

)l

**GROWTH THROUGH MERGER: A CASE STUDY
OF GLAXOSMITHKLINE PLC) /**

**BY
JUNE WANGARI**

UNIVERSITY OF NAIROBI
LOWER KABETE LIBRARY

**A MANAGEMENT RESEARCH PROJECT
SUBMITTED IN PARTIAL FULFILLMENT OF THE
REQUIREMENTS FOR THE AWARD OF DEGREE
OF MASTER OF BUSINESS ADMINISTRATION
(MBA),
SCHOOL OF BUSINESS,
UNIVERSITY OF NAIROBI**



JULY, 2008

DECLARATION

I declare that this project is my original work and has never been presented for academic purposes in any other University.

CANDIDATE: JUNE WANGARI

DATE(91.

This research project has been submitted for examination with my approval as the University Supervisor

SIGNED. **DATE.** 

Prof. Evans Aosa
Department Of Business Administration,
School Of Business,
University Of Nairobi

DEDICATION

I dedicate this project to my daughter Jemima, who was born within the first year of my post graduate studies. And now that she is in kindergarten, I see that I have instilled in her the love for reading and learning and I trust that she will go very far.

ACKNOWLEDGEMENT

I thank God for seeing me through my studies as I tried to balance between my family, my work and my studies.

I wish to acknowledge the contributions that were made in the course of this project by several individuals and organizations. I wish to acknowledge gratefully the following people, whose effort influenced the content and direction of this project.

My first thanks go to my Supervisor Prof. Evans Aosa for his constant analytical criticism and encouragement. Thanks a lot.

I wish to thank my friends for a lot of support and encouragement to me in pursuit of this goal. My thanks also go to GSK managers that despite their busy schedules were available for the interviews and the financial support that saw me through this programme.

For all whose names have been indicated and many more who contributed, though their names have not been indicated, I say God bless you all.

Thank you.

TABLE OF CONTENTS

DECLARATION	II
DEDICATION	III
LIST OF TABLES	VII
LIST OF FIGURES	VIII
ABSTRACT	IX
CHAPTER 1: INTRODUCTION	1
1.1 Background.....	1
1.1.1 <i>Corporate Growth</i>	1
1.1.2 <i>The Pharmaceutical Industry</i>	5
1.1.3 <i>Glaxo SmithKline Pic</i>	9
1.2 Statement of the Problem.....	12
1.3 Objectives of the Study.....	13
1.4 Importance of the Study.....	14
CHAPTER 2: LITERATURE REVIEW	15
2.1 Environmental Dependence.....	15
2.2 Strategy.....	16
2.3 Strategic Response.....	19
2.4 Strategic Options.....	20
2.6 Mergers and Acquisitions.....	25
2.6.1 <i>Tijpes of mergers</i>	27
2.6.2 <i>Steps in a Merger</i>	28
CHAPTER 3: RESEARCH METHODOLOGY	30
3.1 Research Design.....	30
3.2 Data Collection.....	30
3.3 Data Analysis.....	31

CHAPTER 4: RESEARCH FINDINGS AND DISCUSSIONS	32
4.1 Company Profile.....	32
4.2 The Merger Objectives and Process.....	33
4.2.1 <i>The Objectives of the merger</i>	33
4.2.2 <i>The Merger Process</i>	36
4.3 Impact of the Merger.....	41
4.4 Challenges of the GSK Merger.....	47
4.4 Overcoming the Challenges faced.....	50
CHAPTER 5: SUMMARY, CONCLUSION AND RECOMMENDATIONS	54
5.1 Summary.....	54
5.1.1 <i>Documenting Glaxo Wellcome and SmithKline Beecham merger process</i>	54
5.1.2: <i>Establishing whether the merger objectives were met</i>	55
5.2 Conclusions.....	58
5.3 Recommendations for Further Study.....	58
5.4 Limitations of the study.....	59
REFERENCES	60
APPENDIX 1: LETTER OF INTRODUCTION	63
APPENDIX 2: INTERVIEW GUIDE	64

LIST OF TABLES

Table 1: Impact of Merger on Share Price.....	41
Table 2: GSK Position after Merger.....	42

LIST OF FIGURES

Figure 1: GSK Global Presence.....	11
Figure 2: Market Options Matrix.....	20
Figure 3: Stronger Product Line.....	42
Figure 4: Research & Development Productivity.....	43
Figure 5: Products in R&D Pipeline.....	44
Figure 6: Position in Late Stage Product Pipeline.....	45
Figure 7: Growth in Reputation in Supply of HIV drugs to Africa.....	46

ABSTRACT

Organizations today are faced with a lot of challenges. Globalization and liberalisation of economies has put pressure on businesses, not to mention increased demand from investors for higher productivity, greater efficiencies, higher quality of goods and services and higher levels of innovation. As a result, managers need to develop strategies that should gain them competition advantage over their competition and possibly eliminate competition all together.

This is a case study about the merger process and objectives of GlaxoSmithKline (GSK) Pic whose aim is to provide an in-depth understanding of how Glaxo Wellcome and SmithKline Beecham merged to form GlaxoSmithKline Pic in 2001.

The objectives of the study are to document the process of the Glaxo Wellcome and SmithKline Beecham merger and to establish whether the merger objectives were met.

Data for this study was collected through interviews of Senior Managers at GSK and also by use of a non-structured questionnaire. Given the qualitative nature of the data obtained, the mode of analysis used was content analysis.

The study findings indicate that the objectives of the merger were to take advantage of rapid advances in scientific discoveries and technology and

increased consumer knowledge. The increased competition in the pharmaceutical industry meant that it made economic sense for these two powerhouses to merge and to combine skills and resources.

The study managed to document the process of the merger and also established that the merger was a success and the objectives of the merger were met. The study found that this was a merger where neither set of shareholders receives a premium over the market value of their shares before the transaction is announced and was termed as transaction of equals. On completion, GW shareholders held approximately 58.75% of the issued ordinary share capital of GlaxoSmithKline and SB shareholders held approximately 41.25%.

The study concluded that despite the fact that mergers have their own pitfalls, certainly some mergers are a perfect fit of two companies which complement each other's strengths, have obvious benefits and enable the companies to make massive economies of scale. This enables them to win customers and new business while keeping costs down and still fund the billions necessary for research and development.

This study recommends that further research be undertaken to determine the survival of mega mergers and establish the reasons for their post merger survival or death.

Several limitations were encountered during this study. The merger process was controlled from the United Kingdom and the people directly involved in

the merger are located there. However, it would have been very costly to travel to the United Kingdom to obtain my interviews, not to mention that getting appointments for interviews would have been very challenging. Also, many people who were with the company then have since left to pursue other interests elsewhere. I therefore had to contend with interviewing local current management who helped piece together relevant merger information verbally and from data published in the internal employee magazines.

