Achieving Global Growth through Acquisition: Tata's Takeover of Corus

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ABSTRACT

The primary subject matter of this case concerns the long-term viability of Tata Steel's acquisition of Corus, an Anglo-Dutch steel firm. Secondary issues examined in this case include a discussion of emerging trends in the global steel industry, post-acquisition issues facing Tata Steel (including financial and cross-cultural issues), and the impact of this particular transaction on the mindset of other Indian firms that are increasingly seeking an international presence.

Key words: Acquisition, world steel industry, consolidation, cross-cultural issues

CASE SYNOPSIS

Tata Steel (part of the Tata Group based in India) acquired the Anglo-Dutch steel firm Corus after a four month bidding war with Brazil's CSN (Companhia Siderurgica Nacional SA) for US$11.3 billion—this was the biggest acquisition by an Indian firm. Tata's acquisition of Corus made it the fifth largest global steel producer with an annual capacity to produce 25 million tons of steel (Anonymous, 2007, May/June; www.tatasteel.com, 2007, April 3). The acquisition was intended to give Tata Steel access to European markets and to achieve potential synergies in the areas of manufacturing, procurement, R&D, logistics, and back office operations. Critics claimed that the acquisition price at 608 pence per share was substantially higher than an earlier offer of 455 pence per share. Additionally, they felt that it would take several years for potential production and operational synergies to materialize that would yield significant cost savings. Following the acquisition, Tata Steel's stock suffered a significant decline in price causing Standard & Poor's to place it on a credit watch list with negative implications. Did Tata Steel overpay for acquiring Corus? What is the long term possibility of realizing proposed synergies? Will Tata Steel's gamble of being a global steel player payoff in the long run?

TATA GROUP OF COMPANIES-A BRIEF HISTORY

Tata Steel is part of one of India's largest business conglomerates, the Tata Group established by Jamsetji Tata and his extended family. The Tatas were descendants of Persian Zoroastrians who immigrated to India sometime in between the 8th and 10th centuries to escape religious persecution. Although Jamsetji's father opened an export business when Jamsetji was only a teenager, that business faced a financial crisis following the end of the U.S. Civil War and the return of U.S. producers to world markets. With Jamsetji's expert guidance, the company was reborn as Tata and Co., later to be renamed Tata and Sons in 1868. Tata Steel was founded in 1907, and the plant started production in 1912 (information about Tata group profile obtained from www.tatasteel.com). Currently, Tata Steel is now India's largest private steelmaker, the world's 6th largest steelmaker, and due to its ownership of raw materials (coal and iron), can produce steel at lower costs than nearly any other steelmaker in the world (www.tatasteel.com, 2007, July 23).

In 2005-2006, the Tata Group had revenues of $21.9 billion (all $ amounts are referenced with respect to US $) which was approximately 2.8 percent of India's gross domestic product. With a market capitalization of $63.0 billion in 2007, the Tata Group employs around 2,460,000 people and comprises 96 operating companies in seven business sectors: information systems and communications (Tata Consultancy Services), engineering, materials, services, energy, consumer products and chemicals. The group has 28 publicly listed firms with approximately 2 million shareholders. Operations span 85 countries on six continents and there has been an overall rapid growth through acquisition and merger activity (www.tatasteel.com, 2007, July 23).

The company has been run by family members for five generations. The current chairman of Tata Group is Ratan Tata who succeeded J.R.D. Tata in 1991. At his time of succession, the Tata Group was a sprawling network of 250 companies, many doing poorly. He has since downsized the group to 96 firms. Not content to operate only in India, he has increasingly challenged his managers to expand overseas (Bary, Santoli, Laing & Racanelli, 3/26/07).

The Tata Group has made a number of recent acquisitions (Leahy, 2007, May 18). Tata Tea bought out U.S.-based Eight O'Clock Coffee for $220 million; a 30 percent share of Energy Drinks, another U.S. firm, for $677 million; and acquired a 33 percent share of South Aftrica's Joekels Tea Packers. Tata's Indian Hotels bought the Ritz Carlton Boston for $170 million. Tata Motors acquired the truck operations of South Korea's Daewoo. Tata Steel had also purchased Singapore's Natsteel in 2004 for $485 million and Thailand's Millennium Steel for $404 million in 2005.

On February 2, 2007, Tata Steel won its bid to acquire Corus, the Anglo-Dutch steel company. The Corus acquisition by Tata Steel made it a "giant among giants in India Inc." The steel conglomerate is now the largest private company by sales in India, a distinction earlier held by Reliance Industries which is now second (Knight Ridder 2/2/07). The acquisition of Corus is anticipated to make Tata Steel the world's second largest steelmaker within five years.

TRENDS IMPACTING THE WORLD STEEL INDUSTRY

"I really believe that the owners of iron ore are going to rule the industry. They will be OPEC of the steel industry." (Ratan Tata's interview to McKinsey Quarterly quoted by Wheatley in Financial Times, January 29, 2007)

In recent years, the steel industry witnessed a high degree of global consolidation due to a few key factors. These included the following (Anonymous, 2007, February 1, 12; Marsh, 2007, April 19; Miller, 2007, January 3; www.tatasteel.com, 2006, October 20):

- A desire amongst the key players to gain efficiencies resulting from scale,
- Obtaining access to new and growing markets,
- Enhancing purchasing power with respect to suppliers and buyers.

