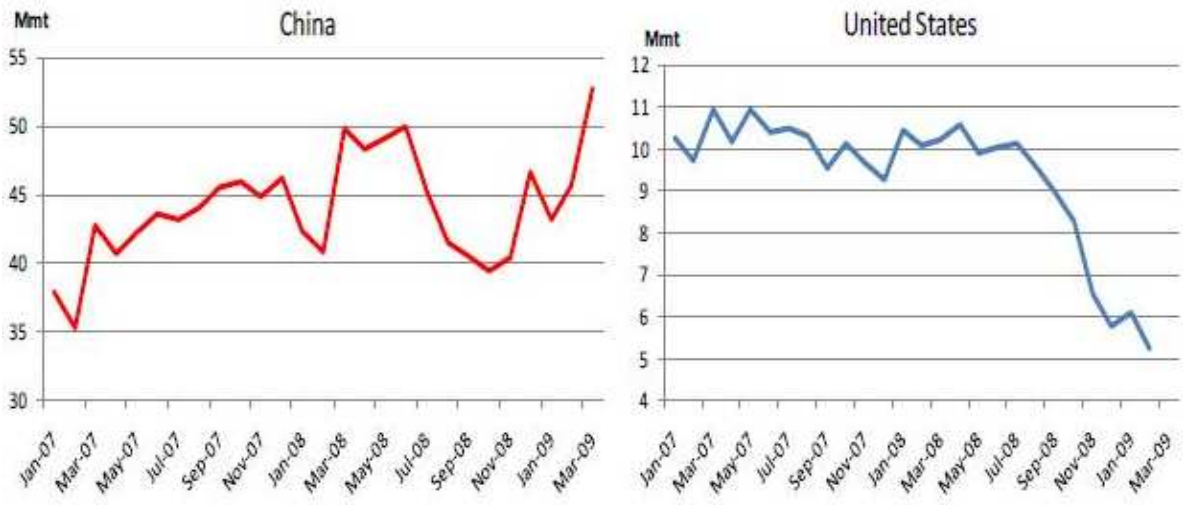
2.3.1. United States (U.S)

Referred as the major steel importer, its main natural steel resources supplier is NAFTA[48], through its countries. Although the financial crisis, U.S demand for steel steadily increases.

All issues involved in the steel industry, as in some other industries, are totally different from other industries globally due to the United States *"management style"*.

United States players have their capital structures highly leveraged, when compared with players from other countries. This fact led the U.S bond issuers of the steel industry to have a higher default rate than in any other world economy.

Liquidity issues were not relevant in the United States, shareholders just focus their analysis on short-term returns and this was the main reason behind the riskier strategies assumed by steelmakers and the impact that the world crisis had promoted in this country.



Graph 15 – U.S and China steel consumption
Source: OECD

[47] Due to Mittal's position in such markets

[48] International trade organization composed by USA, Canada, Mexico, Brazil and China

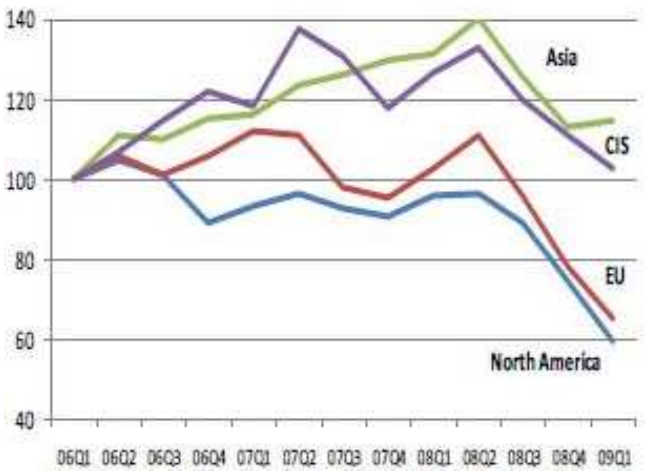
2.3.2. European Union (E.U)

Being a net steel exporter, European Union imported several materials such as semis, hot rolled coil, wire rod, galvanized sheet from 5 main countries: Russia, Turkey (which is trying to enter on European Union), Ukraine, China and India.

Turkey integration in European Union would constitute a colossal step in this industry, as Turkey is the second largest European source of steel imports.

E.U management style is completely different from U.S. European steelmakers hold high cash balances following a cautious approach to liquidity. Shareholders care more about the medium/long term investment return when compared to U.S investors.

However, the main difference between U.S and E.U steel industries is the consolidation of the industry. U.E power is more divided (different countries, with different players) while the U.S, being just one country, has a major player which strongly influences its internal market.



Asia – Main Asiatic countries CIS – Commonwealth of Independent States

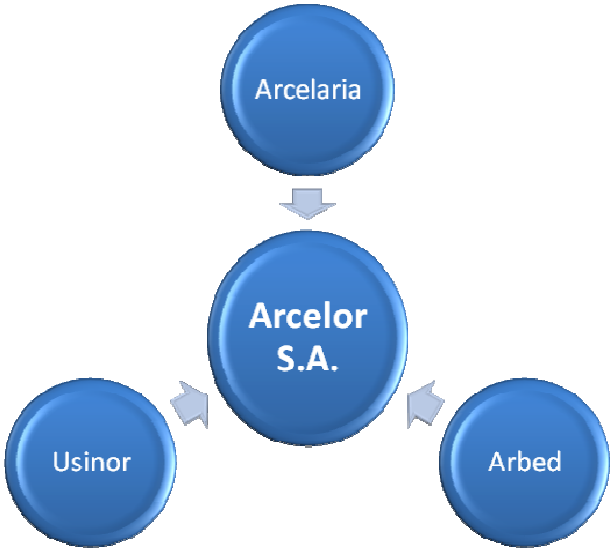
Graph 16 – Steel demand (Index 2006 Q_1=100)

Source: OECD

3. Main players

3.1. Arcelor S.A

Arcelor was created by a merger of the Spanish steel producer Arceralia, the French company Usinor and Arbed, a Luxembourger company.



Graph 17 – Arcelor's foundation
Source: Author

Arcelor's headquarters were placed in Luxembourg, and its production was divided in three lines:

- Flat steel products
- Long steel products
- Stainless steel

In 2005, Arcelor's sales reached USD 38.4 billion (about 71% based in the European Union) with an operating margin of 13.4% (*see Exhibit 3 – main steel transformers information in 2005*). In 2005 the company was the second largest steel producer in terms of output, but the first in revenues [*see annex 2 - top steel producers by output and annex 4 - Arcelor financial data (2003-2005)*].

Arcelor's equity was dispersed (largest shareholder - Mr Grand Duchy just owned 5.6% of total shares).

Organizational history shows involvement in some public bidding war's (mainly acquisitions). In 2005 the lost of Kryvorizhstal acquisition business against Mittal Steel was one example of a controversial bidding war.

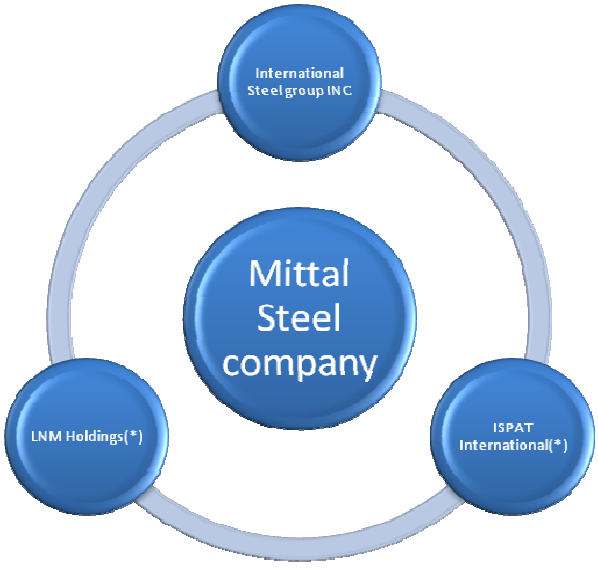
Arcelor was strongly developed on *downstream* markets, where it performed several value added activities and custom projects, through A3S, an Arcelor's division that was responsible for 27% of Arcelor's revenues (2005 information).

In 2006 the organization had 310,000 employees in 60 countries.

3.2. Mittal Steel

The achievement of Mr Mittal in the steel market was mainly supported by growth through acquisitions: Iron and Steel of Trinidad & Tobago, Sibalsa, Sidbec-dosco, Walzdraht Hochfeld, Inland Steel Company are just examples of companies acquired by Mr Mittal.

Mittal Steel was founded in 2004, based on the same process line, as a result of Ispat International N.V (already controlled by Lakshmi Mittal) acquisition of LNM Holdings N.V. which merged with International Steel group INC.



.

(*)Already controlled by Lakshmi Mittal

Graph 18 – Mittal Steel foundation

Source: Author

With the merger, Mittal Steel had become the world's leading steelmaker.

Placing its headquarters in Rotterdam/Netherlands and being managed from London, Mittal's Steel products were divided in the same three lines as Arcelor's products, however having products with a lower value added (when compared with Arcelor).

Equity was divided in two classes: A and B, where Class B shares have ten voting rights, while class A has only one vote per share. This shares where strongly controlled by Mittal family which had about 88% of outstanding shares and 98% of the voting rights.

In 2005 Mittal Steel acquired Kryvorizhstal (Ukrainian steel manufacturer) for USD 4.8 billion, after a controversial auction process. This acquisition allowed Mittal Steel to increase the existent geographic diversification achieving a favorable position in the Eastern markets, strongly dominated by Eastern companies at that time.

At that time Mittal Steel was the largest steel producer by volume with geographic operations spread along the world with:

- America representing 41% of the business
- Europe 38% (mostly Eastern Europe)
- Some African and Asian countries (such as Kazakhstan, Algeria and South Africa) representing 21%

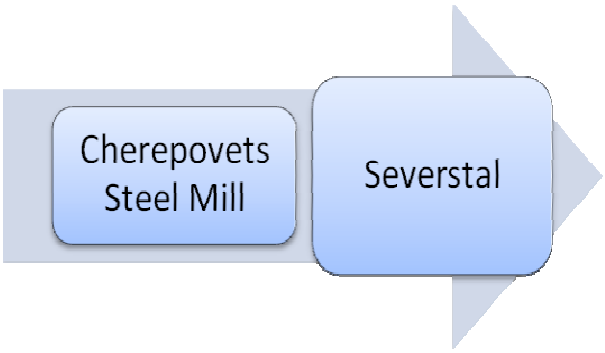
Being also the world's most sufficient steelmaker, where its own mines supplied 56% of the total iron ore and 42% of is coal requirements.

With a production capacity of over 75 million tonnes and an output of 63 million tonnes *(see annex 2 - top steel transformers by output)*. Mittal's sales amounted to USD 28.1 billion, generating an operating margin of 16.9% [*see annex 3 – main steel transformers information in 2005 and annex 5 - Mittal financial data (2003-2005)*].

In 2006 the company had 320,000 employees (10,000 more than Arcelor).

3.3. Severstal S.A

Severstal was a Russian company founded in 24 August 1955 as Cherepovets Steel Mill, and renamed in 24 September 1993 as Severstal S.A. With their headquarters placed in the village of Cherepovets.



Graph 19 – Severstal denomination change
Source: Author

Severstal operated at *downstream* (transformation) and *upstream* (mining) activities, being the Russian largest steel producer.

Although as Cherepovets Steel Mill the business was just centred on the Russian market, as Severstal the company quickly achieved a global position. Severstal owned Severstal North America, U.S fifth largest integrated steel maker and Lucchini, Italian second largest steel group. In addition Severstal also possessed assets in Ukraine, Kazakhstan, United Kingdom and France. All group raw material needs were supported by the mining activities placed in the United States and Russia.

There are two main advantages which Severstal explored:

- Severstal Resources – the mining activities promoted a high level of reserves of coal and iron ore
- As a consequence of this first topic, Severstal was one of the world's lowest cost and most profitable steel producers, generating a higher EBITDA margin (*see annex 3 – main steel transformers information in 2005*)

Severstal S.A was strongly controlled by CEO Mr Alexey Mordashov well related to the Kremlin, owning the preponderant position over company's shares. Severstal strongly felt the economic recession, at that time a *cost reduction* methodology was applied, mainly through

labour costs reduction attitude which was strongly criticized by global newspapers due to the Russian/Cherepovets management style.

In 2006, Severstal employed around 100,000 people, producing 17.6 million of tons of steel, achieving a total sales amount of USD 12,423 million.

4. The Arcelor question

Mittal or Severstal, which one is the more profitable business to Arcelor SA?

Arcelor's Board of Directors strongly opposed to the Mittal's takeover bid, starting to search for some alternatives in order to block this hostile takeover made by its main rival.

In this market perspective, and as a defensive measure, the possibility of merging with Severstal SA had arisen as *"the friendliest merger"* (Guy Dollé – Arcelor CEO 2006). Due to the weak presence of Arcelor in the Russian/Eastern market, merging with the Russian player seamed to be a strong source of competitive advantage. Either Mittal Steel or Severstal SA, combined with Arcelor SA would create the largest steelmaker, but there were some differences between those two options.

1. <u>The merger with Severstal would :</u>

    - Allow the creation of a player with a production capacity around 70 million tonnes, which was a little higher than Mittal's production by itself (63 million tons)

    - Centre 40% of production facilities in two countries with low operational costs: Brazil and Russia (similar in terms of quality of steel produced) promoting a *"shared industrial project between both companies in terms of synergies"* (Financial Times, May 26th, 2006)

    - Build a strong presence in Russia, in Europe and a good position in North American market, mainly in the automotive sector

    - Lead Arcelor to own 68% of the new firm, leaving 32% in the hands of Severstal's spokesmen Alexey Mordashov.

Severstal aimed to became a global company, as Mr Mordashov assumed *"for the first time in Russia's modern history our company can become part of a global company, of the largest player in its field"*.

2. The Mittal's offer would:

- Create a player with a production capacity of 115 million tons, more than 3 times the capacity of the second player (Nippon Steel with a production capacity of 36 million tons)
- Allow the sale of Arcelor high end products into a broader geographic extension, due to Mittal's Steel spread distribution network along the world
- Offer a dominant position in North America, where Mittal had a leadership position after the acquisition of ISG;
- Lead Arcelor to own 55% of the company, leaving 45% over Mr Mittal control

In *Arcelor-Severstal* or *Arcelor-Mittal*, either Mr Mordashov or Mr Mittal would detain a crucial position.

The main difference between these two mergers was that ArcelorMittal's production capacity would be about 65% higher than Arcelor-Severstal, factor of extreme relevance when negotiating with suppliers and clients[49].

In fact, although Russia was the main market for Severstal, Mittal alone had a better position in the Russian market and ArcelorMittal would be the largest steelmaker in every region of the world, even in the Severstal's main market.

Although Severstal mining assets were included in the deal, Mittal was the most self sufficient steelmaker producing products generally with low value added allowing a strong source of raw materials to Arcelor's high end products. About the production facilities, it was true that with Severstal, Arcelor would have production units in the lowest production cost regions: Brazil

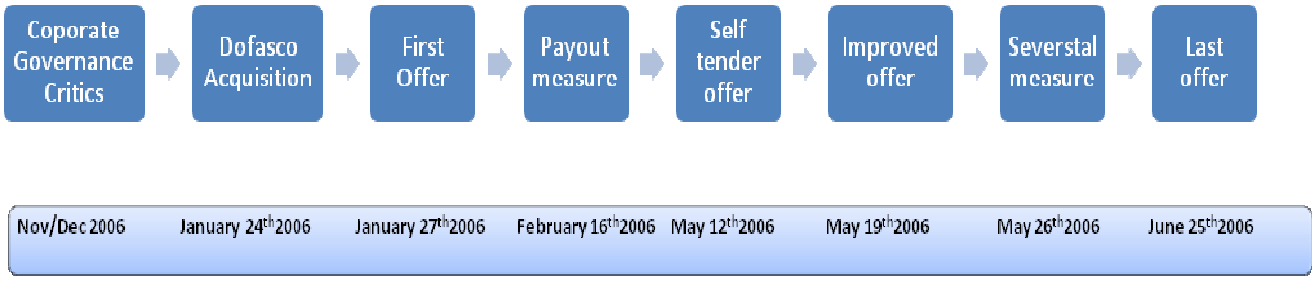
[49] Due to the possible industry concentration and the consequent propensity to obtain synergies related with economies of scale.

and Russia, but the merger with Mittal would have also production units in Brazil and Eastern Europe.

Mittal's bid would create more value to shareholders due to the complementary positions that both companies occupied in the value chain. Mittal was more centred on *upstream operations* and Arcelor stronger on the *downstream* level. Additionally, the largest dimension and broader market dispersion, would position the merged company in a better competitive position to face the market.

5. The process

The business development would be described based on the time frame exposed on the following graph:



Graph 20 – Negotiations between Arcelor and Mittal
Source: Author

5.1. Corporate Governance Critics (November/December 2006)

Different concepts in terms of corporate governance between the two companies were obvious. Mittal was strongly controlled by *Mittal family*, a domination which would prevail after the merger, were they would control "more than 65%" of the merged company. Dominance which was seen as a threat due to problems in the negotiation process as every decision was taken, or strongly influenced, by Mr Mittal (CEO and Chairman of Mittal Steel).

The lack of trust had increased when in the middle of the takeover process it was discovered that three of five Mittal's independent directors had financial links to the CEO of Mittal Steel[50]

Dominance of one individual/family over Mittal contrasted with Arcelor's, where no individual shareholder held more than 6% of Arcelor capital, organization where Chairman and CEO were two independent personalities and no member of the management team was simultaneously a member of the board of directors[51].

Arcelor board of directors strongly opposed to those corporate governance differences and used those disparities as an argument for influencing its shareholders not to tender their shares. Guy Dollé (Arcelor's CEO) defended the Board of directors position stating that they were companies from *"different planets"* accusing Mittal's of *"lack of credibility"*.

5.2. Dofasco acquisition (January 26th 2006)

In order to avoid an undesired *"corporate domination"* Arcelor's Board of Directors noticed that to effectively defend their company defensive measures should take place.

The most remarkably Dofasco acquisition for USD 5.6 billion, after a fierce bidding war against ThyssenKrupp, ended at January, 24th 2006 (3 days before the first Mittal offer). Dofasco was expected to become the Arcelor's platform for growth in North America, promoting an increasing pressure on Mittal's offer.

Dofasco's acquisition had levered Arcelor, as the acquisition value was strongly financed through cash holdings (in addition to some credit lines).

On the other hand, facing Dofasco as a threat, Mr Mittal defended the sale back of Dofasco to ThyssenKrupp group. For Mittal Steel directors, Dofasco integration in the global group would not make a strategic sense *"given the existing extensive and well positioned North American operations"* [www.miitalsteel.com] defending that the holding sale back would allow

[50] Pender J, *"Mittal steel directors have links to founder"*, Financial Times (April 2006)

[51] Only composed by independent directors

to get back the cash expense incurred. For that measure, Mittal had made a pre-agreement with ThyssenKrupp, which Arcelor's Board of Directors strongly opposed to.

At that time another defensive measure took place, without shareholders approval. Arcelor, trying to block Mittal's hostile bid, transferred its Dofasco holding to an independent Dutch foundation, preventing the Canadian company sale for five years.

That was an effective measure as Mittal's takeover risks increased. Mittal was buying Arcelor's assets without having control over them, being impossible to sell Dofasco holding to reduce takeover bid expenses.

Characterized as *"the more efficient defensive measure executed by Arcelor"* and a *"very credible defence"* (Peter Marsh and Peggy Hollinger, Financial Times, April 2006) which had strongly impacted the Mittal's family trust in the takeover success.

Although being a efficient defensive measure it was decided without shareholders approval, reducing the trust of the company *"owners"* on the management team, criticising their ability to run the shareholders interest. The Board of Directors, in any case, should fight for shareholders interests and at that time the requested trust was not felt anymore.