CHAPTER 1: INTRODUCTION

1.1 Background

1.1.1 Corporate Growth

Organizations today are faced with a lot of challenges. These include increased competition, changes in government fiscal policies, demand from various pressure groups, legal factors, changes in government laws and regulations, changes in the global expectations of the working environment, increased consumer or customer expectations, advancement of technology and general economic slump. Globalization and liberalisation of economies has put pressure on businesses, not to mention increased demand from investors for higher productivity, greater efficiencies, higher quality of goods and services and higher levels of innovation. In addition, businesses have found themselves under pressure to be more accountable and responsible to the wider group of stakeholders: suppliers, employees, government, communities and the general public, (GSK Corporate Communications, 2000). As a result, managers need to develop strategies that should gain them competition advantage over their competition and possibly eliminate competition all together.

Management's responsibility to shareholders is to improve shareholder value by ensuring that the organization is equipped with adequate resources to meet day to day challenges, as well as develop strategies that will help it overcome any unforeseen challenges in the future (Kay, 1993). Having

analysed the environment in which the firm operates and identifying the opportunities that exist, as well as its capabilities to enable it tap into these opportunities, the firm has several strategies to choose from in order to achieve its overall objectives and to gain competitive advantage.

According to Porter (1998), competition is at the core of the success or failure of firms. Competition determines the appropriateness of a firm's activities that can contribute to its performance, such as innovation, a cohesive culture, or good implementation. Hence competitive strategy is the search for a favourable position in an industry within which the firm operates. A firm that gains competitive advantage within an industry will in most cases gain in increased market shares, reduced costs, gain new markets and hence, improve profits. The strategic option for a firm depends on the environment it operates in and the resources the firm has to help it overcome the challenges it faces. Hence, the firm has strategic options that are market driven and the environment's response will determine whether the firm will achieve its objectives. These environment- based options would include market options and expansion methods.

According to Lynch (2000), market options would include strategies like market penetration, where the firm uses its current products or services to gain market share, either through improved quality, increased marketing activities or improved productivity. On the other hand, the firm may choose market development where it uses the current product range to reach new

markets. The firm may also choose to develop new products and sell them in the current market segment, hence gaining market share. The firm may also choose to diversify either into related markets where it is familiar with or into unrelated markets, where it feels it has capabilities to explore and make profits.

Innovation is another strategy that firms can use to ensure sustainable growth. According to Pearce and Robinson (1997), companies that have adopted innovation as their growth strategy seek to reap the initial high profits associated with customer acceptance of a new or greatly improved product.

Many companies find themselves faced with the global race to build a market presence in many different national markets, and to establish an attractive position among the global market leaders, not to mention the technology race to capitalise on today's technological and information age revolution (Thompson and Strickland 2003). In such cases, strategic alliances and collaborative partnerships have emerged as an attractive and timely means of breaching the technology and resource gaps that firms encounter today.

As a result, firms have selected different options to expand to other markets through licensing/contract manufacturing, where a firm contracts another to manufacture on its behalf, joint ventures where two or more firms agree

to collaborate on pooling of capital, production and marketing of products or services. Another option would be franchising, which may include manufacturing, marketing, selling and distribution of products or services of the franchiser. Other strategies used by firms to expand their markets will be through exporting, which involves selling of the firm's products or services to another firm or distributors in the targeted country.

Other options that firms may take include foreign branching where the company extends its operations in foreign markets and controls maintained within the host country and on the other hand, foreign subsidiaries, where the parent company still maintains control in all aspects of the subsidiary's operations.

Lynch (2000) argues that strategists concentrating on the resource-based view now regard generic strategies as being largely historic. Resource-based strategies are those strategies that are used by a firm and will mainly involve fortifying the firm's distinct competencies. This enables a firm to achieve organic growth and would include options like analysing the value chain and the processes involved to eliminate waste, analysis of the firm's capabilities vis-a-vis the desired standards within the industry or firm, and cost reduction strategies to enable the firm improve profits.

Mergers and acquisitions have also been options that firms have used especially where it is believed that alliances and partnerships will not deliver

the desired resources and capabilities. According to Rowe (1994), mergers effected for strategic reasons can be beneficial to both the acquiring company and the company acquired. According to Thompson and Strickland (2003), a merger is a combination and pooling of equals, while an acquisition is when one company buys out another. On one hand, acquisitions may offer the acquiring firm with a source for its inputs or raw material, or customers to its outputs, hence vertical integration. On the other hand, acquisitions will eliminate competition and provide access to new markets (Pearce and Robinson 1997). According to Pfeffer (1972), companies may seek to merge to reduce competition by absorbing an important competitor, to manage interdependence with either sources of inputs or purchasers of output by absorbing them and to diversify operations and thereby lessen dependence on the present organizations with which a company exchanges.

1.1.2 The Pharmaceutical Industry

The origins of the pharmaceutical industry are primarily post war. Over time, technological advancement has played a key role in the growth of this industry. The current directory of pharmaceutical companies shows that there are 140 listed pharmaceutical companies in the world, (Emerge 2000b). While the U.S. market (estimated to contribute 41 percent of worldwide pharmaceutical sales in 2004) continues to set the pace, Europe and Japan are also major players, combining to contribute about 39 percent of global pharmaceutical sales in 2004. The pharmaceutical industry

markets two segments of pharmaceutical products; over-the-counter pharmaceuticals, which a patient or customer can pick off the shelf as required, and prescription only pharmaceuticals, which are issued to patients on prescriptions only from qualified doctors. The world pharmaceutical market is one of fastest growing and most profitable sectors of the world economy. However, the \$541.0 billion market is witnessing unprecedented changes.

Such changes include rapid advances in science and technology which leads to a better understanding of the genetic causes of diseases and increased number of potential targets for therapeutic intervention as well as faster development of drugs, hence being first in developing new products is key. This has led to high cost of healthcare against the fact that the Gross Domestic Product is not increasing at a rate sufficient enough to offset the rises in costs.

Patients are becoming more involved in healthcare decisions and are becoming more aware of the products available to treat diseases, (Emerge 2000b). Hence, pharmaceutical firms need to be more thorough in ensuring that the drugs they offer are of the highest quality. This has put pressure on the cost of selling drugs as companies now have to allocate more resources in the marketing and selling of their drugs to convince patients to make the purchase.

Over the last decade, there has been a strong growth of the generic industry that has come about due to expiry of patented products. This industry offers drugs of similar generic efficacy at very low prices, not to mention the emergence of parallel imports that originate from countries with low fixed costs, thus eroding revenues in higher fixed costs countries.