Steel prices were on an upward trend after 2004 and worldwide demand for steel continued to increase until the global economic crisis emerged. Production costs in part depended on manufacturing technology and degree of backward integration having access to power and raw material. As an example, in order to produce a ton of steel, raw materials accounted for 60-70% of the cost while energy (coal and power) accounted for 25-30% of the remaining production costs (Businesswire, 2007, June 11). The rapid growth in the Chinese economy and other developing countries like India during the mid-2000s also created an increasingly strong demand for steel. Not content to depend on its own domestic supplies, China was importing steel from major international producers keeping steel prices high. During that time, there was speculation that China, by far the world's biggest steel maker, would increase its steel capacity which could result in lower world prices (Marsh, 2007, April 19).

The climate at the time of Tata's acquisition of Corus was characterized by an "eat-or-be-eaten" mentality in which steel companies increasingly had to decide whether to be an acquirer or an acquisition target. These mergers and acquisitions were expected to eventually result in a handful of worldwide global giants in the steel industry. Merger and acquisition activity in the world steel industry was likely to result in a higher degree of pricing stability and better margins for the steel producing companies (Anonymous, 2007, February 2, 1; Ibsen & Lawrence, 2007, May 4, 19; Marsh, 2007, April 19, 25).

The following discussion identifies and briefly describes some of the key consolidation moves during mid-2002 in the world steel industry (Anonymous, Metal Producing & Processing, May/June 2007; Bream, 2006, November 21; Ibison & Lawrence, 2007, May 4; Leahy, 2007, April 17; Marsh, 2007, June 6; Marsh, 2007, April 19; Marsh, 2007 April 9; Miller, 2007, January 3; Range, 2007, April 26; Reed, Arndt, Lakshman, & Smith, 2007, April).

- In 2004, Mittal bought International Steel Group, an American company which included assets of the previous Bethlehem Steel.
- In October, 2006, Russian steelmaker Evraz Group bought Oregon Steel Mills of the U.S. for $2.3 billion.
- Mittal's merger with Arcelor ($36.1 billion offer) in 2006 created the largest steel company in the world.
- Nucor, the second largest US steel producer, acquired Harris Steel Group of Canada for $1.07 billion in January 2007.
- Mitsui & Co. Ltd acquired Steel Technologies, Inc. for $350 million.
- The former Calumet Steel (CaluMetals) was acquired by Keystone Consolidated Industries, Inc.
- Sumitomo Metals and Vallourec are pursuing a joint venture in Brazil that is expected to be in production by 2010.
- Companhia Vale do Rio Doce bought out Nucor's interest in a joint venture in Ferro Gusa Carajas S.A.
- Severstal, the largest Russian steelmaker had invested $800 million in a new plant in Mississippi and $900 million in a plant near Detroit.
- Essar Group of India has made a $1.6 billion investment in Algoma Steel of Canada (2007) as well as $4.65 billion offer to buy Minnesota Steel Industries.
- On May 4, 2007, Swedish steelmaker, SSAB, made a $7.7 billion dollars cash offer to acquire Ipsco of Canada.
- In spring 2007, Arcelor-Mittal finalized an $11.4 billion acquisition of Sicartsa, a producer of long steel products from Groupo Villacero.

The momentum of steel industry consolidation appeared to continue in 2007 with companies considering smaller acquisitions, many of which were in North America. Potential targets included the following (Marsh, 2007, June 6):

- AK Steel, a specialty steel maker for the US auto industry valued over $5 billion.
- Allegheny Technologies, a difficult-to-make steel specialty company thought to be worth $14 billion.
- US Steel, the biggest US-based steel maker with many specialty divisions worth about $16 billion.

Lakshmi Mittal, CEO of Arcelor-Mittal the world's biggest steelmaker, believed that mergers would help stabilize prices in the world steel industry which experienced a tremendous degree of volatility over the previous 20 years. Arcelor-Mittal's share price rose steeply following the Arcelor's takeover by Mittal for $36.1 billion in 2006. Positive investor sentiment towards the Arcelor-Mittal merger impacted other steel stocks. Following the Arcelor-Mittal merger, the global steel industry stock market index rose by nearly 24% more than the overall index for all world stocks. According to M&A specialist D. G. Dwyer of Industry Corporate Finance Ltd., the Arcelor-Mittal merger and Tata Steel's acquisition of Corus created a more stable steel industry making the latter more attractive to investors.

All of that progress reversed in 2008, when the global economy contracted. New competition emerged as a result of Chinese support and protection for its steel industry combined with plans to raise import duties. As a reaction to the global economic downturn, global steel production dropped 1.2% to a total of 1.3297 billion tons in 2008. Experts forecast as much as an additional 10% drop in production in 2009, resulting in lost jobs, postponement of investment, and worldwide hard times for the steel industry. Although India has instituted an economic stimulus package that should benefit the steel industry, a number of Tata's companies were challenged by the loss of global demand in the steel and automobile industries.