5.3. First offer (January 27th 2006)

Mr Mittal realized that without reducing their impact on the *"hypothetical merged company"* the takeover process would not take place. In order to achieve the process consummation, Mittal Steel accepted to reduce class B voting rights from 10 to 2 and to restructure the Board of Directors with an independent composition.

Although this seems to be a huge step in the process, the reduction of voting rights had no practical effect as in one or another structure, Mittal family would control more than 65%, therefore the power remained centred on the Mittal family launching the first offer in this sequence.

The idea of a voting process of one share/one vote arose when the separation of chairman and CEO was projected. A restructure become imperative in order to have an effective merger Mr

Mittal needed to make some structural changes in Mittal Steel which would strongly impact on the future of Mittal and Arcelor.

But such measures did not affect Arcelor's Board of Director perspective, which continued to identify Mittal Steel corporate governance as a *monarchy*, rejecting the possibility of being incorporated in a company controlled, directly or indirectly, by a *"king"*[52].

5.4. Payout measure – Getting back shareholders trust (February 16th 2006)

Arcelor was a dispersed company, where the major shareholder controlled less than 6%. Its independent Board of Directors always tried to centre their action according to the shareholders[53] interest, approach which, in their perspective, *"cannot be questioned"*.

This methodology was strongly felt when at February, 16th 2006 Arcelor announced a dividend payout of USD 1.41 per each 639.774 million shares outstanding, in order to distribute part of the announced USD 4.53 billion of net profit [*see annex 2 - top steel producers by output and annex 4 - Arcelor financial data (2003-2005)]* pretending to get back the shareholders trust questioned on Dofasco's acquisition as explained on the topic 5.2.

This higher payout ratio trend followed the increase on net profit (from USD 3.17 billion in 2004 to USD 4.53 billion in 2005), transmitting to the market the idea of stronger prosperity when compared to Mittal's results *[see annex 4 - Arcelor financial data (2003-2005) and annex 5 – Mittal financial data (2003-2005)]*

Arcelor's directors, tried to get back the shareholders trust by revelling what seemed to be a prosper company, stating that they would receive greater returns in the coming years[54]. Arcelor CEO, Guy Dollé, also added that "considering our fantastic results and our stock performance, it is a normal payout" [Arcelor strategic plan 2006-2008 – www.arcelormittal.com].

The shield against Mittal's bid was created by a methodology based on:

---

[52] Shareholder of both companies (May 2006), "*They are completely different companies (…) Mittal should aim to be a best practice leader with one share, one vote"*, should *"split the roles of chairman and chief executive, both held by Mr Mittal"*

[53] *"A company made for shareholders"* (member of Arcelor's Board of Directors, www.ft.com)

[54] One month after Mittal's hostile bid, Arcelor presented its strategic plan for the upcoming 3 years, in which it intends to achieve USD7 billions EBITDA. Further, Arcelor commits to pass this imprpved operating performance to shareholders through payout ratio of 30%

"The Higher the net profit" = "The Higher the dividends"

Dividends which should increase (based on future flows) up to USD 2.2 per share.

This strategic plan was named as *"maximum priority shareholders returns"*, and built an additional pressure on Mittal's offer, as the shareholders, due to higher projected returns, started to feel confident about Arcelor's future.

But with all the defensive measures Arcelor was forced to increase its *gearing ratio*[55] borrowing and additional bank loan of around USD 5 billion.

5.5. Self tender offer (May 12th 2006)

The offers evolution can be seen in the *annex 7 – Mittal offer evolution* had changed the odds of success for each side several times. After the improved offer, on May 12th, Arcelor called an extraordinary general meeting of shareholders in order to approve the launch of a self-tender offer of EUR 44 per share amounting EUR 6.5 billions, with the purpose of cancelling the shares tendered. This price presents a premium of 98% to the last trading price before Mittal's offer and a premium of 16.6% to the last bid offered by Mittal (EUR 37.74) as can be seen in the *annex 8 - premiums*

This self tender offer would only be implemented if Mittal offer failed, so it was seen as an alternative when Arcelor gave a premium over the best option. Arcelor offered a higher premium to persuade its shareholders to accept the self tender offer instead of Mittal's bidding, trying to block it.

With the present measure, Arcelor was replacing equity for debt and so swapping discretionary cash outflows, as the payout ratio is determined by Arcelor Board of directors.

With debt, Arcelor does not have the possibility to adjust interest payments so easily in downturns of the steel industry cycle, as it is possible with dividends (equity). Therefore, as leverage increases, its financial profit gets riskier having the possibility of deteriorating Arcelor's credit rating, increasing borrowing costs.

[55] Total Debt/(Total Debt + Equity)

Hence, Arcelor was giving money to its shareholders at the expense of additional risk. Mittal was also giving money, although at that time only EUR 37.74 (latter increased to EUR 40.4) per share. Creating, after the deal consummation, a much larger company that would be in a better financial position to serve the accumulated debt, including the one incurred with the acquisition. The merger would also promote growth opportunities and a much stronger impact that arising from the combined group and promoting an additional return to shareholders.

The self-tender offer would lead to increase on Arcelor net debt of EUR 6.5 billion achieving a total debt amount of about 22.5 billion, increasing the Net debt/EBITDA ratio from 2.4 up to 3.4.

5.6. Improved offer (May 19th 2006)

Although the request of Arcelor shareholders to *Board of Directors* reconsidered Mittal's offer, launched between Arcelor's defensive measures the second offer was effectively defended by the self-tender offer.

5.7. Severstal Meaure (May 26th 2006)

On May 26th, 2006 Arcelor announced what seemed to be the last and definitive defensive measure when, unexpectedly presented the combination with Severstal. The Russian company was the world's 12th biggest steel maker, with 17 millions tonnes produced in 2005. Company which is strongly controlled by its CEO, holding around 90% of outstanding shares, the same problem as with Mittal.

The *Arcelor-Severstal* deal would allow Mr Mordashov to receive 295 million shares at a price of EUR 44, amounting to EUR 13 billion. Severstal's CEO would become, by far, the largest Arcelor shareholder with 38% of equity and would be able to nominate two of four members in Arcelor's strategic committee, which would give to just one person the power of veto.

Severstal had a strong presence in its main market, Russia, where it produced 11 million tonnes. But, mainly focused on the automobile sector, had also production facilities in Europe (Italy, France, UK) with an output of 3 million tonnes and in United States with 3 million[56].

[56] Mainly due to the placement of the plant near the automaker Ford

In terms of value added it presented revenues per tonne of around the same value as Mittal, while Arcelor showed a higher value added to its products. Company's iron ore and coal mines were also considered a value added to this deal.

EUR

	Arcelor	Mittal	Severstal
Price per tonne	700	510	510

Table 5 – Medium price per tonne sold in Euros (2005)

Source: www.arcelor.com and www.arcelormittal.com

In order to take this action Arcelor scheduled to June 30th, 2006 a voting process where the shareholders voted the deal and, unless more than 50% of Arcelor's entire shareholders base opposed it, the merger with Severstal would go through.

This was considered as unacceptable, due to "attendance of Arcelor's shareholders meetings have never in the past exceeded 35%" [Goldman Sach's letter to Arcelor, www.ft.com, (May 2006)].

Arcelor replied stating that *"has gone beyond legal requirements to shareholders"* (Laitne S, *"Arcelor shrugs off criticism over corporate governance", Financial times May 2006)* and is passing the final decision to shareholders.

As it was referred before, Severstal was not seen as a very transparent company, which raised doubts to Arcelor's shareholders about its assets value. Situation which added to the domination applied by Mr Mordashov did not help to build a positive idea about the company.

Arcelor shares facing the perspective of an unorthodox merger reacted negatively dropping 3.9%. A trend which was reversed a few days later, shares rose 6.14%, when some news defended the possibility of changing the decision process to an orthodox one. Shares instability reflected the way shareholders saw the *"suit"* Arcelor-Severstal merger (Marsh P, *"Arcelor faces Severstal suits over merger"*, Financial times June 2006).

Arcelor's *Board of Directors* was facing a difficult stage, after the hostility showed against Mittal's offer based on corporate governance issues, an incoherent position was showed when accepting a company strongly controlled by a *"Kremlin friend" (*Arcelor's shareholders, May 2006) promoting an unrest position among Arcelor shareholders.

Goldman Sachs defended a "normal" voting process in order to decide the Arcelor's future, which in its perspective should consist of *"two-thirds majority vote of all shares present at an extraordinary general meeting of shareholders"(Goldman Sachs's letter to Arcelor's directors*, May 2006, www.ft.com). At that time, a strong instability was felt and some shareholders questioned the share buyback program, raised as a defensive measure.

5.8. Shareholders questions about defensive measures – the perspective change

Institutional shareholders services, which were advising more than 100 of Arcelor's institutional shareholders, said Arcelor the company was running the risk of *"jeopardising future financial stability of the company"* (Bream R, *"Arcelor shareholders to vote against buy-back"*, Financial times June 2006). Additionally, Arcelor's second largest shareholder with 4.3% added his perspective that *"the share buy-back is a transfer of cash from Arcelor to its shareholders, without any value creation"*.

With all those questions raised and feeling the lost of confidence of its shareholders, Arcelor cancelled the General Meeting scheduled to approve the share buy-back program.

All this opposition to Arcelor's practices started to ease its position and for the first time in 4 months the *Board of Directors* accepted to meet Mittal Steel representatives.

As it was expected, after the first meeting Arcelor reiterated its idea that Severstal was the best partner, but the door was open for further talks.

It seemed that finally claims of Arcelor ultimate owners started to be listened and when the rumours that Arcelor would scrap the share buy-back program partially unveiled, it became more evident that if Mittal sweetened its offer it might win this struggle.

Since the first meeting with Arcelor representatives, Mittal maintained secret talks with some Arcelor's shareholders seeking their support. This promoted an increasing number of meetings between Mittal and Arcelor that ended up with the final offer of EUR 40.4 per share valuing Arcelor equity at EUR 26.9 billions, representing an 82% increase since the last trading day prior the initial offer (see *annex 8 – premiums).* This offer compromised a value of EUR 8.5 billion in cash representing 31% of the total offer, being the remaining paid with shares and only by this offer Mittal objectives were achieved, obtaining Arcelor's board of directors recommendation.

It was just missing a final step, which was achieved when Arcelor's shareholders rejected the merger with Severstal[57].

5.9. Third offer (June 25th 2006)

The evolution of Mittal offers had promoted a confrontation between Arcelor's Board of Directors and shareholders.

The defensive measures executed by the Board of Directors after Mittal offers had created some instability between the *Board of Directors* and the shareholders.

This unrest moment ended with the shareholders requesting *Board of Directors* to reconsidered Mittal's offer, after the second offer (May 19th, 2006).

Although, at that time, Mittal had already conquered the major part of Arcelor's shareholders, the board of directors, continued to strongly oppose to the merger with its main rival. Supporting its position on the low value offered by Mittal, assuming the Severstal merger as a *"more attractive alternative from a strategic, financial and essentially social point of view" ("Arcelor rejects Mittal takeover offer"*, www.people.com, May 2006).

After the second offer and as a way to fight back shareholders tendency to tender their shares, the *Board of Directors* stated that it would resign if the Mittal's takeover was approved. This resignation was not well seen, from the acquirer point of view, as this would probably be

[57] Where more than 50% of Arcelor's entire shareholders based voted against the deal

followed by other employees. Leaving Mittal's Directors leading Arcelor's 110,000 employees in 60 countries involved in a production process with much higher value added than Mittal's.

Although this takeover seems to be a huge opportunity for both parties, it would only be a profitable if the projected synergies of USD 1.6 billions were truly obtained and synergies as:

- Marketing and trading activities – the position of Mittal in some emerging markets would allow an expansion in Arcelor's high end products
- Optimization of manufacturing and integration of new technologies
- Savings in selling, general and administrative expenses

Would only be obtained if both companies work together to pursue the same objectives, contributing with their joined expertise to the new company. The resignation of Arcelor *Board of Directors* would strongly compromise the achievement of the desired synergies.

Pretending to achieve this objective, Mittal Steel suggested a final offer, increasing the offered price, but also promoting strong changes in all the corporate governance initiatives.

At this stage Arcelor's *Board of Directors* realized that, having a huge dependency on *upstream* operations, the only way to become a giant steelmaker is to merge with a complementary company. With such measure higher synergies would be obtained through the experience in all value chain.

Analysing both Arcelor's options, an effective and complementary performance would only be possible with ArcelorMittal's merger, as *"Mittal's strategy is mainly volume driven while Arcelor's is margin driven"* (Arcelor's Board of Directors, June 2006). Mittal business was centred in commodity like. With low end products while Arcelor was the main player on high end products.

By that way, although the second offer allowed Mittal to get the desired shareholders trust, the Arcelor's *Board of Directors* resignation was not desired by Mittal and just the final offer obtained their approbation on this acquisition process allowing both companies to share expertise and acquire the expected synergies.

Synergies and both players work on a synchronized way sharing all expertises and knowledge was the reason which lead to the offer of the additional EUR 1.1 billion made in the final offer (turning a hostile acquisition into a friendly merger).

6. Future cash flows estimation

6.1. Enterprise value

In order to gather a detailed information about the main steel players, the author developed a study combining websites described on the *exhibit 3 – main steel transformers financial data* with the 2005 annual reports of each companies, which can be found enclosed in the thesis.

Identifying Arcelor and Mittal as the main industry players, followed by Nippon Steel, the author conjugated the financial data present on the two main players annual reports, since 2003 to 2005 [*exhibit 4 – Arcelor financial data (2003-2005)* and *Exhibit 5 – Mittal financial data (2003-2005)*]. Such information allowed a direct confrontation between this two main steel players, analysing their evolution before 2005. The author concluded that, although Mittal had achieved a higher output level, Arcelor achieved a higher sales value.

The following step was finding out if the combination was the solution to face the market trends and if it had generated any sort of *synergies*.

The annual reports of ArcelorMittal's group from 2006 to 2008 provided information present on the *exhibit 11 – ArcelorMittal financial data (2006*-2008)* and due to the sales growth driven by the merger of 18.74% in the first year, it was assumed a:

- Sales, other costs and amortizations growth at: 20% in 2009, 15% in 2010, 7.5% in 2011, 5% in 2012 and 3% thereafter
- Cost of sales was assumed a growth of: 15% in 2009, 10% in 2010, 5% in 2011 and 3% in the next years
- Invested capital constant growth of 3%
- After the year 2013 the author estimated a perpetual cash flows growth of 3% (i.e. 2% of inflation an 1% of real growth)

In order to calculate the present value of the future cash flows (enterprise value) a WACC (weighted average cost of capital) calculation was needed

$$WACC = \frac{E}{V} * Re + \frac{D}{V} * Rd * (1 - Tc)$$

Where:

Re = cost of equity

Rd = cost of debt

E = market value of the firm's equity

D = market value of the firm's debt

V = E + D

E/V = percentage of financing that is equity

D/V = percentage of financing that is debt

Tc = corporate tax rate

Such calculation assumed:

- Interest expense, net debt and medium tax rate – extracted from the annual report
- Risk free rate (Rf) – As cash flows were estimated in USD, the relevant rate to consider was the U.S treasury bonds (10y)
- Market capitalization – calculated trough the multiplication of the number of shares outstanding by the market value at 31st December of 2008
- Debt rate (Rd) – computed through a ratio between interest expense and net debt deducted by the medium tax rate; value which cannot be lower than the risk free rate
- Market risk premium (Rm-Rf) – following Damodaran assumption = 5,5%
- Sector risk (βu) – was chosen the Beta Steel (general)
- In this calculation the Beta was adjusted due to the instability years which promoted an exponential growth of this value

The enterprise value of the future cash flows calculated was USD 672,739 million, to which was added to the market value of cash and cash equivalents and deducted the market value of debt arrive at the equity value of ArcelorMittal as can be seen on the *exhibit 15 - ArcelorMittal future cash flows (projection).*

In order to estimate synergies valuation a *"Summed company"* a virtual company assuming that both companies were still operate independently, summing the results generated by each of them.

For the *"Summed company"* it was assumed a constant growth of the sales, cost of sales, other operational costs and invested capital at 3%, except on the first year where due to the high investments it was assumed a growth of 12% in 2006[58]. A special WACC (weighted average cost of capital) was requested to estimate the enterprise value of the future cash flows.

The WACC for the "Summed company" was calculated using the same formula:

$$WACC = \frac{E}{V} * Re + \frac{D}{V} * Rd * (1 - Tc)$$

But with some differences, as two companies with different enterprise values and debt level were considered. To solve such a problem the global WACC was calculated based on the market value of the two companies (see *exhibit 12 – WACC assumptions*).

The enterprise value of future cash flows projected (after 2007) was USD 166,718 million.

[58] Enterprise value just concern the cash flows after 2006, by this way such growth is not considered on EV value but impact on the projection of such cash flows

6.2. Synergies

As distinguished on the topic 9 of the first chapter, there are several kinds of synergies. ArcelorMittal merger had promoted several synergies, from financial to operational synergies being the main synergy promoted by the increasing level of sales which strongly impacted the terminal value.

ArcelorMittal expected synergies amounted to USD 423,521 Million which the author split into the three kinds of synergies early described.

	Value	Percentage of Total Synergies
+ Sales Synergies (Growth Synergies)	284.256	-
- Changes on Invested Capital(*)	-39.521	-
= Growth Synergies	244.736	57,8%
+ Cost Synergies (Operational Synergies)	20.587	4,9%
+ WACC Synergies (Financial Synergies)	158.198	37,4%
= Total Synergies	423.521	100,0%

(*) Changes on Invested Capital promoted by the merger

Table 6 – ArcelorMittal kinds of synergies expected

Source: Author

Operational synergies generated by the merger, had promoted a change on Mittal's production methodology, adding more value to the steel extracted from its mines amounting to USD 20,587 million, 4.9% of total synergies.

Financial synergies, can be assessed through the differences on WACC (weighted average cost of capital), which decreased after the merger. The value amounted to USD 158,198 million, 37.4% of the total synergies.

But the main source of expected value creation was transmitted by the increase of sales promoted by the merger, due to the entry of Arcelor SA high end products on markets early dominated by Mittal Steel. Such kind of synergies amounted to USD 284,256 million, which were deducted by changes on Invested Capital in order to assess growth synergies. Growth synergies amount 244,726 million, 57.8% of the total synergies.

7. The Risks Associated with ArcelorMittal Merger – "Future Fears"

7.1. The integration problem in ArcelorMittal's growth

Developing a historical analysis, until the acquisition process where ArcelorMittal was created, both companies growth was mainly based on acquisitions. As their predecessors, ArcelorMittal based its growth in the same methodology.

To make this growth methodology sustainable, acquired companies need to be strongly controlled, in operational and financial terms.

The new company needs to integrate newly acquired assets with the existent operations by:

- Promoting continuous training and global company knowledge
- Realizing the expected cost savings – Not only by the strong leadership position which allows an increase in the bargaining power over suppliers but also by the requested efficiency increase
- Increasing revenues synergies and other synergic benefits

Although, until now, the integration process has so far proceeded smoothly, further integration steps may not be achieved to the fullest expected extension, which could have a material adverse effect on ArcelorMittal's operational results.

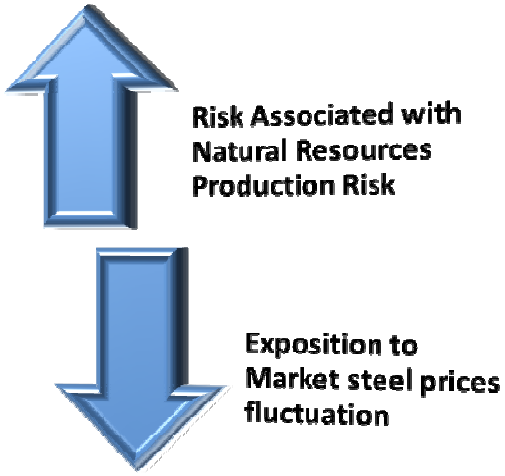
Failing the integration of basic functions, such as best practices integration or the standardization of management information systems, could interfere in some activities and divert management's attention from the daily operations of ArcelorMittal's core businesses. If in the long run these issues are not be taken into account than the merger expectations could not be fully achieved.