As a result, reduced revenues have led to inadequate investment in research and development, the backbone of the pharmaceutical industry. According to Lee, Fisher and Yau (1986), of all the areas to which managers allocate resources, investment in research and development have the longest time frame, offer the least certain outcome, and face the murkiest competitive environment. Furthermore, the funds expended on research and development come directly from current earnings, but the rewards if they materialize at all, contribute only to distant future earnings. However, problematic as it is, effective research and development for pharmaceutical companies is essential to survival and if neglected underfunded or misdirected, the consequences may be fatal and hinder further growth and discoveries of new drugs to combat the ever evolving diseases (GSK Corporate Communications, 2000c).

Besides the pharmaceutical producers and marketers of pharmaceutical products, there are other stakeholders in this industry that are key players in the success of this industry and are all very important. We have clinicians who are well- trained and determine what drugs they will

prescribe to their patients. This has put significant pressure on pharmaceutical firms to develop well trained salespeople with the ability to influence the brands that clinicians prescribe to their patients. Personal selling becomes very important in this industry.

We also have the patients who have become knowledgeable in the diseases that are affecting mankind and the treatment options that are available often resulting to self medication. As such, the industry's response is to develop products for specific patient groups.

Because of the competitive nature within the industry, mergers and acquisitions are the order of the day. Several mergers and acquisitions in the recent past have taken place for example, between Hoechst Marion Roussel (HMR) and Rhone Poulenc to form Aventis (1999), Glaxo Wellcome and SmithKline Beecham to form GlaxoSmithKline (2001), Pfizer and Warner Lambert to form Pfizer (incl WL) in (2002), Astra AB of Sweden and Zeneca Group PLC of UK to form AstraZeneca (1999), acquisition of Aventis by Sanofi Synthelabo (2004), among others. Others have been strategic alliances with small research and development and biotechnology companies on the basis that funding research may bring about the discovery of new blockbuster drugs. Other firms have considered relocating activities to more investment friendly regions, while others opt to shut down altogether. Some firms have entered into the manufacture of generic drugs, others have opted to sign up sales, marketing and distribution activities

with third party agents to reduce on costs and more severely cut down on research and development.

1.1.3 GlaxoSmithKline Pic

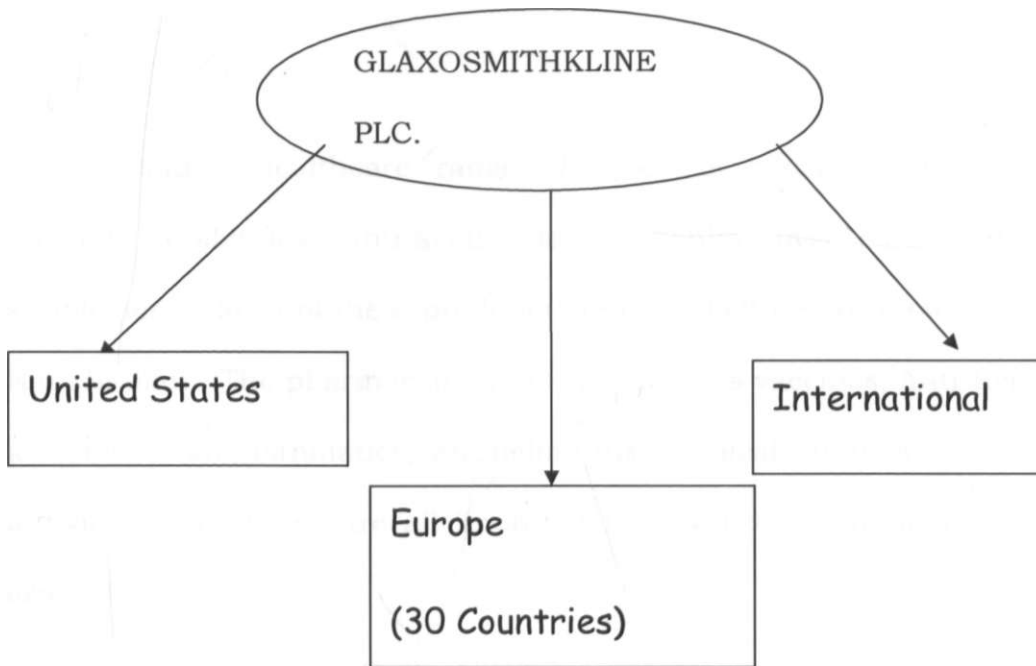
GlaxoSmithKline Pic was formed as a result of a merger between Glaxo Wellcome and SmithKline Beecham. However, each of these two companies has different origins and mergers and acquisitions are not new to them. The Glaxo group has its origins in New Zealand and was established in 1873 as Joseph Nathan & Co., (GSK Corporate Communications, 2000). After moving to London, it acquired an interest in Glaxo's Indian agents, H. J. Foster & Co and later the company was renamed Glaxo India (Private) Ltd. in 1950 and finally evolved into Glaxo India Ltd. in 1989. In 1880, meanwhile, Henry Wellcome and Silas Burroughs had established Burroughs, Wellcome & Co. in London and in 1924 Henry Wellcome established The Wellcome Foundation Limited. In 1967, it acquired medical, consumer and hygiene service company Calmic Ltd., and bought a supplier of dairy hygiene products, Hadleigh- Crowther in 1969. Again in 1971, it acquired Macdonald Taylor, a surgical dressings company. In 1995, Glaxo and Wellcome merged to form Glaxo Wellcome.

SmithKline Beecham was formed in July 1989 as a merger between SmithKline Corporation and Beecham PLC. Its origins date back to 1830, when John Smith established a small apothecary shop and drug wholesaler's in Philadelphia. Smith was joined by other wholesalers and the

company was renamed SmithKline Corporation. Back in England meanwhile, Thomas Beecham, a shepherd boy in 1820s discovered that his flock tended to eat certain vegetation in certain conditions. Experiments showed that these herbs had medicinal qualities and the eventual outcome was Beecham pills. By 1913, the company was producing a million pills each day and over the next 40 years, it diversified into cosmetics, drinks, foods and adhesives through the acquisition of brands like Lucozade, Brylcreem, Eno, Ribena and Macleans. In 1994, SmithKline Beecham acquired Sterling Winthrop to give it the largest consumer healthcare business in Europe and Latin America.