A TIMETABLE OF TATA STEEL'S ACQUISITION OF CORUS

It is important to gain an understanding of the events that led to Corus's desire to be acquired before launching into a detailed discussion of the acquisition activity. Corus, the Anglo-Dutch steelmaker, was formed in 1999 by the merger of British Steel with Hoogovens of the Netherlands. With 47,300 employees working in plants across Britain, the Netherlands, Germany, France, Norway, and Belgium, Corus had the highest cost of production among the world's steel makers. After the merger, a rift developed between the two camps. Matters became worse when the British half of the business sustained serious losses while the Dutch side was quite profitable. The Dutch contended that the UK side of the business was causing the entire organization to be unprofitable. Corus's management realized that the status quo was unsustainable given the increased competition from steelmakers in developing economies who had access to cheaper labor and raw materials. Additionally, higher raw material and energy costs were impacting profitability. So they decided to look for a suitable partner outside Western Europe to acquire Corus, and began negotiations with key players in the steel industry from India, Russia, and Brazil.
($=US dollars; GB pounds=Great Britain Pounds; p=pence; Rs. = Indian Rupees;
The exchange rate is approximately Rs.100= 1.79 Euro or $2.43)

The following timeline outlines these events (Anonymous, 2006, December 12, 23; Bream, 2007, January 27; Lea, 2007, January 31; Leahy, 2006, October 23; McGhee, 2007, January 21; Tata Steel, Ltd, 2007, April 3; West, 2007, March 8):

11/2005	Corus's top management meet Ratan Tata in Mumbai.
Mid-2006	Ratan Tata made an offer of 455p per share to buy Corus
10/17/06	Tata Steel makes a cash offer of GB 5.1billion pounds ($10 billion) bid for Corus worth 455p a share in cash.
10/20/06	Corus's Board of Directors recommend acceptance of Tata Steel's offer.
11/17/06	Companhia Siderurgica Nacional (CSN) of Brazil makes a bid of GBP 5.3 billion for Corus, worth 475p a share in cash.
11/27/06	Corus postpones shareholder meeting from December 4 to December 20 to give CSN time to prepare a formal bid.
11/28/06	Corus reports a 63 per cent increase in quarterly profits.
12/10/06	Tata Steel raises its offer by 10 per cent and makes an offer of GBP 5.5 billion including debt, worth 500p a share in cash.
12/11/06	CSN raises its formal offer for Corus from 500p to 515p a share in cash.
1/21/07	Corus accepts a 515 pence per share offer from CSN, but speculation in the financial markets anticipating a counter offer result in Corus's shares closing at 545 p per share, well above CSN's latest offer.

1/27/07	Tata Steel and CSN agreed to terms for an auction that will begin January 30 at 4:30 p.m. London time and end by 2:30 a.m. with an announcement of the winner by 3:00 a.m. There will be up to nine rounds of bidding.
1/30/07	The British press bills the bid for Corus as a clash between Tata Steel and CSN as a battle to "decide the fate of more than two centuries of British industrial history" (Knight Ridder, 2007 January 30).
1/31/07	The "battle for Corus" starts. It is seen as a clash of two steel titans: Ratan Tata and CSN's Benjamin Steinbruch. (Thomas, 2007 January 31).
2/1/07	After three months of bids and counter-bids, Tata Steel wins a fiercely contested 8-hour closed-door auction against Brazil's CSN for Corus. Tata Steel acquires 21.1 percent of the equity share capital for 608 pence per share ($11.7), besting the CSN bid of 603 pence, paving the way to acquire Corus.
4/2/07	The courts officially approved Tata Steel's acquisition of Corus in a deal valued at GBP 6.2 billion ($12 billion dollars).
4/11/07	Tata Steel's board of directors meet on 4/17 to consider proposals for raising equity funds to finance the Corus acquisition. Tata Steel shares trade at Rs. 495.55 on the Bombay Stock Exchange.
4/18/07	Tata Steel announces that it has deployed teams to work on synergies in areas of manufacturing, procurement, logistics, marketing, iron and steel making. By the end of May, long-term strategic issues and specific areas of synergy were close to conclusion.
4/28/07	Tata Steel announces it will raise $4.1 billion equity capital as partial payment for Corus using a rights issue and a convertible preference share issue along with other financial methods.
5/4/07	Tata Steel will borrow $7.3 billion in loans as part of its long-term financing arrangements in the takeover of Corus. It took advantage of high liquidity in the leveraged loan market and went with a long-term arrangement with Citigroup, Standard Chartered and ABN Amro.
5/17/07	Tata Steel announced plans that would potentially make it the second largest steel maker in the world within five years. Manufacturing capacity is planned to increase from about 25 million tons a year to 40 million by 2012, and then to 50 million by 2015.

POST-ACQUISTION ISSUES FACING TATA STEEL

Tata Steel's acquisition of Corus was not without controversy. There were substantial issues raised during and after the acquisition that require a more comprehensive discussion, especially in light of the turn of events witnessed in the two years following the acquisition. The current industry woes (in December 2008 global steel production declined by 23.4%) are seen by some experts as an opportunity for expansion and strengthening of the industry in India (Anonymous, 2008, October 7 *Indiaserver.com*).