7.2. Independency on upstream operations – strength or a weakness

In operational terms, ArcelorMittal's growth and constant tendency to increase its independency at *upstream* operations brought a substantial increase on mining operations, where Mittal Steel had already a strong presence. Such increase brought a high exposition to risks associated with natural resources extraction, risk exposition which was added to the existent risk of development and production of steel.

The consummation of any of these risks could result in production shortfalls or other damages to property or employees. Working hazards related with mining activities described in (see annex 9 – mining risks associated with ArcelorMittal) can have a strong impact on ArcelorMittal production cycle.

If by one way the market dependency decreases, by the other exposition to natural resources production increases.



Graph 21 – Main advantage and disadvantage on increasing mining activities

Source: Author

7.3. Geographical risk

Strongly present in several emerging countries like Poland, Czech Republic, Brazil, China, Algeria or Argentina and applying its model, ArcelorMittal achieves a *low cost* production. But operating in those countries exposes the company to risks.

Eastern European countries are, nowadays[59], collecting the revenues from the economic reforms imposed when they tried to access to the European Union. Argentina, after periods of strong instability, is trying to recover the political stability and improve economic performance. China is not anymore a country only explored by foreigner investors and some strong domestic players started to arise, conquering not only the Chinese market but the global market.

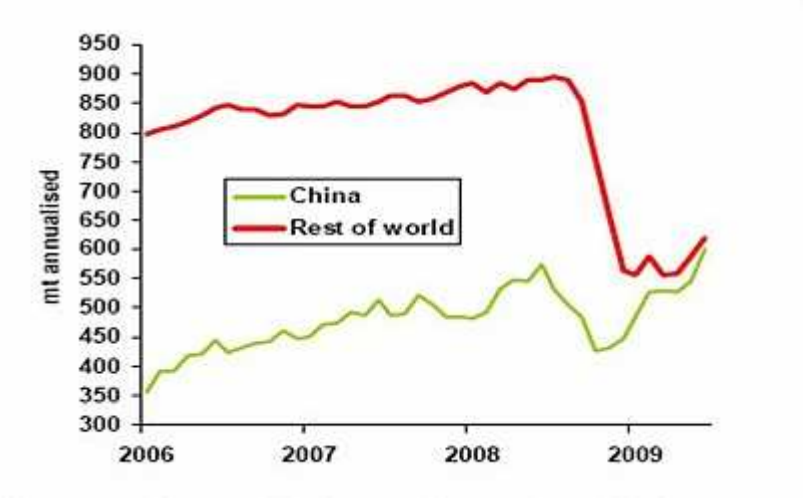
[59] Which slows down with the recent world financial crisis

In some sectors of these economies legal, social and political systems tend to remain underdeveloped and deterioration.

By investing in those countries ArcelorMittal highly increases its exposure to economic and political risks. By this way, any slowdown in the development of these economies or any legal/political crisis will strongly impact the ArcelorMittal's financial and operational structure.

Situation to which can be added the large amount of investments made in those countries, assuming that the exponential growth and modernization will continue, leaving room for an increasing demand for ArcelorMittal's products.

Failing of this assumption started, due to the financial crisis, to be felt by ArcelorMittal. Although in the years after the takeover of Arcelor by Mittal the demand in these countries for steel and steel products increased, the more recent trend shows a decreasing on demand which can be critical for the organizational future prosperity.



Graph 22 – Demand for steel (China against Rest of world)
Source: Worldsteel, WSD, Macquarie research

7.4. People risk

With the merger ArcelorMittal became a huge employer with more than 311,000 employees, spread from the 5 continents *(see annex 10 – number of employees by segment)*.

Arcelor and Mittal together had boosted their production and revenues[60]. On one hand, increasing costs are controlled through the bargaining power over suppliers and other stakeholders achieved with the merger promoting a cutback in production costs. On the other hand some costs cannot be totally controlled on the long run. Pension, other *post-retirement*[61] benefit plans and other cash contributions at some of ArcelorMittal's subsidiaries may increase in the future (reducing the cash available for ArcelorMittal's business). Such costs, due to the uncertainty involved, could be significantly higher than currently estimated amounts.

7.5. Downgrade risk

Financially Mittal tried to increase its level of indebtedness through the takeover process, achieving a stable financial position, pretending in the long run a possible upgrade in credit rating, with the perspective of a decrease on financial costs.

Although some investors fear a downgrade after Mittal's acquisition of Arcelor, being surprised when in the end of 2007 (beginning of 2008) Standard & Poor's raised ArcelorMittal long term corporate credit rating from "BBB" to "BBB+" with a stable outlook. Moddy's investors service upgraded its rating from Baa3 to Baa2 (recently dropped to Baa3 again) and Fitch affirmed its rating of ArcelorMittal at "BBB" and revised its long-term IDR[62] outlook from stable to positive. Since the acquisition process, ArcelorMittal is trying to balance its growth between equity and debt, keeping the same D/E ratio along the recent years.

	ArcelorMittal D/E Ratio
2006	1,2434
2007	1,1715
2008	1,2470

Table 6 – ArcelorMittal D/E ratio

Source:Author & ArcelorMittal reports (2006,2007&2008)

[60] Growth synergies

[61] At December 31, 2007, the value of ArcelorMittal pension in U.S plan assets was USD 2,627 million, while the projected benefit obligation was USD 3,078 million

[62] Issuer Default Rating

Future credit rating downgrades, resulting from exogenous factors (cyclical downturn in the steel industry) or endogenous factors (specific factors within ArcelorMittal) can produce a strong impact on ArcelorMittal's financial situation as any rating decline would increase ArcelorMittal's cost of borrowing and could harm its financial condition.

With a credit downgrade the level of debt outstanding could compromise ArcelorMittal's future, including impairing its ability to request additional financing for the main organizational financial items, like working capital, capital expenditures or even the financial basis for exploring acquisitions market.

In addition, a relevant part of ArcelorMittal's borrowings (current) are linked to variable interest rates and, by this way, exposed to interest rate risk. With the expected rise on interest rates, the financial costs would raise simultaneously.

7.6. Foreign Exchange risks

Other risk associated with ArcelorMittal is the portion of debt denominated in Euro. Such limitation, added to the different currencies in which ArcelorMittal deals, substantially increases the risk associated with currency fluctuation. Any fluctuation in the Euro and, in particular, a further appreciation of the EUR/USD would mechanically increase ArcelorMittal's debt level.

ArcelorMittal also has a relevant part of its revenues in USD and exchange rates against the currencies of the countries, in which ArcelorMittal operates, could have a strong adverse financial impact.

7.7. Capital Expenditures risk

Another financial threat is due to the high level of Capital Expenditures in which ArcelorMittal has based its growth, those investments and other commitments made in the past can limit the future operational flexibility.

7.8. Dominant shareholder risk

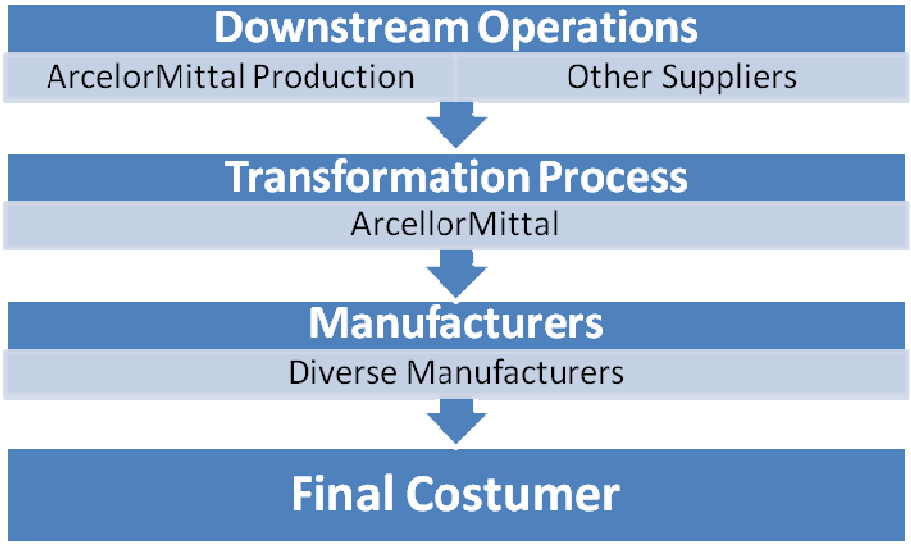
Another risk which can compromise ArcelorMittal's generation of future cash flows is Mr Lakshmi Mittal significant influencing power[63] over decisions adopted on ArcelorMittal general shareholders meetings.

With the acquisition of Arcelor by Mittal, although the President and Chief Executive Officer of ArcelorMittal have lost a fraction of their functions *(see annex 7 – Mittal offer evolution)* Mr Lakshmi Mittal influencing power remains high.

On a first approach it seems to be the better option, as Mr Mittal contributed significantly to shaping and implementing the business strategy of Mittal Steel and subsequently ArcelorMittal. Mr Lakshmi strategic/global vision was essential to create the largest steel group and erasing its position and *"charismatic influence"* could have a material adverse impact, with lack of belonging feeling in some subsidiaries.

7.9. ArcelorMittal distribution process risk

ArcelorMittal flow chart can be described on the following graph:



Graph 22 – ArcelorMittal flow chart

Source: Author

[63] Owning by himself 44% of the total outstanding voting rights

Major external manufacturers are engaged to sell a wide range of end products. In addition, ArcelorMittal's products are used in certain safety-critical applications. If ArcelorMittal products were sold on an inconsistent specification related with the order or the requirements of the application, significant disruptions to the customer's production lines could result. There may also result some significant damages resulting from the use of such products.

Due to the ArcelorMittal limited amount of product liability insurance coverage, a major claim for damages related to products sold could leave ArcelorMittal on an uncomfortable position. Uninsured against a portion or the entire award such situation can compromise its financial condition and future operating results.

7.10. Political risk

7.10.1. Associated with sales

Being a global firm with operations and sales split through the world, ArcelorMittal is highly exposed to trade actions and the settlement of new barriers. As any kind of restriction related with International market trade, actions or regulations or trade legal proceedings will affect organizational potential to sell its products.

7.10.2. Associated with resources requirements

With the merger process both companies tried to reduce its dependency over the commodity demand strongly controlled by Chinese players, although the dependency was reduced, becoming a stronger player brought an increase in supply needs and the market dependency problem was not solved as it was expected.

Political risks become more relevant due to this insufficiency at *upstream* operations. ArcelorMittal's stability may be affected by any restrictions or trade union imposed by the major steel producers *(see annex 2 – top steel producers by output).* Any trade actions may produce a materially adverse effect on ArcelorMittal's business by reducing or eliminating its access to steel markets and by this way retrench production levels.

7.11. Efficient integration risk

As their predecessors ArcelorMittal growth methodology (through acquisitions or mergers) promoted a centralization of several corporate and management functions[64] at its corporate headquarters in Luxembourg.

Although this seems to be an easy and obvious process trend, if ArcelorMittal is not able to centralize its functions successfully, the centralization process and required changes in its operational model may have a strong impact on operational and financial efficiency.

ArcelorMittal cannot fail to integrate newly acquires not only in terms of managing their assets, but also through managing liabilities integration. Being also relevant to manage the future expected growth, which failure could significantly harm ArcelorMittal's future results and require significant expenditures to address the additional operational control requirements of this growth. By this way operational control needs to be increased in order to control all the subsidiaries.

7.12. Assets held for sale

Looking carefully to the balance sheet and analysing the annual report, can be seen that ArcelorMittal has some assets held for sale (page 74 ArcelorMittal Annual report).

If the company is not able to sell them at least at their book value, it would negatively impact the Cash Flow generation process.

7.13. Steel industry

Expectations of a recession in the United States, added to an uncertainty increase in the credit markets strongly impacted Europe and other countries, made consumer confidence decrease, situation which worsen with the concretization of the expected economic downturn.

Such problems added to a highly cyclical industry strongly affected by economic conditions and other factors such as production capacity, fluctuations in steel imports and exports can put at risk ArcelorMittal's future.

[64] Such as central sale of raw materials, purchase/sale of finished products, R&D functions between others

About sales of finish steel products, the market is strongly sensitive to trends imposed by the related industries such as construction, machinery, transportation, which are some of the most important markets for the products of ArcelorMittal.

If the macroeconomic conditions worsen, maintaining the steel demand on a low level, steel transformers performance will be strongly affected.

The global markets in which steel players are placed had become highly competitive. Although being competition positive to the final costumer, by influencing the market to reduce prices or increasing quality. If ArcelorMittal is unable to face this competition threat it could have an adverse financial impact.

On the other hand input costs, strongly manipulated by the Chinese emergency explained in the topic 2.1, in addition to the rising cost of key inputs like other metallic, energy and some transportation costs brought recently an increasing challenge for steel producers.

The historic of the steel industry shows the existence of some over-capacity problems. Excess capacity tends to intensify price competition, this may require a price reduction on ArcelorMittal products and, consequently, may have an adverse effect, influencing its financial condition, as its products contain a high value added.

8. Conclusions

The present thesis has the main purpose of identifying, describing and commenting the main issues around mergers and acquisitions activity, linking such issues with a remarkable process which promoted a significant industrial change. The author selected ArcelorMittal case, an uncommon and unexpected deal, as a way to study a situation where the market leader of a highly dispersed industry (at *downstream* and *upstream* levels) acquired its nearest competitor, achieving an *hegemonic* and stable position on the market which started to be strongly dominated by Chinese and Indian players.

The thesis development was not only focused on the financial perspective but also assessed general management issues, describing the defensive measures and how they impacted on the Mittal's bid on Arcelor, in addition to some recommendations for the future of the merged company.

To reduce this dependency a strong player was needed, and on a dispersed industry just a merger, or an acquisition, involving the two main, or more, industry players would create an effective *competitive advantage*.

In 2005, looking into players competitive advantages, Mittal was seen as the main industry player in terms of output, while Arcelor was the company with a higher value added in is steel products and Severstal was a the major Russian steel company with a strong impact on Eastern markets.

The market was requesting for a change, and Arcelor high end production fitted well either with Mittal's or Severstal's production, both with high outputs but with low value added. At that time and being Mittal the main player in terms of output, the combination Arcelor-Mittal emerged as the solution and a takeover was launched by Mittal Company.

Although the growth strategy of the two companies was similar (mainly based on acquisitions and some mergers - Mittal creation is an example) they are completely different companies according to Arcelor CEO (Mr Guy Dollé) perspective *"from different planets"*. While Arcelor's major shareholder just owned 5.6% of total shares, Mittal family was responsible for 98% of voting right of Mittal Steel.

In this situation Arcelor Board of Directors, defended that, as a way to enter in Eastern market, the major Russian steel producer Severstal was *"the friendliest merger"*.

Arcelor combined either with Severstal or with Mittal would create the largest steelmaker:

- Severstal offer would create a player with a production capacity around 70 million tons
- Mittal offer would make a player with a production capacity of more than 115 million tons (more than three times the production of the second largest steelmaker – Nippon Steel)

Although Mittal was the better option the differences between these two companies delayed the deal consummation.

To all those differences was added a main issue: in Mittal deal Arcelor was the acquired company while on Severstal business Arcelor was the acquirer.

After all the defensive measures executed by Arcelor which compromised its financial stability, the combination with Mittal ended up as being considered by Arcelor's Board of Directors as the *"better solution"*.

After the merger acceptance at 25th June of 2006, the author projected the future cash flows generated by the merged company, based on the annual reports of ArcelorMittal Company of 2007 and 2008, arriving at the enterprise value of USD 672,739 million.

At that time another question arises. Is the merger a better solution for both companies instead of continuing to have independent ownerships and management activities?

To answer this question the author created a "Summed company", considering the sum of the future cash flows of both companies if they still operated independently one from another, in order to calculate the enterprise value.

The author developed an incremental analysis in order to assess the value of the synergies generated by the merger, deducting the value of the *"Summed Company"* from the value of the future cash flows of the *merged company*, achieving a value around USD 423,521 million.

Such value, in the author opinion can be disaggregated into the sources where it was created: growth synergies (Sales synergies), operational synergies (cost savings synergies) and financial synergies (promoted by the decreasing on the discount factor).

Such synergies were estimated as:

- 57.8% growth synergies
- 4.9% operational synergies
- 37.4% financial synergies

The author concluded that the main source of synergies came from an increasing volume of sales promoted by the merger, as Arcelor's high end products entered on the market dominated by Mittal Steel.

But ArcelorMittal future synergies are not assured, the economic and politic instability linked with external factors such as the increasing risks (promoted by increasing operations) at *upstream* level can strongly impact the operational activity, promoting a strong financial impact within the organization. Financial risks may also arise from future downgrades which may strongly compromise the future of ArcelorMittal.

Having their main sales based on USD (United States Dollars) and holding activities placed on several countries, ArcelorMittal is also highly exposed to exchange rate risks, on the valuation executed by the author a constant rate between USD and other currencies was assumed, but due to the market fluctuation such assumption shall not be verified.

However the main issue which can compromise ArcelorMittal's future is the dominance exerted by one person over organizational decisions. Removing Mr Mittal from the *"decision positions"* may lead to a employees belonging loss, his dominance may also compromise the organizational ability to generate *synergies*.

Some synergies where already achieved and both companies were successfully integrated, but the future is not clear and issues such as corporate governance, environmental change, exchange rates, must be closely followed.