Hence, it is clear that the GlaxoSmithKline merger was not the first for the two merging companies. Glaxo Welcome and SmithKline Beecham merged in 2001 to form GlaxoSmithKline. At the time of the merger, GlaxoSmithKline Pic was the leading pharmaceutical company in the world with a market share of 7% and today, it is second to Pfizer with a market share of 7.8% (US \$30 billion annually) of the world's drug market. GlaxoSmithKline Pic operates across three regions as shown in Figure 1.

Figure 1: GSK Global Presence



Source: GSK Corporate Communications, 2001e

GlaxoSmithKline's headquarter is in the United Kingdom. The United State's market is the largest market and is run from two offices in Pennsylvania and North Carolina. GlaxoSmithKline employs over 104,000 employees worldwide. GlaxoSmithKline East Africa is within the International market and houses three strategic business units which have a common shared service which includes human resources, finance, purchasing, customer service, information technology and medical and regulatory affairs department. The strategic business units are The Pharmaceutical Division, The Consumer Healthcare Division and the Global Manufacturing and Supplies, (GMS). These are housed at the GlaxoSmithKline plant in

Nairobi's Industrial Area, with each unit headed by a General Manager. The East African market serves 11 countries of Kenya, Uganda, Tanzania, Rwanda, Burundi, Ethiopia, Eritrea and Djibouti, Mauritius, Seychelles and Madagascar.

The consumer healthcare range of products marketed in East Africa includes analgesics, anti-acids, health drinks, oral care and vitamin supplements. Most of these products are manufactured or repackaged in the Nairobi plant. The pharmaceutical range includes vaccines, Anti-Retrovirals, antibiotics, antiasthmatics, antihelminthes, topical steroids, antimalarials, antivirals, etc. These are all imported from various manufacturing plants around the world.

1.2 Statement of the Problem

Mergers can successfully lead to reduced competition, new products, quality staff, reduced costs and hence more growth. However, mergers can also fail due to resistance to change by staff, budgeted cost savings not realised, disagreements regarding control of new company, incompatible business cultures, key people leave and time spent on negotiations.

The last 10 years has seen the pharmaceutical industry come under pressure. The pressure to develop new molecules for drugs that are being considered resistant, the expiry of patents which attracts generics into the markets, the high costs of developing these drugs and the ever demanding

consumer. This has put pressure in the resources that firms have to invest in their businesses. As a result, many firms in this industry have merged or acquired other firms so as to increase the base of their resources, which can in turn be re-allocated to key aspects of the business to enhance growth. However, the key question after a merger is whether the desired objectives were met.

The GlaxoSmithKline merger was between two leading pharmaceutical companies that were facing the challenges outlined in this paper. Mergers are delicate and things could go wrong. However, it would appear that the GlaxoSmithKline merger has been a success as the company has realized its set objectives. This study will help the beneficiaries understand how GlaxoSmithKline overcame the problems and challenges that came along and is an important study to help scholars understand: What was the process that went into realizing this merger? Were the objectives of the merger met?

1.3 Objectives of the Study

- To document the process of the Glaxo Wellcome and SmithKline Beecham merger.
- To establish whether the merger objectives were met.

1.4 Importance of the Study

The study will provide a basis for debate for academicians, as to whether mergers do really offer benefits to the organization. This will hence provide a link between theory and practise.

The study will also detail the process of the merger that will be helpful to other firms considering the same strategy by providing a deeper understanding of the process. The study will also benefit the general public as a point of knowledge, of how the merger took place.

Merger process is an international strategy used by companies to solve several organisational challenges. This study therefore provides insight into how the process is undertaken and the challenges that may require this strategy to be employed and the types of mergers that can be adopted.

CHAPTER 2: LITERATURE REVIEW

2.1 Environmental Dependence

Firms rely on the environment for its inputs of production. Raw materials, financing, physical assets, labour, etc are all provided by the environment. These inputs are utilised by the firms to produce goods and services that are put back into the environment for consumption. Hence, firms cannot exist without the environment. On the other hand, the environmental circumstances keep changing. This calls for organizations to be more flexible in the strategies they make so that they are able to accommodate the various changes within the environment they operate (Ansoff and McDonnell, 1990).

According to Ansoff and McDonnell, (1990), during the twentieth century, environmental changes have become more complex and novel. The increasing frequency of change has affected many business firms as well as the rate of diffusion of change, i.e. the speed with which new products and services invade markets. The implications of the acceleration of change to a business would mean that there is increased difficulty in anticipating change well in advance to plan a timely response. In this case, firms would need to increase the speed of implementation of the response to market changes. There would be need for flexibility and timely response to surprises which would not be anticipated in advance. This has put pressure on firms to adopt management systems that will help them succeed in the future.

Market intelligence or environmental scanning becomes very important to firms. Strategic surveillance is designed to monitor a broad range of events inside and outside the firm that are likely to affect the course of a firm's strategy (Pearce and Robinson, 1991). Information is power and collecting, analysing and communication of information on competition, market changes, changes in consumer behaviour, changes in governmental policies, global trends and other aspects that could affect the business's strategic direction is crucial for every organization today. Organizations are greatly influenced by the customers, suppliers, rivalry within the industry, availability of substitute products and barriers to entry into an industry and information regarding all these aspects will help the firm develop the appropriate strategies to succeed.

2.2 Strategy

Many authors have attempted to define normatively the term strategy, derived from the Greek word *strategos*, 'art of the general' (Capon, 1987). Andrews (1971:25) defines corporate strategy as 'the pattern of major objectives, purposes, or goals and essential policies and plans for achieving those goals stated in such a way as to define what business the company is in or is to be in and the kind of company it is or is to be'. Hofer and Schendel (1978) discussed strategy in the context of the strategy formulation process, which involves deciding the company's mission, its

objectives, and the major policies governing the use of the firm's resources to achieve its objectives.

According to Mintzberg (1988), strategy is a plan that is consciously made, hence an intended course of action. In this respect, strategies are made in advance of the actions to which they apply and they are developed consciously and purposefully. They may be formally documented in a plan or remain formally unstated though still very clear in one's mind. As a plan, strategy can also be a ploy; a specific manoeuvre intended to outwit an opponent or competitor. Mintzberg continues to argue that if strategies can be intended, then they can also be realized. Realized strategies are those strategies that an organization has really achieved, therefore, developing a pattern in a stream of actions. Hence strategy is consistency in behaviour, whether or not intended.

Traditionally, strategy has been defined as the process of aligning the internal capabilities of an organization with the external demands of its environment (Rowe 1994). The process has focused on the changes in the environment that led to opportunities and threats to which firms had to adjust. How a firm adjusts its internal capabilities will determine how successful it will remain. Rowe (1994) further reports that a number of studies have shown that differences in profitability within industries are more important than such differences between industries; that is, some

companies consistently continue to thrive in difficult environments while others do not succeed even though their industry is very healthy.