DID TATA OVERBID FOR CORUS? VIEWPOINTS OF FINANCIAL ANALYSTS

Many financial analysts felt that Tata Steel overpaid for the Corus acquisition. Immediately after the acquisition announcement, Tata Steel's share price fell by 10.7 percent to

Rs. 463.95 on the Bombay Stock Exchange. According to Martin Stanley, London based head of spread betting at the brokerage firm of GFT Global Markets, "The consensus view seems to be that Tata have probably overpaid, but if further consolidation in this sector occurs going forward then this will look like very fair value" (International Herald Tribune, 1/30/07). Additional concerns were raised about the debt liability of Tata Steel which borrowed more money to fund the acquisition. According to Standard & Poor's analyst Anushkant Taneja, "The size of the Tata acquisition and the potential cash outflow in Tata Steel's offer for Corus could have an adverse impact on its financial risk profile." Standard & Poor's rating service in India, Crisil, placed Tata Steel on the "negative implications" watch list after its Corus acquisition. The contention was that Tata Steel had overstretched itself due to execution risk and lack of experience by Indian companies in acquiring international businesses (Range, 2007, April 26).

Moody's Investor Services downgraded Tata Steel's rating from Baa2 (investment grade) to Ba1 (speculative grade). The primary reason cited was Tata Steel's weakened balance sheet liquidity and financial profile resulting from its largely debt-funded acquisition of Corus. Moody's Senior V.P. Alan Greene stated Tata Steel's current high leverage constrains its financial strength and flexibility and "the main challenge facing management is to de-risk the large capital structure while not neglecting existing operations and opportunities for rapid growth in Asia." He further stated that "Tata Steel's ambitious capacity expansion plan will lead to higher project execution risk over several years and materially elevate financial leverage unless it is deferred." (Businessline, 2007, July 7).

According to Sreesankar, head of research at Il&Fs investments in Mumbai, "They (Tata Steel) wanted the company and they have got it. But we have to see how the finding happens and how the integration progresses. One distinction is that EBITDA (earning before income taxes and depreciation allowance) margins for Tatas are about 40 percent and for Corus is about 7 percent." Clearly, the financial industry analysts were skeptical about the long-term financial viability of this acquisition. According to Shriram Iyer, head of research at Edelweiss in Mumbai, "…the time horizons of investors and of the company may not be aligned" (Leahy, 2007, 16).

DID TATA OVERBID FOR CORUS? VIEWPOINT OF TATA STEEL'S EXECUTIVES

This proposed acquisition represents a defining moment for Tata Steel and is entirely consistent with our strategy of growth through international expansion. This creates a well balanced company, strategically well placed to compete in an increasingly competitive global environment. (Ratan Tata quoted in Financial Express; 2007, February 13)

The Tata Steel board of directors approved the project to acquire Corus, as it was consistent with stated objectives of growth and globalization. Although Tata Steel ended up paying more for Corus than its original bid, its management felt that there were many favorable strategic and financial outcomes to be realized. To begin with, this acquisition would position the combined group as the fifth largest steel company in the world by production output. The new entity would have a meaningful market presence in both Europe (where Corus was a well established brand name) and Asia (where Tata was a well established brand name).

Combining the low cost upstream production in India with the high-end downstream processing facilities of Corus in Europe was intended to create synergies that would significantly improve the competitiveness of European operations. Tata Steel will retain access to low cost raw materials, gain exposure to high growth emerging markets, while gaining price stability in developed markets. There was tremendous potential to create cross-fertilization of research and development capabilities in the automotive, packaging and construction sectors with transfer of technology, best practices and managerial from Europe to India. (www.tatasteel.com, 2006, October 20).

Tata Steel formed teams to work on synergies in areas of manufacturing, procurement, logistics, marketing, iron and steel making. There were 15-18 teams consisting of 3-4 members from both companies. Each team worked on realizing various potential synergies by sharing know-how, adopting best practices, and information to develop efficient practices aiding in cost reduction. B. Muthuraman, Managing Director of Tata Steel expected the synergies to be achieved within three years and to have a higher valuation than $350 million per year indicated at the time of the deal. Muthuraman further noted that the acquisition price for Corus placed production costs at $710 per ton, far less than $1,200 to $1,300 per ton that would have been the price for a greenfield plant with a production capacity for 19 million tons (Bremner and Lakshman, 2007).

During 2007, benefits of the merger for Tata were realized in manufacturing, whereas benefits for Corus were gained through reductions in taxes and shared services. In 2008, Tata made the Fortune 500 list on the basis of its revenues. In large part, this was due to the acquisition of Corus.

From the very inception of the merger project, Tata Steel officials had maintained that funding the acquisition would be supported by Tata Sons and any subsequent borrowing would not be a balance sheet burden. The initial plan was to fund the acquisition of Corus through a debt-equity ratio of 53:47 for an amount of $4.1 billion. The remaining amount was to be acquired though a series of long-term loans which would be serviced through Corus's cash flows. Corus's revenues at the time of takeover were approximately $20 billion (Leahy, 2007, January 26).

Tata Steel's senior executives estimated that cost cutting measures alone could make the acquisition a successful one. The potential existed for production and distribution costs to be spread across Europe, India and other Asian markets. Tata Steel's EBIDTA (earnings before interest, tax, depreciation and amortization) margin of 30 percent was significantly higher compared to Corus' EBITDA of 10 percent. The new entity was estimated to have a combined EBIDTA margin of 14 percent (taking into account that Corus's revenues were five times more that of Tata Steel). The EBITDA was expected to increase to 25 percent by 2012.