Bibliography

Books & Monographs

Coase R.H (1937), the nature of the firm

Ferreira, Domingos; F*usões, aquisições e reestruturações de empresas Vol I*; Colecção Sílabo Gestão

Ferreira, Domingos; F*usões, aquisições e reestruturações de empresas Vol II*; Colecção Sílabo Gestão

Handy C.B (1985), *Understanding Organizations 3rd Edn Harmondsworth*, Penguin Books

Hofstede Geert, *Cultures and organizations: Software of the mind*, McGraw-Hill

Hofstede Geert, *Culture's consequences: International differences in work-related values*, Sage Publications

Hofstede Geert, *Masculinity and Femininity: The Taboo Dimension of National Cultures*, Sage Publications

Hofstede Geert; *Uncommon Sense about Organizations: Cases, Studies and Field Observations;* Sage Publications

Jacquemin A, *Welfare Aspects of Industrial Markets*, Nijenrode studies in economics Vol I

Jacquemin A, *Welfare Aspects of Industrial Markets*, Nijenrode studies in economics Vol II

Montana P. and Charnov B (2008), *Management (4th ed.)*, Barrons Educational Series

Neumann K, *Perspectives on Operations research*, Business and Economics

Ouchi William G, *Theory Z: how American business can meet the Japanese challenge*

Ouchi, William G. (2009). *The Secret of TSL: The Revolutionary Discovery That Raises School Performance*, Copyrighted material

Valente Helder, *Fusões e aquisições regulação e finanças das empresas*, Vida económica

Williamson Oliver E (1975), *Markets and Hierarchies: Analysis and Antitrust* Implications

Press & scientific publications

Atallah Gamal (2007), *Monopolization through endogenous vertical mergers*, Research in Economics 61 pp.99–104

Barmeyera C, Mayrhoferb U (2008), *the contribution of intercultural management to the success of international mergers and acquisitions*, International Business Review 17pp. 28–38

Berkovich E and Narayanan M.P (1993), *Motives for takeover: an empirical investigation*, Journal of finance and quantitative analysis Volume 28 Nº 3 September

Berkovitch E and Narayanan M, *Competition and the medium of exchange in takeovers***,** School of Business Administration: the University of Michigan

Berkovitch E and Narayanan M.P (1993), *Motives for takeovers: an empirical investigation*, Journal of Financial and Quantitative Analysis, Volume 28 Nº 3

Bernstein N A (1967), t*he Coordination and Regulation of Movements,* Oxford, New York: Pergamon Press

Bertrand O and Zuniga P (2006), *R&D and M&A: Are cross-border M&A different? An investigation on OECD countries*, International Journal of Industrial Organization 24 pp.401–423

Bjorvatn K (2004), *Economic integration and the profitability of cross-border mergers and acquisitions*, European Economic Review 48 pp.1211 – 1226

Cossey B (1991), *Systems Assessment in Acquired Subsidiaries*

Cummins J. David and Xie Xiaoying (2008), *Mergers and acquisitions in the US property-liability insurance industry: Productivity and efficiency effects*, Journal of Banking & Finance 32 pp.30–55

Eisenhardt M K (1989), *Agency theory: An assessment and review,* Academy of Management Review, 14(1) pp.57

Fama Eugene F, *Agency Problems and the Theory of the Firm,* The Journal of Political Economy, Vol. 88, No. 2. (Apr., 1980), pp. 288-307

Graves D (1986), *Corporate Cultures*, St Martin′s Press, New York, NY

Harford J (2005), What drives merger waves?, Journal of Financial Economics 77 pp.529–560

Hart J and Vince P (2002), *inexperienced banks and interstate mergers*, Journal of Economics and Business 54 pp.313–330

Haynes Michelle and Thompson Steve (1999), *the productivity effects of bank mergers: Evidence from the UK building societies*, Journal of Banking & Finance 23

Hijzena A, Gorg H, Manchind M (2008), *Cross-border mergers and acquisitions and the role of trade costs*, European Economic Review 52 pp.849–866

Hitt Michael A, King David, Krishnan Hema, Makri Marianna, Schijven Mario, Shimizu K, Zhu H; *Mergers and acquisitions: Overcoming pitfalls, building synergy, and creating value*; Kelley School of Business

Jacquemin A and Margaret E. Slade (1989); *Cartels, collusion and Horizontal mergers*; Chapter 7 in the Handbook of Industrial Organization, Vol. I, R Schmalensee and R Willig (Eds) Amsterdam, North-Holland, 1989, pp. 415–473

Jensen, M.C and W.H. Meckling (1976); *Theory of the firm: managerial behavior, agency costs and ownership structure*; Journal of Financial Economics 3, pp. 305–360

Leger Pierre-Majorique and Quach Louis (2009), *Post-merger performance in the software industry: Theimpact of characteristics of the software product portfolio*, Technovation 29, pp. 704–713

Liu Wanderley and Fehling M (2006), *A practice-based modeling and analysis of social systems: Evaluating resistance-coping strategies in mergers and acquisitions*, Simulation Modelling Practice and Theory 14 360–384

Loverde L (1990), *Technology Driven Deals in Mergers and Acquisitions: How Are They Different?* the Corporate Growth Report

Martynova M and Renneboog L (2008), *Spillover of corporate governance standards in cross-border mergers and acquisitions*, Journal of Corporate Finance 14, pp. 200–223

Murphy M G, Davey K M (2002); *Ambiguity, ambivalence, and indifference in organizational values*; Human Resource Management Journal Vol. 12, pp. 17–32

Nagin D, Rebitzer J B, Sanders S, Taylor L J (2002); *Monitoring, motivation, and management: Determinants of opportunistic behavior in a field experiment*; The American Economic Review Vol 92, pp. 850–873

Palmatier Robert W, Miao C. Fred and Fang Eric (2007); *Sales channel integration after mergers and acquisitions: A methodological approach for avoiding common pitfalls;* Industrial Marketing Management 36, pp. 589–603

Petmezas D (2009), What drives acquisitions? Market valuations and bidder performance, J of Multi Fin. Management 19, pp. 54–74

Porter Michael E (1987), *"From Competitive Advantage to Corporate Strategy"*, Harvard Business Review, May/June 1987, pp 43-59

Porter Michael E. (1980), *Competitive Strategy*, Free Press New York

Rhéaume L and Bhabra H S (2008), *Value creation in information-based industries through convergence: A study of U.S. mergers and acquisitions between 1993 and 2005*, Information & Management 45, pp. 304–311

Robinson S.L and Morrison E.W (2000), *the development of psychological contract breach and violation: A longitudinal study*, Journal of Organizational Behaviour Vol. 21, pp. 46-525

Roll R, Nikas A and Bodt (2005); *Hubris, learning and M&A decisions*; Finance, Anderson Graduate School of Management, UC Los Angeles

Rosenberg R (1987), *Network Trauma: Making Ends Meet When Two Firms Merge*, Data Communications, pp. 102–111

Rossi S and Volpin P F (2004), *Cross-country determinants of mergers and acquisitions*, Journal of Financial Economics 74, pp. 277–304

Rumelt R (1974); Strategy, Structure and Economic Performance; Harvard Business School Division of Research

Spector P E and Fox S (2002), *an emotion-centered model of voluntary work behavior: Some parallels between counterproductive work behavior and organizational citizenship behavior*, Human Resource Management Review Vol 12 pp. 269–292

Stanton J M (2000); *Reactions to employee performance monitoring: Framework, review, and research directions*; Human Performance Vol 13, pp. 85–113

Waldman David A and Javidan Mansour (2009), *Alternative forms of charismatic leadership in the integration of mergers and acquisitions*, The Leadership Quarterly 20, pp. 130–142

Williamson Oliver E, 1985, *The Economic Institutions of Capitalism: Firms, Markets, Relational contracting*, New York: Free press

Williamson Oliver E, Winter Sidney G, *The Nature of the Firm: Origins, Evolution, and Development* (co-edited with Sidney Winter), Oxford University Press, 1991

Thesis

Lopes Sara; *Fusões e aquisições na perspective internacional: consequências económicas e implicações para as regras da concorrência;* Master thesis in economics (Universidade de Coimbra)

Rodrigues Vasco; *Fusões, intervenção pública e mercados pelo controlo de empresas;* Master thesis in economics (Universidade de Economia do Porto)

Ferreira, Manuel Anibal; *Building and leveraging knowledge capabilities through cross-boarder acquisitions, the effect of Multinational Corporation's;* University of Utah

Websites

Http://www.arcelormittal.com
Http://www.arcelormittal.com
Http://www.arcelormittal.com
Http://www.bloomberg.com
Http://www.bottomlinesolutions.com/articles/operational-synergy.htm
Http://www.damodaran.com
Http://www.depts.washington.edu/jfqa/
Http://www.escholarship.org
Http://www.emeraldinsight.com
Http://www.eur-lex.europa.eu
Http://www.europa.eu
Http://www.evraz.com
Http://www.ft.com/
Http://www.google.com/finance
Http://www.homepage.univie.ac.at/
Http://www.internationaltradecommodities.suite101.com/article.cfm/us_steel_imports_exports
Http://www.investing.businessweek.com
Http://www.investorwords.com
Http://www.jfe-steel.co.jp
Http://www.kitcometals.com
Http://www.lme.com/
Http://www.lmo.co.uk
Http://www.mittalsteel.com
Http://www.nsc.co.jp
Http://www.posco.com/
Http://www.sciencedirect.com/
Http://www.severstal.com
Http://www.steel.org

Http://www.steelonthenet.com/files/steel_costs.htm

Http://www.steel-portugal.com/

Http://www.stolaf.edu

Http://www.ussteel.com

Http://www.vernimmen.com

Http://www.wikipedia.com

Http://www.yahoofinance.com

Exhibits

1. Exhbith regulations

1.1. Clayton's Act

The Clayton Antitrust Act is comprised of 12, 13, 14-19, 20, 21, 22-27 of Title 15.

Some sections have been edited or eliminated because of space concerns.

Note also that 13a, 13b, and 21a comprise the "Robinson-Patman Price Discrimination Act" (1936). Sections 15c-15h, and 18a compromise part of the "Hart-Scott-Rodino Antitrust Improvements Act of 1976."

Sec. 13. Discrimination in price, services, or facilities (2 of the Clayton Act)

(a) Price; selection of customers

It shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality, where either or any of the purchases involved in such discrimination are in commerce, where such commodities are sold for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, and where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them: Provided, That nothing herein contained shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered: Provided, however, That the Federal Trade Commission may, after due investigation and hearing to all interested parties, fix and establish quantity limits, and revise the same as it finds necessary, as to particular commodities or classes of commodities, where it finds that available purchasers in greater quantities are so few as to render differentials on account thereof unjustly discriminatory or primitive of monopoly in any line of commerce; and the foregoing shall then not be construed to permit differentials based on

differences in quantities greater than those so fixed and established: And provided further, That nothing herein contained shall prevent persons engaged in selling goods, wares, or merchandise in commerce from selecting their own customers in bona fide transactions and not in restraint of trade: And provided further, That nothing herein contained shall prevent price changes from time to time where in response to changing conditions affecting the market for or the marketability of the goods concerned, such as but not limited to actual or imminent deterioration of perishable goods, obsolescence of seasonal goods, distress sales under court process, or sales in good faith in discontinuance of business in the goods concerned.

(b) Burden of rebutting prima-facie case of discrimination

Upon proof being made, at any hearing on a complaint under this section, that there has been discrimination in price or services or facilities furnished, the burden of rebutting the prima-facie case thus made by showing justification shall be upon the person charged with a violation of this section, and unless justification shall be affirmatively shown, the Commission is authorized to issue an order terminating the discrimination: Provided, however, That nothing herein contained shall prevent a seller rebutting the prima-facie case thus made by showing that his lower price or the furnishing of services or facilities to any purchaser or purchasers was made in good faith to meet an equally low price of a competitor, or the services or facilities furnished by a competitor.

(c) Payment or acceptance of commission, brokerage, or other compensation

It shall be unlawful for any person engaged in commerce, in the course of such commerce, to pay or grant, or to receive or accept, anything of value as a commission, brokerage, or other compensation, or any allowance or discount in lieu thereof, except for services rendered in connection with the sale or purchase of goods, wares, or merchandise, either to the other party to such transaction or to an agent, representative, or other intermediary therein where such intermediary is acting in fact for or in behalf, or is subject to the direct or indirect control, of any party to such transaction other than the person by whom such compensation is so granted or paid.

(d) Payment for services or facilities for processing or sale

It shall be unlawful for any person engaged in commerce to pay or contact for the payment of anything of value to or for the benefit of a customer of such person in the course of such commerce as compensation or in consideration for any services or facilities furnished by or through such customer in connection with the processing, handling, sale, or offering for sale of any products or commodities manufactured, sold, or offered for sale by such person, unless such payment or consideration is available on proportionally equal terms to all other customers competing in the distribution of such products or commodities.

(e) Furnishing services or facilities for processing, handling, etc.

It shall be unlawful for any person to discriminate in favor of one purchaser against another purchaser or purchasers of a commodity bought for resale, with or without processing, by contracting to furnish or furnishing, or by contributing to the furnishing of, any services or facilities connected with the processing, handling, sale, or offering for sale of such commodity so purchased upon terms not accorded to all purchasers on proportionally equal terms.

(f) Knowingly inducing or receiving discriminatory price

It shall be unlawful for any person engaged in commerce, in the course of such commerce, knowingly to induce or receive discrimination in price which is prohibited by this section.

Sec13a. Discrimination in rebates, discounts, or advertising service charges; underselling in particular localities; penalties It shall be unlawful for any person engaged in commerce, in the course of such commerce, to be a party to, or assist in, any transaction of sale, or contract to sell, which discriminates to his knowledge against competitors of the purchaser, in that, any discount, rebate, allowance, or advertising service charge is granted to the purchaser over and above any discount, rebate, allowance, or advertising service charge available at the time of such transaction to said competitors in respect of a sale of goods of like grade, quality, and quantity; to sell, or contract to sell, goods in any part of the United States at prices lower than those exacted by said person elsewhere in the United States for the purpose of destroying competition, or eliminating a

competitor in such part of the United States; or, to sell, or contract to sell, goods at unreasonably low prices for the purpose of destroying competition or eliminating a competitor.

Any person violating any of the provisions of this section shall, upon conviction thereof, be fined not more than USD 5,000 or imprisoned not more than one year, or both.

Sec 13b. Cooperative association; return of net earnings or surplus

Nothing in this Act shall prevent a cooperative association from returning to its members, producers, or consumers the whole, or any part of, the net earnings or surplus resulting from its trading operations, in proportion to their purchases or sales from, to, or through the association.

Sec 13c Exemption of non-profit institutions from price discrimination provisions

Nothing in the Act approved June 19, 1936, known as the Robinson-Patman Antidiscrimination Act, shall apply to purchases of their supplies for their own use by schools, colleges, universities, public libraries, churches, hospitals, and charitable institutions not operated for profit.

Sec 14 Sale, etc., on agreement not to use goods of competitor (§ 3 of the Clayton Act)

It shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies, or other commodities, whether patented or unpatented, for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, or fix a price charged therefor, or discount from, or rebate upon, such price, on the condition, agreement, or understanding that the lessee or purchaser thereof shall not use or deal in the goods, wares, merchandise, machinery, supplies, or other commodities of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, or contract for sale or such condition, agreement, or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce.

Sec 15. Suits by persons injured (4 of the Clayton Act)

(a) Amount of recovery; prejudgment interest

Except as provided in subsection (b) of this section, any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee. The court may award under this section, pursuant to a motion by such person promptly made, simple interest on actual damages for the period beginning on the date of service of such person's pleading setting forth a claim under the antitrust laws and ending on the date of judgment, or for any shorter period therein, if the court finds that the award of such interest for such period is just in the circumstances. In determining whether an award of interest under this section for any period is just in the circumstances, the court shall consider only:

(1) whether such person or the opposing party, or either party's representative, made motions or asserted claims or defenses so lacking in merit as to show that such party or representative acted intentionally for delay, or otherwise acted in bad faith

(2) whether, in the course of the action involved, such person or the opposing party, or either party's representative, violated any applicable rule, statute, or court order providing for sanctions for dilatory behavior or otherwise providing for expeditious proceedings and

(3) whether such person or the opposing party, or either party's representative, engaged in conduct primarily for the purpose of delaying the litigation or increasing the cost thereof.

(b) Amount of damages payable to foreign states and instrumentalities of foreign states

(1) Except as provided in paragraph (2), any person who is a foreign state may not recover under subsection (a) of this section an amount in excess of the actual damages sustained by it and the cost of suit, including a reasonable attorney's fee.

(2) Paragraph (1) shall not apply to a foreign state if -

(A) such foreign state would be denied, under section 1605(a)(2) of title 28, immunity in a case in which the action is based upon a commercial activity, or an act, that is the subject matter of its claim under this section;

(B) such foreign state waives all defences based upon or arising out of its status as a foreign state, to any claims brought against it in the same action;

(C) such foreign state engages primarily in commercial activities; and

(D) such foreign state does not function, with respect to the commercial activity, or the act, that is the subject matter of its claim under this section as a procurement entity for itself or for another foreign state.

Sec 15a Suits by United States; amount of recovery; prejudgment interest (§ 4a of the Clayton Act)

Whenever the United States is hereafter injured in its business or property by reason of anything forbidden in the antitrust laws it may sue therefor in the United States district court for the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by it sustained and the cost of suit. The court may award under this section, pursuant to a motion by the United States promptly made, simple interest on actual damages for the period beginning on the date of service of the pleading of the United States setting forth a claim under the antitrust laws and ending on the date of judgment, or for any shorter period therein, if the court finds that the award of such interest for such period is just in the circumstances. In determining whether an award of interest under this section for any period is just in the circumstances, the court shall consider only -

(1) whether the United States or the opposing party, or either party's representative, made motions or asserted claims or defenses so lacking in merit as to show that such party or representative acted intentionally for delay or otherwise acted in bad faith;

(2) whether, in the course of the action involved, the United States or the opposing party, or either party's representative, violated any applicable rule, statute, or court order providing for sanctions for dilatory behaviour or otherwise providing for expeditious proceedings;

(3) whether the United States or the opposing party, or either party's representative, engaged in conduct primarily for the purpose of delaying the litigation or increasing the cost thereof; and

(4) Whether the award of such interest is necessary to compensate the United States adequately for the injury sustained by the United States.

Sec. 15b. Limitation of actions (4b of the Clayton Act)

Any action to enforce any cause of action under section 15, 15a, or 15c of this title shall be forever barred unless commenced within four years after the cause of action accrued. No cause of action barred under existing law on the effective date of this Act shall be revived by this Act.

Sec. 15c. Actions by State attorneys general (§ 4c of the Clayton Act)

(a) Parents patria; monetary relief; damages; prejudgment interest

(1) Any attorney general of a State may bring a civil action in the name of such State, as parens patriae on behalf of natural persons residing in such State, in any district court of the United States having jurisdiction of the defendant, to secure monetary relief as provided in this section for injury sustained by such natural persons to their property by reason of any violation of sections 1 to 7 of this title. ...

(2) The court shall award the State as monetary relief threefold the total damage sustained as described in paragraph (1) of this subsection, and the cost of suit, including a reasonable attorney's fee. The court may award under this paragraph, pursuant to a motion by such State promptly made, simple interest on the total damage for the period beginning on the date of service of such State's pleading setting forth a claim under the antitrust laws and ending on the date of judgment, or for any shorter period therein, if the court finds that the award of such interest for such period is just in the circumstances. In determining whether an award of interest under this paragraph for any period is just in the circumstances, the court shall consider only -

(A) whether such State or the opposing party, or either party's representative, made motions or asserted claims or defenses so lacking in merit as to show that such party or representative acted intentionally for delay or otherwise acted in bad faith;

(B) whether, in the course of the action involved, such State or the opposing party, or either party's representative, violated any applicable rule, statute, or court order providing for sanctions for dilatory behaviour or other wise providing for expeditious proceedings; and

(C) whether such State or the opposing party, or either party's representative, engaged in conduct primarily for the purpose of delaying the litigation or increasing the cost thereof.

Sec 15d Measurement of damages (4d of the Clayton Act)

In any action under section 15c(a)(1) of this title, in which there has been a determination that a defendant agreed to fix prices in violation of sections 1 to 7 of this title, damages may be proved and assessed in the aggregate by statistical or sampling methods, by the computation of illegal overcharges, or by such other reasonable system of estimating aggregate damages as the court in its discretion may permit without the necessity of separately proving the individual claim of, or amount of damage to, persons on whose behalf the suit was brought.

Sec 17 Antitrust laws not applicable to labour organizations (6 of the Clayton Act)

The labour of a human being is not a commodity or article of commerce. Nothing contained in the antitrust laws shall be construed to forbid the existence and operation of labor, agricultural, or horticultural organizations, instituted for the purposes of mutual help, and not having capital stock or conducted for profit, or to forbid or restrain individual members of such organizations from lawfully carrying out the legitimate objects thereof; nor shall such organizations, or the members thereof, be held or construed to be illegal combinations or conspiracies in restraint of trade, under the antitrust laws.

Sec 18 Acquisition by one corporation of stock of another (7 of the Clayton Act)

No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another person engaged also in commerce or in any activity affecting commerce, where in any

line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.

No person shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of one or more persons engaged in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition, of such stocks or assets, or of the use of such stock by the voting or granting of proxies or otherwise, may be substantially to lessen competition, or to tend to create a monopoly.

This section shall not apply to persons purchasing such stock solely for investment and not using the same by voting or otherwise to bring about, or in attempting to bring about, the substantial lessening of competition. Nor shall anything contained in this section prevent a corporation engaged in commerce or in any activity affecting commerce from causing the formation of subsidiary corporations for the actual carrying on of their immediate lawful business, or the natural and legitimate branches or extensions thereof, or from owning and holding all or a part of the stock of such subsidiary corporations, when the effect of such formation is not to substantially lessen competition.

Nor shall anything herein contained be construed to prohibit any common carrier subject to the laws to regulate commerce from aiding in the construction of branches or short lines so located as to become feeders to the main line of the company so aiding in such construction or from acquiring or owning all or any part of the stock of such branch lines, nor to prevent any such common carrier from acquiring and owning all or any part of the stock of a branch or short line constructed by an independent company where there is no substantial competition between the company owning the branch line so constructed and the company owning the main line acquiring the property or an interest therein, nor to prevent such common carrier from extending any of its lines through the medium of the acquisition of stock or otherwise of any other common carrier where there is no substantial competition between the company extending its lines and the company whose stock, property, or an interest therein is so acquired.