Strategy is a deliberate search for a plan of action that will develop a business's competitive advantage and compound it. The search begins with recognition of where you are and what you have now (Grant, 1998).

By strategy, managers mean their large-scale future-oriented plans for interacting with the competitive environment to achieve company objectives. A strategy is a company's "game plan" (Pearce and Robinson, 1991). Although that plan does not precisely detail all the future deployments of people, finances and materials, it provides a framework for managerial decisions. Further to this, a strategy reflects a company's awareness of how, when, and where it should compete, against whom it should compete and for what purposes it should compete. They further define strategic management as the set of decisions and actions that result in the formulations and implementation of plans designed to achieve a company's objectives.

According to Ansoff and McDonnell (1990), strategic management is a systematic approach to a major and increasingly important responsibility of general management: to position and relate the firm to its environment in a way which will assure its continued success and make it secure from surprises.

2.3 Strategic Response

Strategy prepares the firm to face its complex external environment, and using its corporate capability, develops responsiveness to anticipated threats and opportunities. The firm will not be able to conquer the challenges of the future if it does not have the capabilities to do so. In a discontinuous environment, historical strengths become the weaknesses of tomorrow. Ansoff and McDonnell (1990) describes further that when discontinuous change impacts on the firm, two costs are incurred, the cumulative loss of profit, and the cost incurred in arresting or, reversing the loss. The management problem is to minimize the sum of the two losses by restoring profitability of affected product lines, or by shutting down the operations that support them. The speed with which such challenges occur means that the firm should be in a position to respond with similar speed. According to Barnett (1989), the strategic manager asks if the formulated strategy is appropriate in view of the firm's strengths and weaknesses versus those of potential competitors. In preparation, the manager has searched the environment for competitive threats and the manager must analyse not only the present competitive threats, but the future responses of competitors.

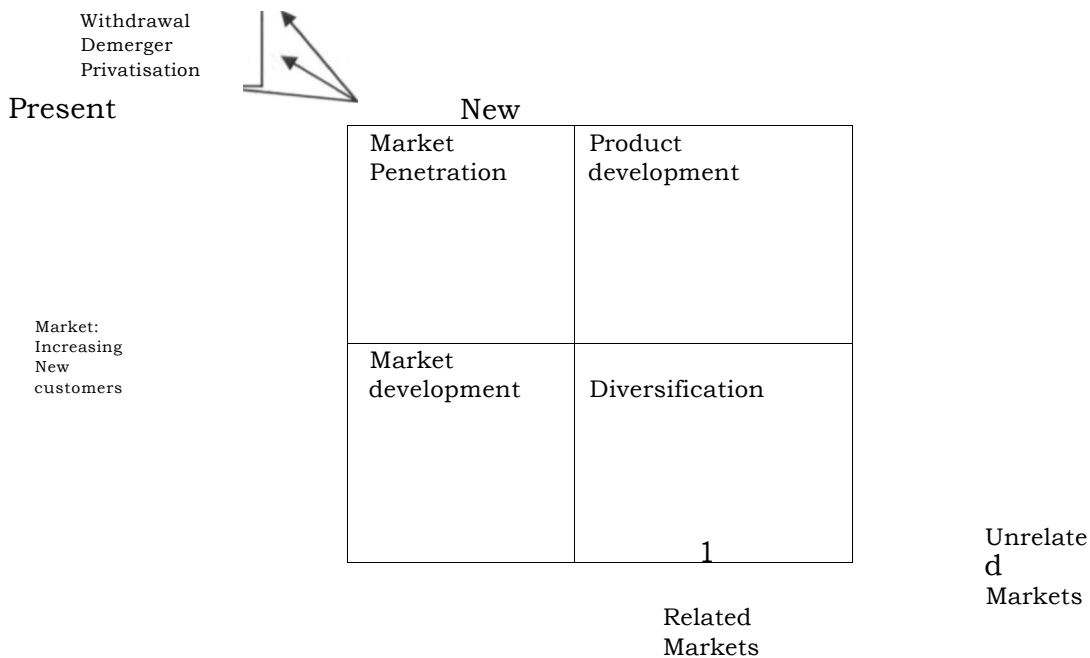
An important implication of the firm-strategy-environment framework is the concept of strategic fit. If the internal capabilities of a firm do not match the strategy, then a capability gap arises. Strategic response requires firms to change their strategy to match the environment which would involve transformation or redesigning of their internal capabilities to match the

strategy. If this fit is not realised, a strategic gap exists. According to Grant (1998), for a strategy to be successful, it must be consistent with the firm's goals and values, with its external environment, with its resources and capabilities, and with its organization and systems.

2.4 Strategic Options

A firm has several strategic options to select from. Whether it uses one or a combination, it must have the capabilities to implement the strategy, so as to get the desired results. Strategies that are market driven would not only give the options of new products and moving to new markets, but also explore the possibility of withdrawal from markets and moving into unrelated markets as represented in figure 2 below.

Figure 2: Market Options Matrix



Source: Lynch R., (2000) **Corporate Strategy, Second Edition**, Aldersgate Consultancy Limited.

A firm may find itself selling or withdrawing a product whose life cycle is in the declining phase with no possibility of saving it, in which case the firm opts to discontinue the product. Other possible reasons for withdrawal would be due to over-extension of the product line, hence withdrawal of some lines to give more focus on existing lines, the firm may be holding subsidiaries for sale when the price is right, or may sell an asset to raise capital to invest elsewhere.

In other instances, demerger, where a firm splits up to form two separate entities, may become an option. This works well especially if the firms are specialised in different products or services. According to Lynch (2000), this strategy has been used especially by public quoted companies, to realise the underlying asset values. It also allows for more focus such that each part is able to focus on its core activities without competing for scarce resources. However, it may destroy the benefits of size, cross-trading and uniqueness of a larger company.

Many government organizations are selling the organization's shares into private ownership. The changes in the levels of service, new product range and general perceptions have been significant. Privatization has seen many firms previously owned by the government start to make profits and improve employee morale, leading to improved service delivery.

Market penetration strategy allows a firm to maintain or gain market share in its current market with its existing products. According to Banerjee (1999), a firm may gain market share by improving the quality of its products, improving its productivity and increasing its marketing activities.

On the other hand, in market development, the firm moves to attract new customers with its existing range of products and services. These may come in form of new segments, new geographical areas or new uses for its products. Hence exporting and internationalization are important in market development.

A new product almost instantly wins a firm new customers and improved market share. However, there must be genuine improvement in performance and a significant contribution to sales and profits to consider the new product a success. Sometimes new products push firms into new markets or attract new users and Lynch (2000) further indicates that this is part of the natural growth of many companies.