Shortly after Tata Steel successfully outbid CSN for Corus, Tata finance director Ishaat Hussain noted that the Corus deal was a "must-do". "Consolidation [in the steel industry] will take place going forward. It [Corus] was perhaps the only significant player which we could see as a possible acquisition in this consolidating phase. That's why Corus was so important to Tata Steel." (Lea, 2007, January 31)

WILL THE ACQUISITION FAIL DUE TO CULTURAL DIFFERENCES?

"Our intention is that Corus will retain its identity for the foreseeable future and will remain an Anglo-Dutch company. The management will be substantially the same." (Ratan Tata quoted in Forbes, 2006, December 12)

As with any acquisition, post-merger integration issues have to contend with cultural undertones and ego clashes. Nearly 70 percent of mergers and acquisitions fail because of cultural issues, and Tata Steel's acquisition of Corus is perhaps even more vulnerable because of potential cultural difficulties that could emerge from the dynamics of cross-border integration. Standard & Poor's rating service in India declared a "negative implications" watch in April, 2007 due the fact that Indian companies often lack experience in international acquisitions with different corporate cultures, employment rules, etc. In an earlier acquisition of Tetley Tea, Tata's previous UK acquisition, it had run into "some cultural and racial obstacles because of concerns that British employees would resent having managers from a former British colony" (Mahagan, 2/1/07).

UK trade unionists warned there would be impending trouble for Corus employees if Tata moved production away from the UK to lower-cost India markets. Union leaders emphasized they were not going to accept the downfall of the UK steel industry and could use any resources to resist its "accelerated or slow demise." Philippe Varin, the French CEO for Corus, didn't make any pledges or commitments, but said that the deal wasn't predicated on closures, but instead, upon global opportunities. And that it was in the best interests of Corus employees to be globally competitive. Tata Steel's executives must take into account that their European employees were beginning to feel uncertain about their fate in the newly created entity. If left unaddressed, this had the potential of creating low morale resulting in decreased productivity (Mahajan, 2007, February 1).

Merger and acquisition experts recommended a "light-handed integration" between Tata Steel and Corus instead of engaging in a comprehensive organizational overhaul (Mahajan, 2007, February 1). It was recommended that Tata Steel allow existing management to continue, with a more comprehensive restructuring set aside for a later date. Taking these recommendations to heart, Tata Steel retained the following top management of Corus to work with integration issues (www.tatasteel.com, 2007, July 23):

- Following the acquisition, Corus's head Philippe Varin was retained as chief executive with Jim Leng assuming the deputy chairman's position. Ratan Tata became the Chairman. Varin is under contract to stay with the firm for another three years.
- On July 10, Corus announced that Malcolm McOmish, Managing Director Corus Packaging Plus, was moved from his current position based at Ijmuiden in the Netherlands to become Managing Director of Cogent Power Ltd within Corus based at Orb in South Wales in the UK. Cogent Power Ltd manufactures and sells steels, which are used in the electrical motor and power generation industry.
- McOmish was succeeded by Theo Henrar, who was Managing Director, Corus Distribution and Building Systems based in the UK. In his new role, Mr. McOmish will continue to remain available to provide strategic support to the tinplate portfolio within Corus Strip Products Division.
- Alastair Aitken was appointed Managing Director, Corus Distribution and Building Systems UK and Ireland.
- In its July 18, 2007 annual general meeting, Tata Steel sought approval from shareholders to appoint four directors of Corus to its board. They were Jim Leng, Philippe Varin, Jacobus Schraven, and Anthony Hayward.
- In January 2009, Philippe Varin's replacement as CEO was announced. Kirby Adams was named the new Corus and Tata Steel Europe CEO. Varin will step down in 2009.
- Jim Leng, another Corus executive, left the firm to become Chairman of Rio Tinto, the world's 3rd largest mining firm and a Tata rival.

Dr. Ashok Kumar a member of British Parliament representing Teesside constituency where part of Corus operations were located was a strong advocate of the Tata Steel acquisition. He believed that the partnership was ideal both on a cultural and practical level and emphasized the potential of the crucial relationship between the UK and India as one of the emerging global economic powers of the 21st century. As India continued to develop, Mr. Kumar believed there would be great opportunities for UK companies who trade in manufactured goods and services. At the time of the merger, India was the third largest investor in the UK and the UK was its fourth largest trading partner. He pointed to the historic ties between India and the UK and contended that trade and commerce could be built upon centuries of cultural understanding. According to Kumar, "Corus joining Tata should be the first span in the bridge bringing our two countries closer together" (Kumar, 2007, February 13).

The Tata Investment Group provided advice and ensured that due diligence was given to cultural issues during mergers and acquisitions. Mr. R. Gopalakrishnan, Executive Director of Tata Sons, expressed an opinion that it is "important to engage with the society in which the business is located" and the post-merger integration and processes must be consistent with the strategic intent of the acquisition. When asked about what lessons the Tata Group had learned from their overseas acquisition experiences, he said the positioning of the business in the host country should be harmonious with the actions of the company. The absolute core and non-negotiable values of the acquiring company need to be explicit to the acquired company managers (Businessline, 2007, April 1). He felt that the acquisition would work well in the long-term and due diligence given to managing cultural issues should serve to enhance trust between the Indian and European sides.