Sec 25 Restraining violations; procedure (15 of the Clayton Act)

The several district courts of the United States are invested with jurisdiction to prevent and restrain violations of this Act, and it shall be the duty of the several United States attorneys, in their respective districts, under the direction of the Attorney General, to institute proceedings in equity to prevent and restrain such violations. Such proceedings may be by way of petition setting forth the case and praying that such violation shall be enjoined or otherwise prohibited. When the parties complained of shall have been duly notified of such petition, the court shall proceed, as soon as may be, to the hearing and determination of the case; and pending such petition, and before final decree, the court may at any time make such temporary restraining order or prohibition as shall be deemed just in the premises. Whenever it shall appear to the court before which any such proceeding may be pending that the ends of justice require that other parties should be brought before the court, the court may cause them to be summoned whether they reside in the district in which the court is held or not, and subpoenas to that end may be served in any district by the marshal thereof.

Sec. 26. Injunctive relief for private parties; exception; costs (16 of the Clayton Act)

Any person, firm, corporation, or association shall be entitled to sue for and have injunctive relief, in any court of the United States having jurisdiction over the parties, against threatened loss or damage by a violation of the antitrust laws, including sections 13, 14, 18, and 19 of this title, when and under the same conditions and principles as injunctive relief against threatened conduct that will cause loss or damage is granted by courts of equity, under the rules governing such proceedings, and upon the execution of proper bond against damages for an injunction improvidently granted and a showing that the danger of irreparable loss or damage is immediate, a preliminary injunction may issue: Provided, That nothing herein contained shall be construed to entitle any person, firm, corporation, or association, except the United States, to bring suit in equity for injunctive relief against any common carrier subject to the provisions of subtitle IV of title 49, in respect of any matter subject to the regulation, supervision, or other jurisdiction of the Interstate Commerce Commission. In any action under this section in which the plaintiff

substantially prevails, the court shall award the cost of suit, including a reasonable attorney's fee, to such plaintiff.

Source: http://www.stolaf.edu/people/becker/antitrust/statutes/clayton.html

1.2. Rule No 4064/89 of 21 December 1989

Council Regulation (EEC) No 4064/89 of 21 December 1989 on the control of concentrations between undertakings

Official Journal L 395 , 30/12/1989 P. 0001 - 0012
Finnish special edition: P. 0082
Swedish special edition: P. 0016

COUNCIL REGULATION (EEC) No 4064/89 of 21 December 1989 on the control of concentrations between undertakings

THE COUNCIL OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic Community, and in particular Articles 87 and 235 thereof,

Having regard to the proposal from the Commission (1),

Having regard to the opinion of the European Parliament (2),

Having regard to the opinion of the Economic and Social Committee (3),

Whereas, for the achievement of the aims of the

Treaty establishing the European Economic Community,

Article 3

(f) Gives the Community the objective of instituting 'a system ensuring that competition in the common market is not distorted';

Whereas this system is essential for the achievement of the internal market by 1992 and its further development;

Whereas the dismantling of internal frontiers is resulting and will continue to result in major corporate re-organizations in the Community, particularly in the form of concentrations;

Whereas such a development must be welcomed as being in line with the requirements of dynamic competition and capable of increasing the competitiveness of European industry, improving the conditions of growth and raising the standard of living in the Community;

Whereas, however, it must be ensured that the process of re-organization does not result in lasting damage to

competition; whereas Community law must therefore include provisions governing those concentrations which may significantly impede effective competition in the common market or in a substantial part of it;

Whereas Articles 85 and 86, while applicable, according to the case-law of the Court of Justice, to certain concentrations, are not, however, sufficient to cover all operations which may prove to be incompatible with the system of undistorted competition envisaged in the Treaty;

Whereas a new legal instrument should therefore be created in the form of a Regulation to permit effective monitoring of all concentrations from the point of view of their effect on the structure of competition in the Community and to be the only instrument applicable to such concentrations;

Whereas this Regulation should therefore be based not only on Article 87 but, principally, on Article 235 of the Treaty, under which the Community may give itself the additional powers of action necessary for the attainment of its objectives, and also with regard to concentrations on the markets for agricultural products listed in Annex II to the Treaty;

Whereas the provisions to be adopted in this Regulation should apply to significant structural changes the impact of which on the market goes beyond the national borders of any one Member State;

Whereas the scope of application of this Regulation should therefore be defined according to the geographical area of activity of the undertakings concerned and be limited by quantitative thresholds in order to cover those concentrations which have a Community dimension; whereas,

at the end of an initial phase of the implementation of this Regulation, these thresholds should be reviewed in the light of the experience gained;

Whereas a concentration with a Community dimension exists where the aggregate turnover of the undertakings concerned exceeds given levels worldwide and throughout

the Community and where at least two of the undertakings concerned have their sole or main fields of activities in different Member States or where, although the undertakings in question act mainly in one and the same Member State, at least one of them has substantial operations in at least one other Member State; whereas that is also the case where the concentrations are effected by undertakings which do not have their principal fields of activities in the Community but which have substantial operations there;

Whereas the arrangements to be introduced for the control of concentrations should, without prejudice to Article 90 (2) of the Treaty, respect the principle of non-discrimination between the public and the private sectors; whereas, in the public sector, calculation of the turnover of an undertaking concerned in a concentration needs, therefore, to take account of undertakings making up an economic unit with an independent power of decision, irrespective of the way in which their capital is held or of the rules of administrative supervision applicable to them;

Whereas it is necessary to establish whether concentrations with a Community dimension are compatible or not with the common market from the point of view of the need to preserve and develop effective competition in the common market; whereas, in so doing, the Commission must place its appraisal within the general framework of the achievement of the fundamental objectives referred to in Article 2 of the Treaty, including that of strengthening the Community's economic and social cohesion, referred to in Article 130a;

Whereas this Regulation should establish the principle that a concentration with a Community dimension which creates or strengthens a position as result of which effective competition in the common market or in a substantial part of it is significantly impeded is to be declared incompatible with the common market;

Whereas concentrations which, by reason of the limited market share of the undertakings concerned, are not liable to impede effective competition may be presumed to be compatible with the common market; whereas, without prejudice to Articles 85 and 86 of the Treaty, an indication

to this effect exists, in particular, where the market share of the undertakings concerned does not exceed 25 % either in the common market or in a substantial part of it;

Whereas the Commission should have the task of taking all the decisions necessary to establish whether or not concentrations of a Community dimension are compatible with the common market, as well as decisions designed to restore effective competition;

Whereas to ensure effective control undertakings should be obliged to give prior notification of concentrations with a Community dimension and provision should be made for the suspension of concentrations for a limited period, and for the possibility of extending or waiving a suspension where necessary; whereas in the interests of legal certainty the validity of transactions must nevertheless be protected as much as necessary;

Whereas a period within which the Commission must initiate a proceeding in respect of a notified concentration and a period within which it must give a final decision on the compatibility or incompatibility with the common market of a notified concentration should be laid down;

Whereas the undertakings concerned must be accorded the right to be heard by the Commission as soon as a proceeding has been initiated; whereas the members of management and supervisory organs and recognized workers' representatives in the undertakings concerned, together with third parties showing a legitimate interest, must also be given the opportunity to be heard;

Whereas the Commission should act in close and constant liaison with the competent authorities of the Member States from which it obtains comments and information;

Whereas, for the purposes of this Regulation, and in accordance with the case-law of the Court of Justice, the Commission must be afforded the assistance of the Member States and must also be empowered to require information to be given and to carry out the necessary investigations in order to appraise concentrations;

Whereas compliance with this Regulation must be enforceable by means of fines and periodic penalty payments; whereas the Court of Justice should be given unlimited jurisdiction in that regard pursuant to Article 172 of the Treaty;

Whereas it is appropriate to define the concept of concentration in such a manner as to cover only operations bringing about a durable change in the structure of the undertakings concerned; whereas it is therefore necessary to exclude from the scope of this Regulation those operations

which have as their object or effect the coordination of the competitive behaviour of independent undertakings, since such operations fall to be examined under the appropriate provisions of Regulations implementing Article 85 or Article 86 of the Treaty; whereas it is appropriate to make this distinction specifically in the case of the creation of joint ventures; Whereas there is no coordination of competitive behaviour within the meaning of this Regulation where two or more undertakings agree to acquire jointly control of one or more other undertakings with the object and effect of sharing amongst themselves such undertakings or their assets;

Whereas the application of this Regulation is not excluded where the undertakings concerned accept restrictions directly related and necessary to the implementation of the concentration;

Whereas the Commission should be given exclusive competence to apply this Regulation, subject to review by the Court of Justice;

Whereas the Member States may not apply their national legislation on competition to concentrations with a Community dimension, unless the Regulation makes provision therefor; whereas the relevant powers of national authorities should be limited to cases where, failing intervention by the Commission, effective competition is likely to be significantly impeded within the territory of a Member State and where the competition interests of that Member State cannot be sufficiently protected otherwise than by this Regulation; whereas the Member States concerned must act promptly in such cases; whereas this Regulation cannot, because of the diversity of national law, fix a single deadline for the adoption of remedies;

Whereas, furthermore, the exclusive application of this Regulation to concentrations with a Community dimension is without prejudice to Article 223 of the Treaty, and does not prevent the Member States' taking appropriate measures to protect legitimate interests other than those pursued by this Regulation, provided that such measures are compatible with the general principles and other provisions of Community law;

Whereas concentrations not referred to in this Regulation come, in principle, within the jurisdiction of the Member States; whereas, however, the Commission should have the power to act, at the request of a Member State concerned, in cases where effective competition would be significantly impeded within that Member State's territory;

Whereas the conditions in which concentrations involving Community undertakings are carried out in non-member countries should be observed, and provision should be made for the possibility of the Council's giving the Commission an appropriate mandate for negotiation with a view to obtaining non-discriminatory treatment for Community undertakings;

Whereas this Regulation in no way detracts from the collective rights of workers as recognized in the undertakings concerned,

HAS ADOPTED THIS REGULATION:

Article 1

Scope

1. Without prejudice to Article 22 this Regulation shall apply to all concentrations with a Community dimension as defined in paragraph 2.

2. For the purposes of this Regulation, a concentration has a Community dimension where;

(a) the aggregate worldwide turnover of all the undertakings concerned is more than ECU 5 000 million, and

(b) the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than ECU 250 million,

Unless each of the undertakings concerned achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State.

3. The thresholds laid down in paragraph 2 will be reviewed before the end of the fourth year following that of the adoption of this Regulation by the Council acting by a qualified majority on a proposal from the Commission.

Article 2

Appraisal of concentrations

1. Concentrations within the scope of this Regulation shall be appraised in accordance with the following provisions with a view to establishing whether or not they are compatible with the common market.

In making this appraisal, the Commission shall take into account:

(a) the need to preserve and develop effective competition within the common market in view of, among other things, the structure of all the markets concerned and the actual or potential competition from undertakings located either within or without the Community;

(b) the market position of the undertakings concerned and their economic and financial power, the opportunities available to suppliers and users, their access to supplies or markets, any legal or other barriers to entry, supply and demand trends for the relevant goods and services, the interests of the intermediate and ultimate consumers, and the development of technical and economic progress provided that it is to consumers' advantage and does not form an obstacle to competition.

2. A concentration which does not create or strengthen a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part of it shall be declared compatible with the common market.

3. A concentration which creates or strengthens a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part of it shall be declared incompatible with the common market.

Article 3

Definition of concentration

1. A concentration shall be deemed to arise where:

(a) two or more previously independent undertakings merge, or

(b) one or more persons already controlling at least one undertaking, or one or more undertakings acquire, whether by purchase of securities or assets, by contract or by any other means, direct or indirect control of the whole or parts of one or more other undertakings.

2. An operation, including the creation of a joint venture, which has as its object or effect the coordination of the competitive behaviour of undertakings which remain independent shall not constitute a concentration within the meaning of paragraph 1 (b).

The creation of a joint venture performing on a lasting basis all the functions of an autonomous economic entity, which does not give rise to coordination of the competitive behaviour of the parties amongst themselves or between them and the joint venture, shall constitute a concentration within the meaning of paragraph 1 (b).

3. For the purposes of this Regulation, control shall be constituted by rights, contracts or any other means which, either separately or jointly and having regard to the considerations of fact or law involved, confer the possibility of exercising decisive influence on an undertaking, in particular by:

(a) ownership or the right to use all or part of the assets of an undertaking;

(b) rights or contracts which confer decisive influence on the composition, voting or decisions of the organs of an undertaking.

4. Control is acquired by persons or undertakings which:

(a) are holders of the rights or entitled to rights under the contracts concerned, or

(b) while not being holders of such rights or entitled to rights under such contracts, have the power to exercise the rights deriving therefrom.

5. A concentration shall not be deemed to arise where:

(a) credit institutions or other financial institutions or insurance companies, the normal activities of which include transactions and dealing in securities for their own account or for the account of others, hold on a temporary basis securities which they have acquired in an undertaking with a view to reselling them, provided that they do not exercise voting rights in respect of those securities with a view to determining the competitive behaviour of that undertaking or provided that they exercise such voting rights only with a view to preparing the sale of all or part of that

undertaking or of its assets or the sale of those securities and that any such sale takes place within one year of the date of acquisition; that period may be extended by the Commission on request where such institutions or companies justify the fact that the sale was not reasonably possible within the period set;

(b) control is acquired by an office holder according to the law of a Member State relating to liquidation, winding up, insolvency, cessation of payments, compositions or analogous proceedings;

(c) the operations referred to in paragraph 1 (b) are carried out by the financial holding companies referred to in Article 5 (3) of the Fourth Council Directive 78/660/EEC of 25 July 1978 on the annual accounts of certain types of companies (4), as last amended by Directive 84/569/EEC (5), provided however that the voting rights in respect of the holding are exercised, in particular in relation to the appointment of members of the management and supervisory bodies of the undertakings in which they have holdings, only to maintain the full value of those investments and not to determine directly or indirectly the competitive conduct of those undertakings.

Article 4

Prior notification of concentrations

1. Concentrations with a Community dimension as referred to by this Regulation shall be notified to the Commission not more than one week after the conclusion of the agreement, or the announcement of the public bid, or the acquisition of a controlling interest. That week shall begin when the first of those events occurs.

2. A concentration which consists of a merger within the meaning of Article 3 (1) (a) or in the acquisition of joint control within the meaning of Article 3 (1) (b) shall be notified jointly by the parties to the merger or by those acquiring joint control as the case may be. In all other cases,

the notification shall be effected by the person or undertaking acquiring control of the whole or parts of one or more undertakings.

3. Where the Commission finds that a notified concentration falls within the scope of this Regulation, it shall publish the fact of the notification, at the same time indicating the names of

the parties, the nature of the concentration and the economic sectors involved. The Commission shall take account of the legitimate interest of undertakings in the protection of their business secrets.

Article 5

Calculation of turnover

1. Aggregate turnover within the meaning of Article 1 (2) shall comprise the amounts derived by the undertakings concerned in the preceding financial year from the sale of products and the provision of services falling within the undertakings' ordinary activities after deduction of sales rebates and of value added tax and other taxes directly related to turnover. The aggregate turnover of an undertaking concerned shall not include the sale of products or the provision of services between any of the undertakings referred to in paragraph 4.

Turnover, in the Community or in a Member State, shall comprise products sold and services provided to undertakings or consumers, in the Community or in that Member State as the case may be.

2. By way of derogation from paragraph 1, where the concentration consists in the acquisition of parts, whether or not constituted as legal entities, of one or more undertakings, only the turnover relating to the parts which are the subject of the transaction shall be taken into account with regard to the seller or sellers.

However, two or more transactions within the meaning of the first subparagraph which take place within a two-year period between the same persons or undertakings shall be treated as one and the same concentration arising on the date of the last transaction.

3. In place of turnover the following shall be used:

(a) for credit institutions and other financial institutions, as regards Article 1 (2) (a), one-tenth of their total assets.

As regards Article 1 (2) (b) and the final part of Article

1 (2), total Community-wide turnover shall be replaced by one-tenth of total assets multiplied by the ratio between loans and advances to credit institutions and customers in transactions with Community residents and the total sum of those loans and advances.

As regards the final part of Article 1 (2), total turnover within one Member State shall be replaced by one-tenth of total assets multiplied by the ratio between loans and

advances to credit institutions and customers in transactions with residents of that Member State and the total sum of those loans and advances;

(b) for insurance undertakings, the value of gross premiums written which shall comprise all amounts received and receivable in respect of insurance contracts issued by or on behalf of the insurance undertakings, including also outgoing reinsurance premiums, and after deduction of taxes and par fiscal contributions or levies charged by reference to the amounts of individual premiums or the total volume of premiums; as regards Article 1 (2) (b) and the final part of Article 1 (2), gross premiums received from Community residents and from residents of one Member State respectively shall be taken into account.

4. Without prejudice to paragraph 2, the turnover of an undertaking concerned within the meaning of Article 1 (2) shall be calculated by adding together the respective turnover of the following:

(a) the undertaking concerned;

(b) those undertakings in which the undertaking concerned, directly or indirectly;

- owns more than half the capital or business assets, or

- has the power to exercise more than half the voting rights, or

- has the power to appoint more than half the members of the supervisory board, the administrative board or bodies legally representing the undertakings, or

- has the right to manage the undertakings' affairs;

(c) those undertakings which have in an undertaking concerned the rights or powers listed in (b);

(d) those undertakings in which an undertaking as referred to in (c) has the rights or powers listed in (b);

(e) those undertakings in which two or more undertakings as referred to in (a) to (d) jointly have the rights or powers listed in (b).

5. Where undertakings concerned by the concentration jointly have the rights or powers listed in paragraph 4 (b), in calculating the turnover of the undertakings concerned for the purposes of Article 1 (2);

(a) no account shall be taken of the turnover resulting from the sale of products or the provision of services between the joint undertaking and each of the undertakings concerned or any other undertaking connected with any one of them, as set out in paragraph 4 (b) to (e);

(b) account shall be taken of the turnover resulting from the sale of products and the provision of services between

the joint undertaking and any third undertakings. This turnover shall be apportioned equally amongst the undertakings concerned.

Article 6

Examination of the notification and initiation of proceedings

1. The Commission shall examine the notification as soon as it is received.

(a) Where it concludes that the concentration notified does not fall within the scope of this Regulation, it shall record that finding by means of a decision.

(b) Where it finds that the concentration notified, although falling within the scope of this Regulation, does not raise serious doubts as to its compatibility with the common market, it shall decide not to oppose it and shall declare that it is compatible with the common market.

(c) If, on the other hand, it finds that the concentration notified falls within the scope of this Regulation and raises serious doubts as to its compatibility with the common market, it shall decide to initiate proceedings.

2. The Commission shall notify its decision to the undertakings concerned and the competent authorities of the Member States without delay.

Article 7

Suspension of concentrations

1. For the purposes of paragraph 2 a concentration as defined in Article 1 shall not be put into effect either before its notification or within the first three weeks following its notification.

2. Where the Commission, following a preliminary examination of the notification within the period provided for in paragraph 1, finds it necessary in order to ensure the full effectiveness of any decision taken later pursuant to Article 8 (3) and (4), it may decide on its own initiative to continue the suspension of a concentration in whole or in part until it takes a final decision, or to take other interim measures to that effect.

3. Paragraphs 1 and 2 shall not impede the implementation of a public bid which has been notified to the Commission in accordance with Article 4 (1) by the date of its announcement, provided that the acquirer does not exercise the voting rights attached to the securities in question or does so only to maintain the full value of those investments and on the basis of a derogation granted by the Commission pursuant to paragraph 4.

4. The Commission may, on request, grant a derogation from the obligations imposed in paragraphs 1, 2 or 3 in order

to prevent serious damage to one or more undertakings concerned by a concentration or to a third party. That derogation may be made subject to conditions and obligations in order to ensure conditions of effective competition. A derogation may be applied for and granted at any time, even before notification or after the transaction.

5. The validity of any transaction carried out in contravention of paragraph 1 or 2 shall be dependent on a decision pursuant to Article 6 (1) (b) or 8 (2) or (3) or by virtue of the presumption established by Article 10 (6).