A firm may opt to diversify within its related markets or may diversify in unrelated markets. The firm moves from its current products and markets into new areas. Moving into related markets means a market that has some existing connection with its existing value chain. Synergy is the main reason given to such a strategy. The value to be generated by owning and controlling more of the value chain is greater because the various elements

support each other. Diversification into unrelated areas comes with significant risks and uncertainties. Synergy in this strategy may be from financial reasons, or there may be opportunities to employ existing underutilised resources in a new field, or the desire to move into a different area of activities perhaps because the current one is in decline.

The methods by which market options might be achieved depend on the level the firm is operating in. Within the home country, the methods of expansion usually used are through joint ventures, franchising and alliances, innovation, acquisitions and mergers (Lynch, 2000).

A joint venture is the formation of a company whose shares are owned jointly by the two parent companies while an alliance is a weaker contractual agreement or even minority shareholding between two parent companies (Lynch, 2000). According to Roberts (1980), to meet ambitious plans for growth and diversification, corporates are turning in increasing numbers to new venture strategies, as no other strategy for enhancing growth in size or profitability currently offers a higher probability of success. These would include venture capital, where a firm invests money in the stock of another firm: venture nurturing, where a firm provides capital investment and managerial assistance to another firm: venture spin off, where firm may develop an idea or technology that does not fit its mainstream interest, hence, spin off the new business as a separate corporation: New style joint ventures, where large and small firms enter

jointly into new ventures and the combination of resources allows for the rapid diffusion of technology-based product innovations into large national and international markets: Venture merging and melding, where the firm combines with another to gain competencies in other areas and new markets: and Internal ventures, where a firm sets up a separate entity within itself for the purpose of entering different markets or developing radically different products.

A franchise is a form of licensing agreement in which the contractor provides the licensee with a pre-formed package of activity which may include manufacturing, distribution and selling. Licensing is a form of franchising common in science and engineering based industries. The parent company licenses another firm to manufacture on their behalf and the licensee pays the parent company a fee, usually a percentage of its turnover.

Innovation has also been adopted by other firms as a strategy towards growth. Rather than face stiffening competition as the basis of profitability shifts from innovation to production or marketing competence, innovating firms seek for other original or novel ideas (Pearce, 1997). The rationale of the innovation strategy is to create new product life cycle while making similar existing products obsolete. Beyond the home country, more options exist including exporting, setting up overseas offices and undertaking full manufacturing, setting up multinational operations and introducing global operations

2.6 Mergers and Acquisitions

According to Thompson (2003) an acquisition is when one company, the acquirer, purchases and absorbs the operations of another, the acquired, while a merger is a combination and pooling of equals, with the newly created company often taking on a new name. Strategic fit implies that the merger is synergistic and that the new combined firm produces more benefits to the stakeholders than the two did separately before the merger. Hence, the most common objective of companies entering a merger is to expand the business and to enable firms to operate more efficiently.

Depending on the type of mergers, some mergers are likely to lessen competition. That, in turn, could lead to reduced availability of goods and services which will in turn drive prices up. The quality of goods and services produced may be compromised as there is not much to benchmark against and generally innovation would cease to be a priority. However, more and more companies are finding mergers and acquisitions the quickest route companies have to new markets and to new capabilities. The legendary merger mania of the 1980s, pales beside the mergers and acquisitions of this decade. In 1998 alone, 12,356 deals involving U.S. targets were announced for a total value of \$ 1.63 trillion compared to 4,066 deals worth \$378.9 billion announced in 1988 (Rappaport, 1999).

Mergers or acquisitions tend to drive up the stock price of the targeted company; however, if a company is acquired by issuing junk bonds, the

capital structure is changed (Rowe 1994). In this case the stock prices may rise in the short run, but shareholder value may suffer in the long run. In mergers, there will be job cuts especially where there is duplication of roles, or the so-called 'non essential' positions. Some of these may be in research and development, the life-force to many companies, and cutting on this budget may lead to the eventual demise of a company. Rowe (1994) further argues that conflicting corporate cultures leads to failure of many mergers.

The ability to adapt is a key determinant of the success of a merger. On the other hand, introduction of change often creates fear and anxiety. As a result, there is opposition, sabotage, neglect or inaction towards the change and this could lead to failure of a merger. The strategic fit of the merging companies is very important. Large-company mentality and structure can destroy the enthusiasm that makes high-tech and entrepreneurial companies successful. The large company culture demands management discipline but the imposition of tight controls and red tape inhibits creativity for the entrepreneurial company. This often leads to a decline of morale and the drive to be the best often disappears. This could see key employees leave the company which may hamper growth for the company (Rowe, 1994).

According to Rowe (1994), a successful merger will involve four key considerations: the executive who becomes the change agent, the culture which reflects the change environment, the values of the individuals whose

activities affect the change process and the match between pre-merger values and culture and those of the new entity. This is because making the merged company a cohesive, compatible company can become a nightmare.

2.6.1 Types of mergers

In business or economics a merger is a combination of two companies into one larger company. Such actions are commonly voluntary and involve stock swap or cash payment to the target. Stock swap is often used as it allows the shareholders of the two companies to share the risk involved in the deal. A merger can resemble a takeover but result in a new company name (often combining the names of the original companies) and in new branding; in some cases, terming the combination a "merger" rather than an acquisition is done purely for political or marketing reasons. A merger is a tool used by companies for the purpose of expanding their operations often aiming at an increase of their long term profitability. Usually mergers occur in a consensual (occurring by mutual consent) setting where executives from the target company help those from the purchaser in a due diligence process to ensure that the deal is beneficial to both parties ([www.wikipedia.com / mergers](http://www.wikipedia.com/mergers)).

Historically, mergers have often failed (Straub, 2007) to add significantly to the value of the acquiring firm's shares (King, et al., 2004). Corporate mergers may be aimed at reducing market competition, cutting costs (for example, laying off employees, operating at a more technologically efficient scale, etc.), reducing taxes, removing management, "empire building" by the

acquiring managers, or other purposes which may or may not be consistent with public policy or public welfare. The types of mergers are as follows:-

1. Horizontal mergers take place where the two merging companies produce similar product in the same industry.
2. Vertical mergers occur when two firms, each working at different stages in the production of the same good, combine.
3. Congeneric mergers occur where two merging firms are in the same general industry, but they have no mutual buyer/customer or supplier relationship, such as a merger between a bank and a leasing company. Example: Prudential's acquisition of Bache 85 Company.
4. Conglomerate mergers take place when the two firms operate in different industries.