IMPACT OF CORUS ACQUISITION ON INDIAN CORPORATE MORALE

There was tremendous outpouring of nationalistic euphoria and economic patriotism in the Indian press after this deal. During the early weeks of 2007, The Times of India the best-selling English daily newspaper, was reportedly "inviting its readers to discuss the new 'India poised for global supremacy' Johnson, 2007, February 3). The Tata deal has fed an unmistakable undertone of triumph as the country's status as the world's second fastest growing economy." The Economic Times, India's best selling business newspaper reported "For India, this deal is not about size—it's the first step towards what we call the Global Indian Takeover." (Johnson, 2007, February 3).

According to Ratan Tata, who spoke at the time of the acquisition, "It's a tremendous strategic acquisition. I believe this will the first step in showing that Indian industry can in fact step outside the shores of India in an international marketplace and acquit itself as a global player" (International Herald Tribune, 2007, January 30). Kamal Nath (Johnson, 2007 January 15, 4), the Indian Minister for Commerce and Industry felt that the "global perception of India is changing…it's a two-way street now….not only is India seeking foreign investment, but Indian companies are emerging investors in other countries." The Confederation of Indian Industry, India's largest business association described the acquisition as "path breaking" which would enable emerging Indian firms to gain greater respect from the global business community.

For the first time in 2006, overseas acquisitions by Indian firms exceeded the value of foreign companies buying in India. During the first six months of 2006, Indian companies had completed approximately 78 cross-border acquisitions worth $5.2 billion. For the year ending 2006, outbound deals by Indian companies totaled $22.4 billion compared with $11.3 billion in purchases from abroad. (Harris 2007, March 9). Indian business executives attribute this new confidence in part to a decade of restructuring that started in 1991 when newly drafted laws allowed greater foreign competition. Others point to the successes of Indian based firms such as Infosys Technologies, Wipro and TCS who have proven to be world class competitors from a cost/quality perspective.

In the wake of Tata Steel's acquisition of Corus, the chief executive of ICICI, India's second largest bank, proposed that Indian firms now "have the confidence to go out and buy" buoyed by substantial corporate profits which have provided large cash surpluses over the last 18 quarters. He believed that the Tata-Corus deal would most likely lead to a string of takeovers in the UK by Indian companies (Knight Ridder, 2007, April 27). An article published in the Wall Street Journal predicted a global shopping spree by Indian companies due to easier access to funds, an annual growth rate of over 8%, and a strong desire to engage in worldwide competition (Range, 2007). In the first two months of 2007, Indian companies seeking new technology, better overseas market access, and greater production capacity arranged or closed on foreign purchase deals worth $21 billion.

Mr. P. K. Vijayaraghavan, Associate Director, PricewaterhouseCoopers Private Ltd. spoke on the importance of corporate restructuring for India and noted that Tata Steel's acquisition of Corus was an outstanding example of Indian corporate thinking. (Businessline, 2007, March 8). The easy availability of global funds drove many Indian companies toward acquisitions following the Tata Steel acquisition of Corus which spurred transactions from rivals such as Essar group taking over two steel companies in North America. India's largest bank, State Bank of India which is government-controlled, and ICICI, India's largest private bank responded to the surge in deal-making and investment by raising capital. "The banking sector is facing a growing need for capital because of the expected rise in capital expenditure by the corporate sector over the next few years to meet funding requirements." (Leahy, 2007, July 7)

A proposed amendment to Competition (Amendment) Bill of 2006 and the Competition Act (2002) required companies undertaking mergers or acquisitions in India or overseas to compulsorily report the proposal to the Competition Commission of India before making such a deal. The proposal would limit acquisitions that might have an appreciably adverse effect on competition within India markets. The dollar limit thresholds are $2 billion if the acquirer is a group in India and $6 billion if the acquirer is outside of India (Businessline, 2007, May 6).

Cross-border mergers and acquisitions have gained tremendous popularity among Indian executives as a means to achieve growth and secure a global presence. According to David (2007), there are numerous seminars dealing with mergers and acquisitions where seasoned M&A executives offer advice on a number of topics ranging from government rules and regulations, pitfalls to avoid, and cultural issues impacting post-merger scenarios.

CONCLUSION

On July 23, 2007, Tata Steel stock reached a 52-week high close of 721.00 on the Bombay Stock Exchange's (BSE) 30-stock Sensex after hitting a low of 399.00 on March 8, 2007. Tata Steel was one of the market leaders for the BSE Sensex up 27% in 2007. Standard & Poor's Ratings Services cut its credit rating to BB from BBB and removed them from the negative watch list on which they were placed after the financing structure for the acquisition of Corus was announced. The rating was changed to a positive outlook. According to one Standard & Poor's analyst, "the rating remains constrained by the weak business profile of Corus, which is characterized by lack of integration or upstream linkages and relatively high cost of operations in the UK, resulting in lower-than average profitability." However, S&P maintains that the strategic significance and size of Corus, along with its importance to Tata Steel's future plans, give strong economic impetus to support the acquisition (Forbes.com, 2007, July 11). Unfortunately, the current global economic downturn has wiped all previous gains. By February 2009, Tata Steel's stock price had declined to Rs. 168.05, after a 52-week low of Rs.145.35 and a 52-week high of Rs. 925.00.