This Article shall, however, have no effect on the validity of transactions in securities including those convertible into other securities admitted to trading on a market which is regulated and supervised by authorities recognized by public bodies, operates regularly and is accessible directly or indirectly to the public, unless the buyer and seller knew or ought to have known that the transaction was carried out in contravention of paragraph 1 or 2.

Article 8

Powers of decision of the Commission

1. Without prejudice to Article 9, each proceeding initiated pursuant to Article 6 (1) (c) shall be closed by means of a decision as provided for in paragraphs 2 to 5.

2. Where the Commission finds that, following modification by the undertakings concerned if necessary, a notified concentration fulfils the criterion laid down in Article 2 (2), it shall issue a decision declaring the concentration compatible with the common market.

It may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to modifying the original concentration plan. The decision declaring the concentration compatible shall also cover restrictions directly related and necessary to the implementation of the concentration.

3. Where the Commission finds that a concentration fulfils the criterion laid down in Article 2 (3), it shall issue a decision declaring that the concentration is incompatible with the common market.

4. Where a concentration has already been implemented, the Commission may, in a decision pursuant to paragraph 3 or by a separate decision, require the undertakings or assets brought together to be separated or the cessation of joint control or any other action that may be appropriate in order to restore conditions of effective competition.

5. The Commission may revoke the decision it has taken pursuant to paragraph 2 where:

(a) the declaration of compatibility is based on incorrect information for which one of the undertakings concerned is responsible or where it has been obtained by deceit, or

(b) the undertakings concerned commit a breach of an obligation attached to the decision.

6. In the case referred to in paragraph 5, the Commission may take a decision pursuant to paragraph 3, without being bound by the deadline referred to in Article 10 (3).

Article 9

Referral to the competent authorities of the Member States

1. The Commission may, by means of a decision notified without delay to the undertakings concerned and the competent authorities of the other Member States, refer a notified concentration to the competent authorities of the Member State concerned in the following circumstances.

2. Within three weeks of the date of receipt of the copy of the notification a Member State may inform the Commission which shall inform the undertakings concerned that a concentration threatens to create or to strengthen a dominant position as a result of which effective competition would be significantly impeded on a market, within that Member State, which presents all the characteristics of a distinct market, be it a substantial part of the common market or not.

3. If the Commission considers that, having regard to the market for the products or services in question and the geographical reference market within the meaning of paragraph 7, there is such a distinct market and that such a threat exists either:

(a) it shall itself deal with the case in order to maintain or restore effective competition on the market concerned, or

(b) it shall refer the case to the competent authorities of the Member State concerned with a view to the application of that State's national competition law.

If, however, the Commission considers that such a distinct market or threat does not exist it shall adopt a decision to that effect which it shall address to the Member State concerned.

4. A decision to refer or not to refer pursuant to paragraph 3 shall be taken where:

(a) as a general rule within the six-week period provided for in Article 10 (1), second subparagraph, where the

Commission has not initiated proceedings pursuant to Article 6 (1) (b), or

(b) within three months at most of the notification of the concentration concerned where the Commission has initiated proceedings under Article 6 (1) (c), without taking the preparatory steps in order to adopt the necessary measures pursuant to Article 8 (2), second subparagraph, (3) or (4) to maintain or restore effective competition on the market concerned.

5. If within the three months referred to in paragraph 4 (b) the Commission, despite a reminder from the Member State concerned, has taken no decision on referral in accordance with paragraph 3 or taken the preparatory steps referred to in paragraph 4 (b), it shall be deemed to have taken a decision to refer the case to the Member State concerned in accordance with paragraph 3 (b).

6. The publication of any report or the announcement of the findings of the examination of the concentration by the competent authority of the Member State concerned shall be effected not more than four months after the Commission's referral.

7. The geographical reference market shall consist of the area in which the undertakings concerned are involved in the supply of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighboring areas because, in particular, conditions of competition are appreciably different in those areas. This assessment should take account in particular of the nature and characteristics of the products or services concerned, of the existence of entry barriers or of consumer preferences, of appreciable differences of the undertakings' market shares between neighboring areas or of substantial price differences.

8. In applying the provisions of this Article, the Member State concerned may take only the measures strictly necessary to safeguard or restore effective competition on the market concerned.

9. In accordance with the relevant provisions of the Treaty, any Member State may appeal to the Court of Justice, and in particular request the application of Article 186, for the purpose of applying its national competition law.

10. This Article will be reviewed before the end of the fourth year following that of the adoption of this Regulation.

Article 10

Time limits for initiating proceedings and for decisions

1. The decisions referred to in Article 6 (1) must be taken within one month at most. That period shall begin on the day following the receipt of a notification or, if the information to be supplied with the notification is incomplete, on the day following the receipt of the complete information.

That period shall be increased to six weeks if the Commission receives a request from a Member State in accordance with Article 9 (2).

2. Decisions taken pursuant to Article 8 (2) concerning notified concentrations must be taken as soon as it appears that the serious doubts referred to in Article 6 (1) (c) have been removed, particularly as a result of modifications made by the undertakings concerned, and at the latest by the deadline laid down in paragraph 3.

3. Without prejudice to Article 8 (6), decisions taken pursuant to Article 8 (3) concerning notified concentrations must be taken within not more than four months of the date on which the proceeding is initiated.

4. The period set by paragraph 3 shall exceptionally be suspended where, owing to circumstances for which one of the undertakings involved in the concentration is responsible, the Commission has had to request information by decision pursuant to Article 11 or to order an investigation by decision pursuant to Article 13.

5. Where the Court of Justice gives a judgment which annuls the whole or part of a Commission decision taken under this Regulation, the periods laid down in this Regulation shall start again from the date of the judgment.

6. Where the Commission has not taken a decision in accordance with Article 6 (1) (b) or (c) or Article 8 (2) or (3) within the deadlines set in paragraphs 1 and 3 respectively, the concentration shall be deemed declared compatible with the common market, without prejudice to Article 9.

Article 11

Requests for information

1. In carrying out the duties assigned to it by this Regulation, the Commission may obtain all necessary information from the Governments and competent authorities of the Member States,

from the persons referred to in Article 3 (1) (b), and from undertakings and associations of undertakings.

2. When sending a request for information to a person, an undertaking or an association of undertakings, the Commission shall at the same time send a copy of the request to the competent authority of the Member State within the territory of which the residence of the person or the seat of the undertaking or association of undertakings is situated.

3. In its request the Commission shall state the legal basis and the purpose of the request and also the penalties provided for in Article 14 (1) (b) for supplying incorrect information.

4. The information requested shall be provided, in the case of undertakings, by their owners or their representatives and, in the case of legal persons, companies or firms, or of associations having no legal personality, by the persons authorized to represent them by law or by their statutes.

5. Where a person, an undertaking or an association of undertakings does not provide the information requested within the period fixed by the Commission or provides incomplete information, the Commission shall by decision require the information to be provided. The decision shall specify what information is required, fix an appropriate period within which it is to be supplied and state the penalties provided for in Articles 14 (1) (b) and 15 (1) (a) and the right to have the decision reviewed by the Court of Justice.

6. The Commission shall at the same time send a copy of its decision to the competent authority of the Member State within the territory of which the residence of the person or the seat of the undertaking or association of undertakings is situated.

Article 12

Investigations by the authorities of the Member States

1. At the request of the Commission, the competent authorities of the Member States shall undertake the investigations which the Commission considers to be necessary pursuant to Article 13 (1), or which it has ordered by decision pursuant to Article 13 (3). The officials of the competent authorities of the Member States responsible for conducting those investigations shall

exercise their powers upon production of an authorization in writing issued by the competent authority of the Member State within the territory of which the investigation is to be carried out. Such authorization shall specify the subject matter and purpose of the investigation.

2. If so requested by the Commission or by the competent authority of the Member State within the territory of which the investigation is to be carried out, officials of the Commission may assist the officials of that authority in carrying out their duties.

Article 13

Investigative powers of the Commission

1. In carrying out the duties assigned to it by this Regulation, the Commission may undertake all necessary investigations into undertakings and associations of undertakings.

To that end the officials authorized by the Commission shall be empowered:

(a) to examine the books and other business records;

(b) to take or demand copies of or extracts from the books and business records;

(c) to ask for oral explanations on the spot;

(d) to enter any premises, land and means of transport of undertakings.

2. The officials of the Commission authorized to carry out the investigations shall exercise their powers on production of an authorization in writing specifying the subject matter and purpose of the investigation and the penalties provided for in Article 14 (1) (c) in cases where production of the required books or other business records is incomplete. In good time before the investigation, the Commission shall inform, in writing, the competent authority of the Member State within the territory of which the investigation is to be carried out of the investigation and of the identities of the authorized officials.

3. Undertakings and associations of undertakings shall submit to investigations ordered by decision of the Commission. The decision shall specify the subject matter and purpose of the investigation, appoint the date on which it shall begin and state the penalties provided for in

Articles 14 (1) (c) and 15 (1) (b) and the right to have the decision reviewed by the Court of Justice.

4. The Commission shall in good time and in writing inform the competent authority of the Member State within the territory of which the investigation is to be carried out of its intention of taking a decision pursuant to paragraph 3. It shall hear the competent authority before taking its decision.

5. Officials of the competent authority of the Member State within the territory of which the investigation is to be carried out may, at the request of that authority or of the Commission, assist the officials of the Commission in carrying out their duties.

6. Where an undertaking or association of undertakings opposes an investigation ordered pursuant to this Article, the Member State concerned shall afford the necessary assistance to the officials authorized by the Commission to enable them to carry out their investigation. To this end the Member States shall, after consulting the Commission, take the necessary measures within one year of the entry into force of this Regulation.

Article 14

Fines

1. The Commission may by decision impose on the persons referred to in Article 3 (1) (b), undertakings or associations of undertakings fines of from ECU 1 000 to 50 000 where intentionally or negligently:

(a) they omit to notify a concentration in accordance with Article 4;

(b) they supply incorrect or misleading information in a notification pursuant to Article 4;

(c) they supply incorrect information in response to a request made pursuant to Article 11 or fail to supply information within the period fixed by a decision taken pursuant to Article 11;

(d) they produce the required books or other business records in incomplete form during investigations pursuant to Article 12 or 13, or refuse to submit to an investigation ordered by decision taken pursuant to Article 13.

2. The Commission may by decision impose fines not exceeding 10 % of the aggregate turnover of the undertakings concerned within the meaning of Article 5 on the persons or undertakings concerned where, either intentionally or negligently, they;

(a) fail to comply with an obligation imposed by decision pursuant to Article 7 (4) or 8 (2), second subparagraph;

(b) put into effect a concentration in breach of Article 7 (1) or disregard a decision taken pursuant to Article 7 (2);

(c) put into effect a concentration declared incompatible with the common market by decision pursuant to Article 8 (3) or do not take the measures ordered by decision pursuant to Article 8 (4).

3. In setting the amount of a fine, regard shall be had to the nature and gravity of the infringement.

4. Decisions taken pursuant to paragraphs 1 and 2 shall not be of a criminal law nature.

Article 15

Periodic penalty payments

1. The Commission may by decision impose on the persons referred to in Article 3 (1) (b), undertakings or associations of undertakings concerned periodic penalty payments of up to ECU 25 000 for each day of the delay calculated from the date set in the decision, in order to compel them:

(a) to supply complete and correct information which it has requested by decision pursuant to Article 11;

(b) to submit to an investigation which it has ordered by decision pursuant to Article 13.

2. The Commission may by decision impose on the persons referred to in Article 3 (1) (b) or on undertakings periodic penalty payments of up to ECU 100 000 for each day of the delay calculated from the date set in the decision, in order to compel them:

(a) to comply with an obligation imposed by decision pursuant to Article 7 (4) or 8 (2), second subparagraph, or

(b) to apply the measures ordered by decision pursuant to Article 8 (4).

3. Where the persons referred to in Article 3 (1) (b), undertakings or associations of undertakings have satisfied the obligation which it was the purpose of the periodic penalty payment to enforce, the Commission may set the total amount of the periodic penalty payments at a lower figure than that which would arise under the original decision.

Article 16

Review by the Court of Justice

The Court of Justice shall have unlimited jurisdiction within the meaning of Article 172 of the Treaty to review decisions whereby the Commission has fixed a fine or periodic penalty payments; it may cancel, reduce or increase the fine or periodic penalty payment imposed.

Article 17

Professional secrecy

1. Information acquired as a result of the application of Articles 11, 12, 13 and 18 shall be used only for the purposes of the relevant request, investigation or hearing.

2. Without prejudice to Articles 4 (3), 18 and 20, the Commission and the competent authorities of the Member States, their officials and other servants shall not disclose information they have acquired through the application of this Regulation of the kind covered by the obligation of professional secrecy.

3. Paragraphs 1 and 2 shall not prevent publication of general information or of surveys which do not contain information relating to particular undertakings or associations of undertakings.

Article 18

Hearing of the parties and of third persons

1. Before taking any decision provided for in Article 7 (2) and (4), 8 (2), second subparagraph, and (3) to (5), 14 and 15, the Commission shall give the persons, undertakings and associations of undertakings concerned the opportunity, at

every stage of the procedure up to the consultation of the Advisory Committee, of making known their views on the objections against them.

2. By way of derogation from paragraph 1, a decision to continue the suspension of a concentration or to grant a derogation from suspension as referred to in Article 7 (2) or (4) may be taken provisionally, without the persons, undertakings or associations of undertakings concerned being given the opportunity to make known their views beforehand, provided that the Commission gives them that opportunity as soon as possible after having taken its decision.

3. The Commission shall base its decision only on objections on which the parties have been able to submit their observations. The rights of the defence shall be fully respected in the proceedings. Access to the file shall be open at least to the parties directly involved, subject to the legitimate interest of undertakings in the protection of their business secrets.

4. Insofar as the Commission and the competent authorities of the Member States deem it necessary, they may also hear other natural or legal persons. Natural or legal persons showing a legitimate interest and especially members of the administrative or management organs of the undertakings concerned or recognized workers' representatives of those undertakings shall be entitled, upon application, to be heard.

Article 19

Liaison with the authorities of the Member States

1. The Commission shall transmit to the competent authorities of the Member States copies of notifications within three working days and, as soon as possible, copies of the most important documents lodged with or issued by the Commission pursuant to this Regulation.

2. The Commission shall carry out the procedures set out in this Regulation in close and constant liaison with the competent authorities of the Member States, which may express their views upon those procedures. For the purposes of Article 9 it shall obtain information from the competent

authority of the Member State as referred to in paragraph 2 of that Article and give it the opportunity to make known its views at every stage of the procedure up to the adoption of a decision pursuant to paragraph 3 of that Article; to that end it shall give it access to the file.

3. An Advisory Committee on concentrations shall be consulted before any decision is taken pursuant to Articles

8 (2) to (5), 14 or 15, or any provisions are adopted pursuant to Article 23.

4. The Advisory Committee shall consist of representatives of the authorities of the Member States. Each Member State shall appoint one or two representatives; if

unable to attend, they may be replaced by other representatives. At least one of the representatives of a Member State shall be competent in matters of restrictive practices and dominant positions.

5. Consultation shall take place at a joint meeting convened at the invitation of and chaired by the Commission. A summary of the facts, together with the most important documents and a preliminary draft of the decision to be taken for each case considered, shall be sent with the invitation. The meeting shall take place not less than 14 days after the invitation has been sent. The Commission may in exceptional cases shorten that period as appropriate in order to avoid serious harm to one or more of the undertakings concerned by a concentration.

6. The Advisory Committee shall deliver an opinion on the Commission's draft decision, if necessary by taking a vote. The Advisory Committee may deliver an opinion even if some members are absent and unrepresented. The opinion shall be delivered in writing and appended to the draft decision. The Commission shall take the utmost account of the opinion delivered by the Committee. It shall inform the Committee of the manner in which its opinion has been taken into account.

7. The Advisory Committee may recommend publication of the opinion. The Commission may carry out such publication. The decision to publish shall take due account of the legitimate interest of undertakings in the protection of their business secrets and of the interest of the undertakings concerned in such publication taking place.

Article 20

Publication of decisions

1. The Commission shall publish the decisions which it takes pursuant to Article 8 (2), where conditions and obligations are attached to them, and to Article 8 (2) to (5) in the Official Journal of the European Communities.

2. The publication shall state the names of the parties and the main content of the decision; it shall have regard to the legitimate interest of undertakings in the protection of their business secrets.

Article 21 Jurisdiction

1. Subject to review by the Court of Justice, the Commission shall have sole competence to take the decisions provided for in this Regulation.

2. No Member State shall apply its national legislation on competition to any concentration that has a Community dimension.

The first subparagraph shall be without prejudice to any Member State's power to carry out any enquiries necessary for the application of Article 9 (2) or after referral, pursuant

to Article 9 (3), first subparagraph, indent (b), or (5), to take the measures strictly necessary for the application of Article

9 (8).

3. Notwithstanding paragraphs 1 and 2, Member States may take appropriate measures to protect legitimate interests other than those taken into consideration by this Regulation and compatible with the general principles and other provisions of Community law.

Public security, plurality of the media and prudential rules shall be regarded as legitimate interests within the meaning of the first subparagraph.

Any other public interest must be communicated to the Commission by the Member State concerned and shall be recognized by the Commission after an assessment of its compatibility with the general principles and other provisions of Community law before the measures referred

to above may be taken. The Commission shall inform the Member State concerned of its decision within one month of that communication.

Article 22

Application of the Regulation

1. This Regulation alone shall apply to concentrations as defined in Article 3.

2. Regulations No 17 (6), (EEC) No 1017/68 (7), (EEC) No 4056/86 (8) and (EEC) No 3975/87 (9) shall not apply to concentrations as defined in Article 3.

3. If the Commission finds, at the request of a Member State, that a concentration as defined in Article 3 that has no Community dimension within the meaning of Article 1 creates or strengthens a dominant position as a result of which effective competition would be significantly impeded within the territory of the Member State concerned it may, insofar as the concentration affects trade between Member States, adopt the decisions provided for in Article 8 (2), second subparagraph, (3) and (4).

4. Articles 2 (1) (a) and (b), 5, 6, 8 and 10 to 20 shall apply. The period within which the proceedings defined in Article 10 (1) may be initiated shall begin on the date of the receipt of the request from the Member State. The request must be made within one month at most of the date on which the concentration was made known to the Member State or effected. This period shall begin on the date of the first of those events.

5. Pursuant to paragraph 3 the Commission shall take only the measures strictly necessary to maintain or restore effective competition within the territory of the Member State at the request of which it intervenes.

6. Paragraphs 3 to 5 shall continue to apply until the thresholds referred to in Article 1 (2) have been reviewed.

Article 23

Implementing provisions

The Commission shall have the power to adopt implementing provisions concerning the form, content and other details of notifications pursuant to Article 4, time limits pursuant to Article 10, and hearings pursuant to Article 18.

Article 24

Relations with non-member countries

1. The Member States shall inform the Commission of any general difficulties encountered by their undertakings with concentrations as defined in Article 3 in a non-member country.

2. Initially not more than one year after the entry into force of this Regulation and thereafter periodically the Commission shall draw up a report examining the treatment accorded to Community undertakings, in the terms referred to in paragraphs 3 and 4, as regards concentrations in non-member countries. The Commission shall submit those reports to the Council, together with any recommendations.

3. Whenever it appears to the Commission, either on the basis of the reports referred to in paragraph 2 or on the basis of other information, that a non-member country does not grant Community undertakings treatment comparable to that granted by the Community to undertakings from that non-member country, the Commission may submit proposals to the Council for the appropriate mandate for negotiation with a view to obtaining comparable treatment for Community undertakings.

4. Measures taken pursuant to this Article shall comply with the obligations of the Community or of the Member States, without prejudice to Article 234 of the Treaty, under international agreements, whether bilateral or multilateral.