2.6.2 Steps in a Merger

According to the Herra (2007), there are three major steps in a merger transaction: planning, resolution, and implementation.

1. Planning, which is the most complex part of the merger process, entails the analysis, the action plan, and the negotiations between the parties involved. The planning stage may last any length of time, but once it is complete, the merger process is well on the way. More in detail, the planning stage also includes:
 - signing of the letter of intent which starts off the negotiations;
 - the appointing of advisors who play the role of consultants, examining the strengths, weaknesses, opportunities, and threats of the merger;

- detailing the timetable (deadline), conditions (share exchange ratio), and type of transaction (merger by integration or through the formation of a new company);
 - Expert report on the consistency of the share exchange ratio, for all of the companies involved.
2. The resolution is simply management's approval first, then by the shareholders involved in the merger plan. The resolution stage also includes:
- the Board of Directors calling an extraordinary shareholders' meeting whose item on the agenda is the merger proposal;
 - the extraordinary shareholders' meeting being called to pass a resolution on the item on the agenda;
 - any opposition to the merger by creditors and bondholders within 60 days of the resolution;
 - green light from the Italian Antitrust Authority, that evaluates the impact of the merger and imposes any obligations as a prerequisite for approving the merger.
3. Implementation is the final stage of the merger process, including enrolment of the merger deed in the Company Register.

CHAPTER 3: RESEARCH METHODOLOGY

3.1 Research Design

This was a case study on GlaxoSmithKline Pic which was chosen for its size and impact and which was thought would provide an in-depth understanding of how mergers of this size would portend. Glaxo Welcome and SmithKline Beecham merged to form GlaxoSmithKline Pic in 2001. This study design was chosen because case studies provide in-depth analysis of the study problem. Mergers are also unique and therefore can only be studied well and comprehensively when they are taken as cases.

3.2 Data Collection

Details of the merger were required from this study. Four senior managers were interviewed. The managers were selected for interview as they played a key role in the merger process and as head of their respective businesses.

Questionnaires were used to obtain primary data. Secondary data was obtained from GSK in-house publications that are developed in the United Kingdom and distributed to every region and periodic newsletters and magazines that are distributed to members of staff worldwide.

The General Manager of the Pharmaceutical division, the General Manager of the Global Manufacturing and Supplies division, the Finance Director of GlaxoSmithKline, who has since retired but was a key player in the merger

process in East Africa and the Human Resource director of the East African Market, responded to the study.

3.3 Data Analysis

Given the qualitative nature of the data obtained, the mode of analysis used was content analysis. It was deemed as a good means of analyzing interactions and its ease of reference and interpretation by the beneficiaries of this study. According to Cooper and Emory (1995), content analysis guards against selective perception of the content, has the provision for the rigorous application of reliability and validity criteria, and is amenable to computerization.

CHAPTER 4: RESEARCH FINDINGS AND DISCUSSIONS

4.1 Company Profile

GlaxoSmithKline was officially formed in December 2000 and the corporate identity unveiled on 8th January 2001. It is a Public Limited Company with the key principle shareholders being large pension funds in the United Kingdom and some fund managers in the United States of America. It is listed in the London and New York Stock Exchanges. It defines its core business as the research and development, manufacturing, marketing and distribution of pharmaceutical and consumer healthcare brands. It is the only pharmaceutical company to tackle the three "priority" diseases identified by the World Health Organization: HIV/AIDS, tuberculosis and malaria.

GlaxoSmithKline employs over 104,000 employees in over 116 countries. This being a UK based company it is run by a board which consists of three executive directors - the Chief Executive Director, the Chief Finance Officer, the Chairman of Research and Development, and nine non-executive directors. The Corporate Executive Team is responsible for the strategic management of the company. The team's responsibility is to lead the company to become a world leader in the pharmaceutical industry.

GlaxoSmithKline's mission explains why GlaxoSmithKline is in business and reads: 'Our quest is to improve the quality of human life by enabling

people do more, feel better and live longer'. The strategic intent is to become the indisputable leader in the pharmaceutical industry.

4.2 The Merger Objectives and Process

4.2.1 The Objectives of the merger

Rapidly evolving technologies and advances in the understanding of the underlying causes of disease are leading to fundamental changes in the pharmaceutical industry, and in turn presenting new challenges and opportunities for pharmaceutical companies. Glaxo Wellcome and SmithKline Beecham believed that significant scale and resources would be required in order to sustain investment in the skills, technology and expertise necessary to discover, develop and deliver new and better medicines to patients in a faster and more efficient way.

Change in the pharmaceutical industry is being driven primarily by rapid advances in science and technology, growing importance of marketing power, and emergence of patients as more knowledgeable consumers. Glaxo Wellcome and SmithKline Beecham believed that the combination of the skills and resources of the two groups would create the leading research-based pharmaceuticals company in the world. The proposed merger would improve the two groups' ability to generate sustainable long-term growth and enhance shareholder value in an increasingly competitive environment.

The above would be derived from Global leadership and scale in the pharmaceutical industry. Based on September 1999 moving annual total (MAT) market estimates of pharmaceutical industry sales, Glaxo SmithKline would have been ranked the largest pharmaceutical company in the world, the United States and in Europe.

The merged company would have a powerful R&D capability combining both companies' expertise and technology with a current annual R&D budget of approximately £2.4 billion (\$4.0 billion) to deliver long-term growth. This would create an enhanced platform to discover and develop new medicines more effectively and efficiently.

With one of the largest sales forces and marketing resources in the global pharmaceutical industry, Glaxo SmithKline would have increased share of voice with physicians and opinion leaders in the healthcare industry, which would allow the company to maximize the potential of its existing products and future pipeline.

Glaxo SmithKline's combined product portfolio would comprise a number of successful and fast growing products alongside established franchises in its key therapeutic areas. Pharmaceutical products with sales greater than £250 million (\$415 million) would represent approximately two thirds of total pharmaceutical sales.

The merger was expected to generate substantial operational synergies. Management of the two companies estimated that annual pre-tax cost savings of £1.0 billion (\$1.7 billion) were achievable from the third anniversary of completion of the merger. It was expected that £250 million (\$415 million) of these savings would be derived from combining the two research and development (R&D) organisations and would be reinvested in R&D. The other cost savings of £750 million (\$1.2 billion) were expected to come from reducing the overlap in administration, selling and marketing and manufacturing facilities.