Clearly, Tata Steel gambled on a strategy based on anticipation of global consolidation of the steel industry. Along with Arcelor-Mittal, it may still be poised to emerge as one the few global steel producers. Tata Steel's strategy will pay off if consolidation in the European steel leads to a more stable pricing structure if not now, by 2011. Second, if potential customers like Toyota want to buy steel in different countries in Europe as well as in India, this would give global steel producers (like Tata Steel) a competitive advantage (Financial Times, 2007, February 1, 12). Clearly, the global steel industry and Tata Steel in particular will be closely watched in the years ahead, as some experts continue to maintain that the steel industry is a forecaster of overall global economic well-being.

DISCUSSION QUESTIONS

1. Did Tata Steel overpay for acquiring Corus?
2. Will Tata Steel's acquisition of Corus be viable in the long-term? What indications lead you to that conclusion?
3. What are the emerging trends in the worldwide steel industry? How did these trends potentially affect Tata Steel's bid for Corus?
4. What cross-cultural issues have been of concern in the Tata Steel acquisition of Corus? Do you believe that these issues have been addressed? How were the issues uniquely different from those raised by the merger of British Steel and Hoogovens when Corus was originally formed?
5. Will this acquisition have an impact on other Indian firms that are increasingly seeking an international presence?

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TEACHING NOTE

ACHIEVING GLOBAL GROWTH THROUGH ACQUISITION: TATA'S TAKEOVER OF CORUS

The case is appropriate for use in graduate courses in Strategy or International Business. This case should be assigned when covering chapters that address entry modes into new markets and/or those that discuss mergers and acquisitions. First, it can be used to discuss industry trends and pricing dynamics in the world steel industry. Second, it can also be used to illustrate growth by acquisition--a widely used strategy undertaken by many firms that are seeking a global presence. Third, it enables MBA students to gain country insights about India--a rapidly emerging economy which is poised to become an economic powerhouse over the next ten years. Last, the case can be used to discuss cross-cultural complexities of cross-border acquisitions. Of course, the instructor can choose to integrate the above mentioned viewpoints in a number of ways to achieve a synergistic effect when assigning this case to students. The primary focus of this case concerns the long-term viability of Tata Steel's acquisition of Corus. Secondary objectives examined in this case include a discussion of emerging trends in the global steel industry, post-acquisition issues facing Tata Steel (including financial and cross-cultural issues), and the impact of this particular transaction on the mindset of other Indian firms that are increasingly seeking an international presence.

CASE SYNOPSIS

The case is decision-based and uses secondary data sources. Tata Steel (part of the Tata Group based in India) acquired the Anglo-Dutch steel firm Corus after a four month bidding war with Brazil's CSN (Companhia Siderurgica Nacional SA) for US$11.3 billion—this was the biggest acquisition by an Indian firm. Tata's acquisition of Corus made it the fifth largest global steel producer with an annual capacity to produce 25 million tons of steel. The acquisition was intended to give Tata Steel access to European markets and to achieve potential synergies in the areas of manufacturing, procurement, R&D, logistics, and back office operations. Critics claimed that the acquisition price at 608 pence per share was substantially higher than an earlier offer of 455 pence per share. Additionally, they felt that it would take several years for potential production and operational synergies to materialize that would yield significant cost savings boosting financial yield. Tata Steel's stock suffered a significant decline in price causing Standard & Poor's to place it on a credit watch list with negative implications. Did Tata Steel overpay for acquiring Corus? What is the long term possibility of realizing proposed synergies? Will Tata Steel's gamble of being a global steel player payoff in the long run? Will Tata Steel be able to sustain itself during the global economic crisis?

DISCUSSION QUESTIONS

1. Did Tata Steel overpay for acquiring Corus?

There are two very different viewpoints that are presented in the case. Most financial analysts familiar with the acquisition felt that Tata Steel overpaid for Corus and acquired significant debt along the way. They felt that there were too many "ifs" along the way for this acquisition to be successful in the long run. Tata's initial offer of $8 billion at 455 pence per share ended with a final offer of $12 billion at 608 pence per share. Tata Steel also picked up the responsibility of ensuring that the pension funds of over 47,000 Corus's employees were adequately funded.

The opposing view is that of Tata Steel's executives, who felt that they paid a fair price for acquiring Corus Steel. Through this acquisition, they added 19 million tons of production capacity vaulting the new entity to become the fifth largest steel maker in the world. According to Ratan Tata, starting a greenfield venture in Europe and building a strong brand name would have been more expensive that the current Corus production cost of $710 per ton. Tata Sons, the holding company was going to infuse $4.1 billion in capital through a mixture of debt and equity. Tata Steel's executives always felt that Corus's cash flows were more than sufficient to meet the debt incurred due to the acquisition and that due to synergies and cost savings they would be able to realize a savings of $350 million.