Article 25

Entry into force

1. This Regulation shall enter into force on 21 September 1990.

2. This Regulation shall not apply to any concentration which was the subject of an agreement or announcement or where control was acquired within the meaning of Article

4 (1) before the date of this Regulation's entry into force and it shall not in any circumstances apply to any concentration in respect of which proceedings were initiated before that date by a Member State's authority with responsibility for competition.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 21 December 1989.

For the Council

The President

E. CRESSON

Note: The statements entered in the Council minutes relating to this Regulation will be published later in the Official Journal of the European Communities.

Source: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31989R4064:EN:HTML

2. Exhibit top steel transformers by output

Million metric tons of crude steel output

	2005	2006	2007	2008
Arcelor	46,70	-	-	-
Mittal	63,00	-	-	-
ArceloMittal	-	-	116,40	103,30
Nippon Steel	32,00	32,70	35,70	37,50
Baosteel Group	22,70	22,50	28,60	35,40
Posco	30,50	30,10	31,10	34,70
Hebei Steel Group	NA	NA	22,80	33,30
JFE	29,90	32,00	34,00	33,00
Wuhan Steel Group	13,00	13,80	20,20	27,70
Tata Steel	18,20	18,30	26,60	24,40
Jiangsu Shagang Group	10,50	14,60	NA	23,30
U.S Steel	19,30	21,20	21,50	23,20

Source: www.wikipedia.com and www.scribd.com

3. Exhibit main steel transformers financial data (2005)

		Arcelor (31-12-2005)	Mittal (31-12-2005)	Nippon Steel (31-03-2006)	JFE Holdings (31-03-2006)	POSCO (31-12-2005)	US Steel (31-12-2005)	Corus (31-12-2005)	Severstal (31-12-2005)
Millions of USD	Revenues	38.438	28.132	33.259	26.376	26.041	14.039	17.444	9.775
Millions of USD	EBITDA	6.649	5.575	6.467	5.893	7.620	1.740	1.772	2.458
Millions of USD	EBIT	5.158	4.746	4.906	4.403	6.023	1.439	1.170	2.320
Millions of USD	Net Profit	4.533	3.365	2.928	2.775	3.972	910	776	1.696
Millions of USD	Net Profit (Before Minority Interests)	5.042	3.885	3.060	2.808	3.966	947	778	1.760
Millions of USD	Total Debt	21.550	19.058	23.502	19.429	7.565	6.466	7.851	6.937
Millions of USD	Net Debt	16.075	16.909	22.138	19.152	6.918	4.992	6.353	4.667
Millions of USD	Equity	20.784	11.984	15.170	11.475	19.670	3.356	5.811	8.397
Millions of USD	Total Assets	42.334	31.042	38.672	30.904	27.235	9.822	13.662	15.334
Millions of USD	Fixed Assets (Long Term Assets)	21.447	19.330	25.863	20.988	15.710	4.991	7.051	9.342
Millions of USD	Market capitalization	15.798	18.770	24.067	19.796	15.840	5.450	NA	9.215
Millions of USD	NWC Needs (*)	5.537	4.282	1.039	227	5.906	852	2.567	1.553
Millions of USD	Pre tax Income	5.232	4.703	4.815	4.335	5.434	1.312	998	2.316
	Medium Tax Rate = (Tax/Pre Tax Income)(**)	8,92%	14,10%	39,47%	35,30%	29,34%	27,82%	31,03%	25,40%
	EBITDA margin	17,30%	19,82%	19,44%	22,34%	29,26%	12,39%	10,16%	25,15%
	Operating Margin	13,42%	16,87%	14,75%	16,69%	23,13%	10,25%	6,71%	23,74%
	Total Debt/EBITDA	3,24	3,42	3,63	3,30	0,99	3,72	4,43	2,82
	Net Debt/EBITDA	2,42	3,03	3,42	3,25	0,91	2,87	3,59	1,90
	Debt to equity	103,69%	159,03%	154,92%	169,31%	38,46%	192,67%	135,11%	82,61%
	Gearing(***)	50,90%	61,39%	60,77%	62,87%	27,78%	65,83%	57,47%	45,24%
Millions	Number of shares - Shares outstanding	639,77	712,89	6.731,18	587,24	79,20	113,38	NA	930,80
USD	Earning (net profit) per share	$7,09	$4,72	$0,43	$4,73	$50,15	$8,03	NA	$1,82
USD	Dividends per share	$1,41	$0,40	$0,08	$0,88	$1,98	$0,40	$0,09	$0,37
USD	Earnings (EBITDA) per share	$10,39	$7,82	$0,96	$10,03	$96,21	$15,35	Group	$2,64
	Shares price (dec 31th, 2005)	$24,69	$26,33	$3,58	$33,71	$200,00	$48,07	$5,07	$9,90
	P/E multiple	3,48	5,58	8,22	7,13	3,99	5,99	NA	5,43
	P/E Multiple(EBITDA)	2,38	3,37	3,72	3,36	2,08	3,13	NA	3,75
	ROIC	17,41%	17,27%	11,04%	13,43%	19,69%	17,78%	8,39%	15,89%
	ROA	12,18%	15,29%	12,69%	14,25%	22,12%	14,65%	8,56%	15,13%
	EV/EBITDA	4,79	6,40	7,14	6,61	2,99	6,00	NA	5,65

NA - Not Available

(*) NWC needs = (Current Assets - Cash and Cash Equivalents) - (Current Liabilities -Short Term Debt)
(**) Defered Taxes and Minority Interests considered
(***) Gearing = Total Debt/(Equity+Total Debt)

Sources:

Annual Report of all the companies in 2005 and 2006
www.bloomberg.com
http://investing.businessweek.com
www.google.com/finance
www.yahoofinance.com
www.arcelormittal.com

1USD - JPY	117,47	31-03-2006
1USD - JPY	117,87	31-12-2005
1USD - KRW	1010,00	31-12-2005
1USD - EUR	0,8484	31-12-2005
1USD - GBP	0,5813	31-12-2005

Notes:

In POSCO Minority Interests are Summed
In Severstal there are also loss from Discounted Operations (Considered)

4. Exhibit Arcelor financial data (2003-2005)

		Arcelor (31-12-2003)	Arcelor (31-12-2004)	Arcelor (31-12-2005)
Millions of USD	Revenues	30.555	35.568	38.438
Millions of USD	EBITDA	2.626	5.258	6.649
Millions of USD	EBIT	870	3.906	5.158
Millions of USD	Net Profit	303	2.699	4.533
Millions of USD	Net Profit (Before Minority Interests)	490	3.174	5.042
Millions of USD	Total Debt	21.069	21.550	21.550
Millions of USD	Net Debt	18.841	16.785	16.075
Millions of USD	Equity	7.936	14.412	20.784
Millions of USD	Total Assets	29.005	35.962	42.334
Millions of USD	Fixed Assets (Long Term Assets)	14.840	17.993	21.447
Millions of USD	Market capitalization	9.142	14.651	15.642
Millions of USD	NWC Needs (*)	8.197	6.578	5.537
Millions of USD	Invested Capital (Fixed Assets + NWC)	23.036	24.571	26.985
	WACC	7,56%	7,93%	8,09%
	Pre tax Income	657	3.779	5.232
	Defered Taxes	-112	-180	277
	Medium Tax Rate = (Tax/Pre Tax Income) (**)	8,26%	11,23%	8,92%
Millions of USD	Number of Shares outstanding	533,04	639,77	639,77
USD	Shares price (dec 31th, 2005)	$17,15	$22,90	$24,45
	ROIC	3,46%	14,11%	17,41%
	ROA	3,00%	10,86%	12,18%

(*) NWC needs = (Current Assets - Cash and Cash Equivalents) - (Current Liabilities -Short Term Debt)

(**) Defered Taxes and Minority Interests considered

5. Exhbit Mittal financial data (2003-2005)

		Mittal (31-12-2003)	Mittal (31-12-2004)	Mittal (31-12-2005)
Millions of USD	Revenues	9.567	22.197	28.132
Millions of USD	EBITDA	1.630	6.969	5.575
Millions of USD	EBIT	1.299	6.416	4.746
Millions of USD	Net Profit	1.182	4.701	3.365
Millions of USD	Net Profit (Before Minority Interests)	1.217	5.316	3.885
Millions of USD	Total Debt	7.315	11.564	19.058
Millions of USD	Net Debt	6.415	8.930	16.909
Millions of USD	Equity	2.822	7.589	11.984
Millions of USD	Total Assets	10.137	19.153	31.042
Millions of USD	Fixed Assets (Long Term Assets)	6.454	9.528	19.330
Millions of USD	Market capitalization	5.737	24.843	18.773
Millions of USD	NWC Needs (*)	944	1.102	4.282
Millions of USD	Invested Capital (Fixed Assets + NWC)	7.398	10.630	23.612
	WACC	7,70%	7,62%	7,98%
	Pre tax Income	1.400	6.133	4.703
	Defered Taxes	-141	-86	-155
	Medium Tax Rate = (Tax/Pre Tax Income) (**)	3,00%	11,92%	14,10%
Millions of USD	Number of Shares outstanding	646,74	642,77	712,98
USD	Shares price (dec 31th, 2005)	8,87	38,65	26,33
	ROIC	17,03%	53,16%	17,27%
	ROA	12,81%	33,50%	15,29%

(*) NWC needs = (Current Assets - Cash and Cash Equivalents) - (Current Liabilities -Short Term Debt)

(**) Defered Taxes and Minority Interests considered

6. Exhibit Arcelor + Mittal financial data (2003-2005)

		Arcelor + Mittal (31-12-2003)	Arcelor + Mittal (31-12-2004)	Arcelor + Mittal (31-12-2005)
Millions of USD	Revenues	40.122	57.765	66.570
Millions of USD	EBITDA	4.256	12.227	12.224
Millions of USD	EBIT	2.169	10.322	9.904
Millions of USD	Net Profit	1.485	7.400	7.898
Millions of USD	Net Profit (Before Minority Interests)	1.707	8.490	8.927
Millions of USD	Total Debt	28.384	33.114	40.608
Millions of USD	Net Debt	25.256	25.715	32.984
Millions of USD	Equity	10.758	22.001	32.768
Millions of USD	Total Assets	39.142	55.115	73.376
Millions of USD	Fixed Assets (Long Term Assets)	21.294	27.521	40.777
Millions of USD	Market capitalization	14.878	39.494	34.415
Millions of USD	NWC Needs (*)	9.141	7.680	9.819
Millions of USD	Invested Capital (Fixed Assets + NWC)	30.434	35.201	50.597
	WACC	7,61%	7,77%	8,03%
	Pre tax Income	2.057	9.912	9.935
	Defered Taxes	-253	-266	122
	Medium Tax Rate = (Tax/Pre Tax Income) (**)	29,28%	17,03%	8,92%
Millions of USD	Number of Shares outstanding (***)	1.385	1.385	1.385
USD	Shares price (dec 31th, 2005)	10,74	28,51	24,84
	ROIC	5,04%	24,33%	17,83%
	ROA	5,54%	18,73%	13,50%

(*) NWC Needs = (Current Assets - Cash and Cash Equivalents) - (Current Liabilities -Short Term Debt)
(**) Defered Taxes and Minority Interests considered
(***) Number of Shares After the Merger (2006)

Sources:

Annual Report of Arcelor SA and Mittal Steel in 2003, 2004 and 2005
www.bloomberg.com
www.google.com/finance
www.yahoofinance.com
www.arcelormittal.com

1USD - JPY	117,47	31-03-2006
1USD - JPY	117,87	31-12-2005
1USD - KRW	1020,73	31-12-2005
1USD - EUR	0,8484	31-12-2005
1USD - GBP	0,5813	31-12-2005

7. Exhibit Mittal offer evolution

Initial offer January 27th, 2006:

Mittal Steel be offering to acquire all outstanding Arcelor ordinary shares and arecelor Convertible Bonds (2017 OCEANEs), as follow:

- 4 Mittal Steel shares and €35.25 for each 5 Arcelor shares
- 4 new Mittal Steel shares and €40 for every 5 Arcelor Convertible Bond

Or, instead of this cash and share offer, holders may elect the following combination provided that 75% of the tender Arcelor shares are exchanged for new Mittal Steel shares and 25% are exchanged for cash:

- €28.21 per Arcelor share, or
- 16 new Mittal shares for every 15 Arcelor shares

The completion of the offer will be subject to the following conditions:

- Number of Arcelor shares tendered to the offer presents more than 50% of the total share capital and voting rights
- Shares of Mittal Steel approve the acquisition of Arcelor
- During the offer period, no exceptional events occur and Arcelor does not take any actions that alter Arcelor's substance

Additionally to this offer, Mittal Steel agrees:

- Reduce class B share's voting rights from 10 to 2
- Maintain a majority of independent directors on its Board of Directors
- Sell Dofasco to ThyssenKrupp for € 3.8 billions
- Launch a takeover bid for Arcelor Brasil and Acesita

Improved offer, May 19th, 2006

Under the improved offer, Mitall Steel will be offering to acquire outstanding Arcelor ordinary shares and Arcelor Convertible Bonds (2017 OCEANEs), as follows:

- 1 Mitall Steel share and €11.1 for each Arcelor ordinary share (the amount of cash being reduced to €10.05 upon a payment by Arcelor of the announced €1.85 in dividend)
- 1 Mitall Steel shares and €12.12 (to be increased by €0.80 upon distribution by Arcelor of its announced ordinary dividend) for each Arcelor Convertible Bond

Or, instead of this cash and share offer, holders may elect the following combination provided that 70.6% of the tender Arcelor shares are exchanged for new Mittal Steel shares and 29.4% are exchanged for cash:

- 17 new Mittal Steel shares for 12 Arcelor shares (such ratio should become 1.3773 new Mittal Steel shares for each Arcelor share upon payment by Arcelor of the announced €1.85 dividends, or
- €37.74 in cash for each Arcelor share (the amount of cash being reduced to €36.69 upon payment by Arcelor of the announced €1.85 dividends

Additionally to the initial offer, Mittal Steel agrees to further reduce in voting rights to one share – one vote structure and the Board of Directors composition will be made of equal number of Arcelor and Mittal elements

Final offer, June 25th, 2006

Under the improved offer, Mitall Steel will be offering to acquire outstanding Arcelor ordinary shares and Arcelor Convertible Bonds (2017 OCEANEs), as follows:

- 13 Mittal Steel shares and €150.60 for each 12 Arcelor shares
- 13 new Mittal Steel shares and €188.42 for 12 Arcelor Convertible Bond

This offer valued Arcelor shares at €40.40 and its shareholders will have the rights to receive a cash stock mix in any proportion the elect, provided that 31% pf the aggregate consideration paid is paid in cash and 69% in stock. The maximum amount of cash to be paid by Mittal Steel will be approximately €8.5 billions

8. Exhibit premiums

	Premiums				
	Arcelor price (€)	Initial offer	Improved offer	Final offer	Self tender offer
Offer per share price		28,21	37,74	40,4	44
Last closing price (26th January)	22,22	27%	70%	82%	98%
3 months prior avg.	20,59	36%	83%	96%	114%
1 year prior avg.	18,14	55%	108%	123%	143%
All times high	22,22	27%	70%	82%	98%

Source: www.mittalsttel.com

9. Exhibit mining risks associated with ArcelorMittal

Mining operations are subject to hazards and risks normally associated with the exploration, development and production of natural resources, any of which could result in production shortfalls or damage to persons or property. In particular, hazards associated with open-pit mining operations include, among others:

- flooding of the open pit
- collapse of the open-pit wall
- accidents associated with the operation of large open-pit mining and rock transportation equipment
- accidents associated with the preparation and ignition of large-scale open-pit blasting operations
- production disruptions due to weather and
- Hazards associated with the disposal of mineralized waste water, such as groundwater and waterway contamination.

Hazards associated with underground mining operations include, among others:

- underground fires and explosions, including those caused by flammable gas
- cave-ins or falls of ground
- discharges of gases and toxic chemicals
- flooding
- sinkhole formation and ground subsidence
- other accidents and conditions resulting from drilling and
- Blasting and removing, and processing material from, an underground mine.

ArcelorMittal is at risk of experiencing any or all of these hazards. For example, in September 2006, a methane gas explosion at ArcelorMittal's Lenina mine in Kazakhstan resulted in 41 fatalities and a production shutdown of two days to fully investigate the incident and in January 2008, a methane gas explosion at ArcelorMittal's Abaiskaya mine in Kazakhstan resulted in 30 fatalities. It is estimated that it will take approximately six months before another unit is ready for production at the mine. The occurrence of any of these hazards could delay production, increase production costs and result in death or injury to persons, damage to property and liability for ArcelorMittal, some or all of which may not be covered by insurance.

Source: www.arcelormittal.com [adapted by the author]

10. Exhibit number of employees by segment

	2005	2006	2007
Flat Carbon Americas	21.046	36.700	35.491
Flat Carbon Europe	29.811	67.238	68.000
Long Carbon Americas and Europe	20.050	40.893	56.462
AACIS	153.235	148.291	123.526
Stainless Steel	-	11.542	11.570
AM3S	-	11.560	13.086
Other activities	144	3.354	3.331
Total	224.286	319.578	311.466

Source: www.arcelormittal.com

11. Exhibit ArcelorMittal financial data (2006* - 2008)

		ArcelorMittal (31-12-2006)(*)	ArcelorMittal (31-12-2007)	ArcelorMittal (31-12-2008)
Millions of USD	Revenues	58.870	105.216	124.936
Millions of USD	EBITDA	9.856	19.400	18.336
Millions of USD	EBIT	7.532	14.830	12.236
Millions of USD	Net Profit	5.247	10.368	9.399
Millions of USD	Net Profit (Before Minority Interests)	6.106	11.850	10.439
Millions of USD	Total Debt	62.453	72.090	73.858
Millions of USD	Net Debt	56.307	63.985	66.280
Millions of USD	Equity	50.228	61.535	59.230
Millions of USD	Total Assets	112.681	133.625	133.088
Millions of USD	Fixed Assets (Long Term Assets)	73.268	88.297	88.674
Millions of USD	Market capitalization	58.431	109.958	33.590
Millions of USD	NWC Needs (**)	13.629	13.556	14.476
Millions of USD	Invested Capital (Fixed Assets + NWC)	86.897	101.853	103.150
	WACC	10,38%	12,22%	10,19%
	Pre tax Income	7.228	14.888	11.537
	Defered Taxes	-145	494	-1.396
	Medium Tax Rate = (Tax/Pre Tax Income) (***)	17,53%	17,09%	21,62%
Millions of USD	Number of Shares outstanding	1.385	1.422	1.366
USD	Shares price (dec 31th, 2005)	42,18	77,35	24,59
	ROIC	7,15%	12,07%	9,30%
	ROA	6,68%	11,10%	9,19%

(*) Half year (Values After the Merger)
(**) NWC needs = (Current Assets - Cash and Cash Equivalents) - (Current Liabilities -Short Term Debt)
(***) Defered Taxes and Minority Interests considered

Sources:

Annual Report of ArcelorMittal in 2006,2007 and 2008
www.bloomberg.com
www.google.com/finance
www.yahoofinance.com
www.arcelormittal.com

12. Exhibit Wacc assumptions

		Arcelor (31-12-2003)	Arcelor (31-12-2004)	Arcelor (31-12-2005)
Millions of USD	Interest expense	605	845	569
Millions of USD	Net Debt	18.841	16.785	16.075
	Medium Tax Rate = (Tax/Pre Tax Income)	8,26%	11,23%	8,92%
	RD	4,25%	4,47%	4,39%
Millions of USD	Net Debt (Debt)	18.841	16.785	16.075
Millions of USD	Market Capitalization (Equity)	9.142	14.651	15.642
	Rf (Risk Free) (*)	4,25%	4,22%	4,39%
	Rm-Rf (**)	5,50%	5,50%	5,50%
	βu (***)	0,63	0,74	0,91
	βL	1,82	1,49	1,76
	Re	14,27%	12,43%	14,08%
	WACC	7,52%	8,18%	9,17%

		Mittal (31-12-2003)	Mittal (31-12-2004)	Mittal (31-12-2005)
Millions of USD	Interest expense	156	285	299
Millions of USD	Net Debt	6.415	8.930	16.909
	Medium Tax Rate = (Tax/Pre Tax Income)	3,00%	11,92%	14,10%
	RD	4,25%	4,22%	4,39%
Millions of USD	Net Debt (Debt)	6.415	8.930	16.909
Millions of USD	Market Capitalization (Equity)	5.737	24.843	18.773
	Rf (Risk Free) (*)	4,25%	4,22%	4,39%
	Rm-Rf (**)	5,50%	5,50%	5,50%
	βu (***)	0,63	0,74	0,91
	βL	1,31	0,97	1,61
	Re	11,47%	9,58%	13,27%
	WACC	7,66%	8,16%	9,06%

		Arcelor + Mittal (31-12-2003)	Arcelor + Mittal (31-12-2004)	Arcelor + Mittal (31-12-2005)
	Arcelor WACC	7,52%	8,18%	9,17%
Millions of USD	Arcelor Entreprise Value	27.983	31.435	31.717
	Mittal WACC	7,66%	8,16%	9,06%
Millions of USD	Mittal Entreprise Value	12.152	33.773	35.682
	Arcelor + Mittal WACC	7,56%	8,17%	9,11%

		ArcelorMittal (31-12-2006)	ArcelorMittal (31-12-2007)	ArcelorMittal (31-12-2008)
Millions of USD	Interest expense	905	1.504	2.849
Millions of USD	Net Debt	56.307	63.985	66.280
	Medium Tax Rate = (Tax/Pre Tax Income)	17,53%	17,09%	21,62%
	RD	4,70%	4,02%	3,37%
Millions of USD	Net Debt (Debt)	56.307	63.985	66.280
Millions of USD	Market Capitalization (Equity)	58.431	109.958	33.590
	Rf (Risk Free) (*)	4,70%	4,02%	2,21%
	Rm-Rf (**)	5,50%	5,50%	5,50%
	βu (***)	1,13	1,59	1,53
	βL	2,03	2,36	3,90
	Re	15,85%	16,98%	23,64%
	WACC	10,38%	12,22%	10,19%
	Adjusted βu (****)	0,76	0,76	0,76
	Adjusted βL	1,36	1,13	1,94
	Adjusted Re	12,20%	10,22%	12,85%
	Adjusted WACC	8,52%	7,94%	6,56%

(*) US Treasury Bonds, 10 Y
(**) Rm-Rf Damodaran assumption = 5,5%
(***) βu = Beta Steel(general)
(****) Adjusted Beta due to the instability years which promoted a exponential growth

Sources:

Annual Report of Arcelor SA and Mittal Steel in 2005 and 2006
Annual Report of ArcelorMittal in 2006, 2007 and 2008
www.bloomberg.com
www.google.com/finance
www.yahoofinance.com
www.arcelormittal.com
www.damodaran.com

1USD - JPY	117,47	31-03-2006
1USD - JPY	117,87	31-12-2005
1USD - KRW	1020,73	31-12-2005
1USD - EUR	0,8484	31-12-2005
1USD - GBP	0,5813	31-12-2005

13. Exhibit Wacc calculation

	Index:	Annual
	1982-84=100	growth rate
2000 (actual)	172,2	3,37%
2001 (actual)	177,1	2,85%
2002 (actual)	179,9	1,58%
2003 (actual)	184,0	2,28%
2004 (actual)	188,9	2,66%
2005 (actual)	195,3	3,39%
2006 (actual)	201,6	3,23%
2007 (actual)	207,342	2,85%
2008 (actual)	215,303	3,84%
2009	214,050	-0,58%
2010	218,050	1,87%
2011	222,629	2,10%
2012	227,750	2,30%
2013	233,216	2,40%
2014	239,046	2,50%
2015	245,022	2,50%
2016	251,148	2,50%
2017	257,426	2,50%
2018	263,862	2,50%

Source: U.S. Bureau of Labor Statistics; The Puget Sound Economic Forecaster, prepared by Conway Pedersen Economics, Inc (assumed a constant growth after 2015)

Arcelor +Mittal	
Nominal Wacc	Real Wacc
8,17%	5,36%
9,11%	5,54%
8,85%	5,45%
8,45%	5,45%
9,50%	5,45%
4,84%	5,45%
7,42%	5,45%
7,66%	5,45%
7,88%	5,45%
7,98%	5,45%
8,09%	5,45%
8,09%	5,45%
8,09%	5,45%
8,09%	5,45%
8,09%	5,45%

ArcelorMittal	
Nominal Wacc	Real Wacc
7,94%	4,95%
6,56%	2,62%
3,18%	3,78%
5,72%	3,78%
5,96%	3,78%
6,17%	3,78%
6,27%	3,78%
6,38%	3,78%
6,38%	3,78%
6,38%	3,78%
6,38%	3,78%
6,38%	3,78%

ARCELOR + MITTAL WACC

	Arcelor +Mittal (2004)	Arcelor +Mittal (2005)	Arcelor +Mittal (2006)	Arcelor +Mittal (2007)	Arcelor +Mittal (2008)	Arcelor +Mittal (2009)
Arcelor + Mittal WACC	8,17%	9,11%	8,85%	8,45%	9,50%	4,84%

	Arcelor +Mittal (2010)	Arcelor +Mittal (2011)	Arcelor +Mittal (2012)	Arcelor +Mittal (2013)	Arcelor +Mittal (2014)	Arcelor +Mittal (2015)
Arcelor + Mittal WACC	7,42%	7,66%	7,88%	7,98%	8,09%	8,09%

	Arcelor +Mittal (2016)	Arcelor +Mittal (2017)	Arcelor +Mittal (2018)
Arcelor + Mittal WACC	8,09%	8,09%	8,09%

ARCELORMITTAL WACC

	ArcelorMittal (2007)	ArcelorMittal (2008)	ArcelorMittal (2009)	ArcelorMittal (2010)	ArcelorMittal (2011)	ArcelorMittal (2012)
ArcelorMittal WACC	7,94%	6,56%	3,18%	5,72%	5,96%	6,17%

	ArcelorMittal (2013)	ArcelorMittal (2014)	ArcelorMittal (2015)	ArcelorMittal (2016)	ArcelorMittal (2017)	ArcelorMittal (2018)
ArcelorMittal WACC	6,27%	6,38%	6,38%	6,38%	6,38%	6,38%

Sources:

Annual Report of Arcelor SA and Mittal Steel in 2003, 2004 and 2005
Annual Report of ArcelorMittal in 2006,2007 and 2008
U.S. Bureau of Labor Statistics
www.bloomberg.com
www.google.com/finance
www.yahoofinance.com
www.arcelormittal.com

14. Exhibit Arcelor + Mittal future cash flows (projection)

	2004	2005	2006(*)	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Sales	57.765	66.570	64.697	66.638	68.637	70.696	72.817	75.001	77.252	79.569	81.956	84.415	86.947	89.556	92.242
Cost of Sales	43.764	52.838	49.016	50.486	52.001	53.561	55.168	56.823	58.527	60.283	62.092	63.954	65.873	67.849	69.885
Gross Margin	14.001	13.732	15.681	16.152	16.636	17.135	17.649	18.179	18.724	19.286	19.865	20.460	21.074	21.707	22.358
Other Operational Costs	1.774	1.508	1.987	2.047	2.108	2.171	2.236	2.303	2.373	2.444	2.517	2.593	2.670	2.750	2.833
EBITDA	12.227	12.224	13.694	14.105	14.528	14.964	15.413	15.875	16.352	16.842	17.348	17.868	18.404	18.956	19.525
Amortizations and deperciations	1.905	2.320	2.134	2.198	2.264	2.331	2.401	2.473	2.548	2.624	2.703	2.784	2.867	2.953	3.042
EBIT	10.322	9.904	11.561	11.908	12.265	12.633	13.012	13.402	13.804	14.218	14.645	15.084	15.537	16.003	16.483
EBIT (1-t)	8.090	7.763	9.061	9.333	9.613	9.902	10.199	10.505	10.820	11.144	11.479	11.823	12.178	12.543	12.919
Amortizations and depreciations	1.905	2.320	2.134	2.198	2.264	2.331	2.401	2.473	2.548	2.624	2.703	2.784	2.867	2.953	3.042
Invested Capital (**)	35.201	50.597	52.115	53.678	55.289	56.947	58.656	60.415	62.228	64.095	66.017	67.998	70.038	72.139	74.303
Change in Invested Capital	4.767	15.396	1.518	1.563	1.610	1.659	1.708	1.760	1.812	1.867	1.923	1.981	2.040	2.101	2.164
FCFF	3.324	-7.633	7.543	7.770	8.003	8.243	8.490	8.745	9.007	9.277	9.556	9.842	10.138	10.442	10.755
Continuing Value															211.449
WACC Summed company	8,17%	9,11%	8,85%	8,45%	9,50%	4,84%	7,42%	7,66%	7,88%	7,98%	8,09%	8,09%	8,09%	8,09%	8,09%
Discount factor (***)				100,00%	91,33%	87,11%	81,09%	75,32%	69,82%	64,66%	59,82%	55,35%	51,21%	47,38%	43,83%
Discounted FCFF				7.770	7.309	7.181	6.885	6.587	6.289	5.999	5.717	5.448	5.191	4.947	4.714
PV of Continuing Value															92.683
Enterprise Value				166.718											

(*) Projections assumed a growth of 12% due to high investements in the previous years
(**) Constant growth at 3% rate
(***) Assuming a constante D/E ratio since 2005

GROWTH BETWEEN YEAR 2004 AND 2005:

Revenue g	15,24%
COS g	20,73%
EBIT g	-4,05%
Amort g	21,78%

CONSTANT TAX RATE:

Tax rate	21,62%

1USD - JPY	117,47	31-03-2006
1USD - JPY	117,87	31-12-2005
1USD - KRW	1020,73	31-12-2005
1USD - EUR	0,8484	31-12-2005
1USD - GBP	0,5813	31-12-2005

15. Exhibit ArcelorMittal future cash flows (projection)

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Sales	105.216	124.936	149.923	172.412	185.343	194.610	200.448	206.461	212.655	219.035	225.606	232.374
Cost of Sales (*)	80.383	100.010	115.012	126.513	132.838	136.823	140.928	145.156	149.511	153.996	158.616	163.374
Gross Margin	24.833	24.926	34.912	45.899	52.504	57.786	59.520	61.305	63.145	65.039	66.990	69.000
Other Operational Costs	5.433	6.590	7.908	9.094	9.776	10.265	10.573	10.890	11.217	11.553	11.900	12.257
EBITDA	19.400	18.336	27.004	36.805	42.728	47.521	48.947	50.415	51.928	53.486	55.090	56.743
Amortizations and deperciations	4.570	6.100	7.320	8.418	9.049	9.502	9.787	10.080	10.383	10.694	11.015	11.346
EBIT	14.830	12.236	19.684	28.387	33.679	38.019	39.160	40.335	41.545	42.791	44.075	45.397
EBIT (1-t)	11.624	9.591	15.428	22.250	26.397	29.800	30.694	31.614	32.563	33.540	34.546	35.582
Amortizations and depreciations	4.570	6.100	7.320	8.418	9.049	9.502	9.787	10.080	10.383	10.694	11.015	11.346
Invested Capital (**)	101.853	103.150	106.245	109.432	112.715	116.096	119.579	123.166	126.861	130.667	134.587	138.625
Change in Invested Capital	14.956	1.297	3.095	3.187	3.283	3.381	3.483	3.587	3.695	3.806	3.920	4.038
FCFF	-3.332	8.294	12.334	19.062	23.114	26.418	27.211	28.027	28.868	29.734	30.626	31.545
Continuing Value												933.713
WACC	7,94%	6,56%	3,18%	5,72%	5,96%	6,17%	6,27%	6,38%	6,38%	6,38%	6,38%	6,38%
Discount Factor (***)	100,00%	93,84%	90,95%	86,03%	81,19%	76,47%	71,95%	67,64%	63,58%	59,77%	56,19%	52,82%
Discounted FCFF	-3.332	7.783	11.218	16.399	18.766	20.201	19.579	18.957	18.355	17.772	17.208	16.661
PV of Continuing Value												493.171
Enterprise Value	672.739											
Market Value of Cash and equivalents	8.105											
Firm Value	680.844											
Debt (Market value)	63.985											
Equity value	616.859											

(*) COGS growth at a low level than Sales - due to decrease in market dependency
(**) Constant growth at 3% rate
(***) Assuming a constante ratio D/E since 2005

GROWTH BETWEEN YEAR 2007 AND 2008:

Revenue g	18,74%
COS g	21,30%
EBIT g	21,20%
Amort g	33,48%

CONSTANT TAX RATE:

Tax rate	21,62%

16. Exhibit ArcelorMittal incremental cash flows (projection)

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Sales	38.578	56.299	79.227	99.595	110.341	117.358	120.879	124.505	128.240	132.088	136.050	140.132
Cost of Sales (*)	29.897	48.009	61.451	71.345	76.016	78.296	80.645	83.064	85.556	88.123	90.767	93.490
Gross Margin	8.681	8.290	17.776	28.250	34.325	39.062	40.234	41.441	42.684	43.965	45.284	46.642
Other Operational Costs	3.386	4.482	5.737	6.858	7.473	7.893	8.129	8.373	8.624	8.883	9.150	9.424
EBITDA	5.295	3.808	12.040	21.392	26.853	31.169	32.105	33.068	34.060	35.081	36.134	37.218
Amortizations and deperciations	2.372	3.836	4.989	6.017	6.576	6.954	7.163	7.378	7.599	7.827	8.062	8.304
EBIT	2.922	-29	7.051	15.375	20.277	24.215	24.942	25.690	26.461	27.254	28.072	28.914
EBIT (1-t)	2.291	-23	5.527	12.051	15.893	18.980	19.549	20.136	20.740	21.362	22.003	22.663
Amortizations and depreciations	2.372	3.836	4.989	6.017	6.576	6.954	7.163	7.378	7.599	7.827	8.062	8.304
Invested Capital (**)	48.175	47.861	49.297	50.776	52.299	53.868	55.484	57.149	58.863	60.629	62.448	64.322
Change in Invested Capital	13.393	-313	1.436	1.479	1.523	1.569	1.616	1.665	1.714	1.766	1.819	1.873
FCFF	-11.102	291	4.091	10.572	14.370	17.411	17.933	18.471	19.025	19.596	20.184	20.790
Continuing Value												615.366
WACC ArcelorMittal		6,56%	3,18%	5,72%	5,96%	6,17%	6,27%	6,38%	6,38%	6,38%	6,38%	6,38%
Discount Factor (***)	100,00%	93,84%	90,95%	86,03%	81,19%	76,47%	71,95%	67,64%	63,58%	59,77%	56,19%	52,82%
Discounted FCFF	-11.102	273	3.721	9.095	11.666	13.314	12.904	12.494	12.097	11.713	11.341	10.981
PV of Continuing Value												325.026
Enterprise Value	423.521											

(*) COGS growth at a low level than Sales - due to decrease in market dependency
(**) Constant growth at 3% rate
(***) Assuming a constante ratio D/E since 2005

GROWTH BETWEEN YEAR 2007 AND 2008:

Revenue g	45,93%
COS g	60,58%
EBIT g	-100,98%
Amort g	61,71%

CONSTANT TAX RATE:

Tax rate	21,62%

1USD - JPY	117,47	31-03-2006
1USD - JPY	117,87	31-12-2005
1USD - KRW	1020,73	31-12-2005
1USD - EUR	0,8484	31-12-2005
1USD - GBP	0,5813	31-12-2005

17. Exhibit Synergies

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Δ Sales	38.578	56.299	79.227	99.595	110.341	117.358	120.879	124.505	128.240	132.088	136.050	140.132
Operating margin of Summed company	17,87%	17,87%	17,87%	17,87%	17,87%	17,87%	17,87%	17,87%	17,87%	17,87%	17,87%	17,87%
Tax rate	21,62%	21,62%	21,62%	21,62%	21,62%	21,62%	21,62%	21,62%	21,62%	21,62%	21,62%	21,62%
EBIT (1-t) (Summed company)	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%
Sales synergy = Δ Sales * [(EBIT(1-t)/Sales)]	5.403	7.885	11.096	13.949	15.454	16.437	16.930	17.438	17.961	18.500	19.055	19.626
Sales synergies terminal value												385.865
Discounted sales synergies	5.403	7.201	9.666	11.312	11.640	11.477	10.947	10.432	9.941	9.473	9.028	177.736
PV of sales synergies	284.256											

Sales (ArcelorMittal)	105.216	124.936	149.923	172.412	185.343	194.610	200.448	206.461	212.655	219.035	225.606	232.374
EBIT(1-t)/Sales (Summed company)	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%	14,01%
EBIT(1-t)/Sales (ArcelorMittal)	11,05%	7,68%	10,29%	12,90%	14,24%	15,31%	15,31%	15,31%	15,31%	15,31%	15,31%	15,31%
Cost synergies = Sales total * [EBIT(1-t)/Sales (historical) - EBIT(1-t)/Sales (projected)]	-3.113	-7.908	-5.570	-1.898	439	2.543	2.619	2.698	2.779	2.862	2.948	3.037
Cost synergies termial value												59.699
Discounted cost synergies	-3.113	-7.222	-4.852	-1.539	330	1.776	1.694	1.614	1.538	1.466	1.397	27.498
PV of cost synergies	20.587											

Sales synergies + cost synergies	2.291	-23	5.527	12.051	15.893	18.980	19.549	20.136	20.740	21.362	22.003	22.663
												670.819

Change in Invested Capital (ArcelorMittal)	14.956	1.297	3.095	3.187	3.283	3.381	3.483	3.587	3.695	3.806	3.920	4.038
Change in Invested Capital (Summed company)	1.563	1.610	1.659	1.708	1.760	1.812	1.867	1.923	1.981	2.040	2.101	2.164
Incremental Change in Invested Capital	-13.393	313	-1.436	-1.479	-1.523	-1.569	-1.616	-1.665	-1.714	-1.766	-1.819	-1.873
Invested capital terminal value												-36.833
Discounted Incremental Change in Invested Capital	-13.393	286	-1.251	-1.199	-1.147	-1.096	-1.045	-996	-949	-904	-862	-16.966
Total PV of Incremental Change in Invested Capital	-39.521											

INCREMENTAL CASH FLOWS	-11.102	291	4.091	10.572	14.370	17.411	17.933	18.471	19.025	19.596	20.184	20.790
Terminal Value												408.732
TOTAL INCREMENTAL CASH FLOWS	-11.102	291	4.091	10.572	14.370	17.411	17.933	18.471	19.025	19.596	20.184	429.521

WACC (Summed company)	8,45%	9,50%	4,84%	7,42%	7,66%	7,88%	7,98%	8,09%	8,09%	8,09%	8,09%	8,09%
Discount factor (Summed company)	100,00%	91,33%	87,11%	81,09%	75,32%	69,82%	64,66%	59,82%	55,35%	51,21%	47,38%	43,83%
Incremental cash flows discounted at expected WACC	-11.102	266	3.564	8.573	10.823	12.157	11.596	11.050	10.530	10.035	9.563	188.269
PV @ WACC Summed company	265.323											
Incremental cash flows	-11.102	291	4.091	10.572	14.370	17.411	17.933	18.471	19.025	19.596	20.184	636.155
Terminal Value new WACC												615.366
Projected WACC discounted rate	7,94%	6,56%	3,18%	5,72%	5,96%	6,17%	6,27%	6,38%	6,38%	6,38%	6,38%	6,38%
Discount rate	100,00%	93,84%	90,95%	86,03%	81,19%	76,47%	71,95%	67,64%	63,58%	59,77%	56,19%	52,82%
Incremental cash flows discounted at expected WACC	-11.102	273	3.721	9.095	11.666	13.314	12.904	12.494	12.097	11.713	11.341	336.006
PV @ WACC ArcelorMittal	423.521											
Differences	0	7	157	522	843	1.157	1.308	1.444	1.567	1.678	1.778	147.738
PV Difference in WACC	158.198											