The real answer as to whether Tata Steel overpaid for Corus may lie in the long-term value of the merger to Tata. Having been unable to predict the global drop in demand for steel that began shortly following the merger, Tata has since found itself facing questions of survival that center around issues of viabilities of economies and international competitiveness. It could be argued that the merger with Corus, which resulted in a marked boost in the company's revenues, has contributed to the long-term viability of the firm. It resulted in bolstering Tata Steel's reputation, putting the company on the Fortune 500 list, and increasing the likelihood that Tata will be able to sustain itself during the economic downturn.

2. Will Tata Steel's acquisition of Corus be viable in the long-term? What indications lead you to that conclusion?

There are many points that support the viability of this acquisition in the long-term.

First, the acquisition was part of a well thought and articulated strategy; Ratan Tata had emphasized the need to go global for all companies that were part of the Tata Group. Tata Steel was one of the lowest cost steel producers in the world and had access to abundant supplies of iron-ore. Tata Steel was seeking access to well established European markets. Corus Steel was a well established brand name in Europe but was not cost-effective in its operations. Having acquired Natsteel and Millenium Steel, the Corus acquisition was part of Tata Steel's long-term strategy to achieve a global presence to service global buyers in multiple locations.

Second, the proposed long term synergies involve the low cost resources of Tata Steel combined with the high-tech research aspects of Corus. The potential cross-fertilization of research and development capabilities with transfer of technology and best practices from Europe will help Tata Steel operations. The access to low cost raw materials and exposure to high growth in emerging markets should have combined with price stability in developed markets. The acquisition will position the combined group as the fifth largest steel company in the world by production output and will provide a meaningful presence in both Europe, where Corus is a well-established brand name, and Asia, where Tata is a well-established brand name. Tata Steel quickly formed teams to work on synergies in areas of manufacturing, procurement, logistics, marketing, iron and steel making. The fifteen to eighteen teams consist of 3-4 members from both companies. Each team worked on realizing potential synergies by sharing know-how, adopting best practices, and information to develop efficient practices to aid cost reduction.

Third, Tata Steel paid attention to the cross cultural issues that had led to less than successful mergers previously. Tata Group had learned from their overseas acquisition experiences the importance of managing cultural issues to enhance trust between the European and Indian sides. The teams formed to work on synergies should avoid potential cultural difficulties that could emerge from the dynamics of cross-border integration. Many of the Corus top managers have been retained to work with integration issues. Effective in May, Tata Steel appointed four key executives of Corus to its board of directors.

One indicator contrary to long-term viability is the encumbrance of Corus's pension fund which Tata Steel had to assume during the merger. That financial obligation may prove to be corrosive as equity markets continue to decline.

3. What are the emerging trends in the worldwide steel industry? How did these trends potentially affect Tata Steel's bid for Corus?

The worldwide steel industry experienced a great deal of global consolidation due to a few key factors that included a desire amongst the key players to gain efficiencies resulting from scale, to obtain access to new and growing markets, and to enhance purchasing power with respect to suppliers and buyers. Worldwide demand for steel continued to increase and steel prices were on an upward trend from 2004 to 2007. Production costs depended on having access to power and raw material and on manufacturing technology.

Steel companies increasingly had to decide whether to be an acquirer or an acquisition target. The latest rounds of mergers and acquisition activity were expected to eventually result in a handful of worldwide global giants in the steel industry. The key consolidation in the two years prior to the Tata/Corus merger was Mittal's merger with Arcelor to create the largest steel company in the world. Major Russian steelmakers Evraz Group and Severstal and Swedish steelmaker SSAB made acquisitions in North America and elsewhere and were pursuing more.

Pressure on Tata Steel to maintain a competitive major global presence and extend its influence in new and growing markets in view of increasing consolidation in the steel industry necessitated the merger.

4. What cross-cultural issues have been of concern in the Tata Steel acquisition of Corus? Do you believe that these issues have been addressed? How were the issues different from those raised by the merger of British Steel and Hoogovens that formed Corus?

Tata Steel approached the Corus acquisition with full awareness of the concerns that might arise due to cultural and racial obstacles caused by British employees resentful of having managers from a former British colony. There was also considerable concern among the European employees that Tata Steel would move production away from the UK to lower cost Indian markets. Tata Steel addressed these issues by allowing existing management to continue and by setting aside any more comprehensive restructuring for a later date. The top management teams were assigned the specific tasks of working with integration issues and building trust.

It is difficult to say that these issues were adequately addressed, especially since much of the resentment created by the merger stemmed from deep-seated animosities toward a country with former colonial attachments to the UK and ownership by new management of different racial and ethnic orientations. The psychic distance between the UK and India is much greater than that perceived to exist between UK and the Netherlands. Thus, the issues raised over the earlier merger were not as virulent.

5. Will this acquisition have an impact on other Indian firms that are increasingly seeking an international presence?

Judging from the reaction of the popular press in India, Tata Steel's acquisition of Corus was hailed as a bold and visionary move. Many Indian business men and women considered this acquisition as symbolic of India's growing ascendancy in the international business arena. The fact that India was once a British colony seems to have given this acquisition a different flavor--the colonizer is now being acquired by the colony! This acquisition did a lot to bolster the confidence levels of not only reputed larger sized Indian firms like Wipro and Infosys to seek overseas targets; it spawned a whole new breed of entrepreneurs who are ready to engage in takeovers of firms in emerging economies like Kazakhstan and other central Asian countries.