The commercial rationale for the merger held firm throughout that time was to create:

- i) A group with combined sales from continuing businesses of approximately £15.0 billion (\$24.9 billion), and an estimated 7.3 per cent share of the global pharmaceutical market
- ii) A powerful R&D capability combining both companies' expertise and technology with an annual R&D budget of approximately £2.4 billion (\$4.0 billion)
- iii) An enhanced platform to discover and develop new medicines more effectively and efficiently
- iv) One of the most extensive development pipelines in the pharmaceutical industry, with a total of 30 new chemical entities (NCEs) and 19 vaccines in clinical development (phase II / III), of

which 13 NCEs and 10 vaccines were in late-stage development (phase III)

- v) A market leader in four of the five largest therapeutic categories in the pharmaceutical industry: anti-infectives, Central Nervous System, respiratory and alimentary and metabolic; a leading position in the vaccines market and a strong position in consumer healthcare and over-the-counter medicines
- vi) An industry-leading sales and marketing force of approximately 40,000 employees globally, including over 7,200 sales representatives in the US, providing Glaxo SmithKline with global marketing strength
- vii) £1.0 billion (\$1.7 billion) in annual pre-tax cost savings from the third anniversary of completion of which £250 million (\$415 million) was expected to be reinvested in R&D
- viii) A truly global organisation with wide geographic spread and strong presence in the important US market

4.2.2 The Merger Process

The transaction was structured as a nil-premium merger (A merger where none of the shareholders receives a premium over the market value of their shares before the transaction is announced) of equals. It was effected by way of a scheme of arrangement in which a new holding company, GlaxoSmithKline, was put in place over the merger parties. On completion, Glaxo Welcome (GW) shareholders held approximately 58.75% of the issued ordinary share capital of Glaxo Welcome (GW) and SmithKline Beecham (SB) shareholders held approximately 41.25%.

The blueprint for the merger structure was chosen in early 1998 when a merger between GW and SB was first proposed. Although the initial attempt at merging did not proceed, the merger structure favoured at that time was chosen as the method by which the two companies would unite two years later when the merger plans were revived.

As both companies are constituted under English law, the two main alternatives considered were a recommended takeover or a merger by scheme of arrangement under section 425 of the Companies Act 1985 (1985 Act). The parties chose a scheme of arrangement, involving reductions of share capital of both GW and SB, in which the two companies merged under a new holding company. This particular arrangement had three main advantages over a takeover: A substantial stamp duty saving. Stamp duty is payable by the purchaser on the transfer of shares at a rate of 0.5% of the consideration. The scheme did not involve the transfer of shares and there was therefore no stamp duty. Assuming that SB would have been the target company, stamp duty (calculated on the basis of its market capitalisation at the time of the announcement) would have amounted to over £200 million. If GW had been the target company the stamp duty cost would have been even greater. It supported the concept of a merger of equals, which would not have been the case if one company had purchased the shares of the other. Also, a nil-premium merger is more commonly effected by a scheme of arrangement than by a takeover. GW and SB were acquired by a newly

formed English holding company, GlaxoSmithKline, by means of a scheme of arrangement of each of GW and SB. Under the scheme GW and SB shares were cancelled in return for the issue of GlaxoSmithKline shares to the former public shareholders in those two companies. GW and SB became wholly owned subsidiaries of GlaxoSmithKline when the scheme became effective.

It benefited from the exemption from the registration requirements provided by section 3(a)(10) of the US Securities Act of 1933. As a result, it was not necessary to file a registration statement with the US Securities and Exchange Commission to effect the merger.

The merger also involved several steps. The begin with the merger required the approval of shareholders of both GW and SB, first at court convened meetings to approve the scheme and secondly at extraordinary general meetings (EGMs) to approve the reductions of capital. Following this, a scheme must be approved by a majority in number representing three-fourths in value of the shareholders or class of shareholders voting, whether in person or by proxy (section 425(2), 1985 Act). A meeting to seek this approval is convened at the direction of the court. Once the scheme has been sanctioned by the court, all shareholders (or class of shareholders), and not just those who voted in favour, are bound by the terms of the scheme. The scheme of arrangement was made between GW and its shareholders and SB and its shareholders where the existing shares were

cancelled. All the ordinary share capital of GW and SB in issue before the voting record time, and any further shares issued at or after the voting record time and before 6pm on the day before the order date were cancelled.

GW and SB became subsidiaries of GlaxoSmithKline. The share capital of GW and SB were increased to their former amount by the creation of new GW and SB shares equal to the number of shares cancelled. GW and SB applied the reserve arising as a result of the reduction of capital in paying up in full at par the new GW and SB shares, which were allotted and issued credited as fully paid to GlaxoSmithKline. GW and SB therefore became wholly owned subsidiaries of GlaxoSmithKline.

In consideration for the cancellation of the shares and the issue of new GW and SB shares to GlaxoSmithKline, GW shareholders and SB shareholders who were on the companies' respective share registers at the scheme record time, received fully paid GlaxoSmithKline shares on the basis of one GlaxoSmithKline share for each GW share and 0.4552 GlaxoSmithKline shares for each SB share.

The scheme became effective when the court orders sanctioning the scheme (section 425, Companies Act 1985) (1985 Act) and confirming the reductions of capital (section 137, 1985 Act) were delivered to the Registrar of Companies for registration and, in the case of the reductions of capital, registered by him. The effective date was 27th December, 2000.

GW and SB shares issued to any person except GW or SB on or after the effective date were automatically exchanged under the articles of association (as amended) of GW and SB for GlaxoSmithKline shares on the same terms as under the scheme.

As the scheme involved a reduction of capital, it was necessary for both GW and SB to hold an EGM to approve the reduction and the steps required to be taken in connection with it. The special resolutions (requiring a 75% majority of shares voted) put to shareholders were that the share capital of the companies be reduced by cancelling and extinguishing all the shares then in issue, that on the reduction taking effect, the share capitals of the two companies be increased to their former amount by the creation of new ordinary shares equal to the number of scheme shares cancelled and that the reserve arising as a result of the cancellation of shares be applied in paying up in full at par the new ordinary shares, that the new shares be allotted and issued credited as fully paid to GlaxoSmithKline, and that the directors of the companies be authorised under section 80 of the 1985 Act to allot the new ordinary shares (*Legal & Commercial Publishing Limited, 2001*)

The four meetings (a court convened meeting and EGM for each of GW and SB) were held on the same day. As is customary, each company held the court convened meeting first and this was followed shortly afterwards by the

EGM. At each of the meetings the resolutions required to implement the merger were passed by substantial majorities.

4.3 Impact of the Merger

One of the objectives of the merger was to combine skills and resources. The £114 billion merger created a giant with an estimated global market share of 7% of the world pharmaceutical market. In achieving this strategic intent, the company has performed well as per expectations. Starting with the stock price, in 2004, the GlaxoSmithKline share price in the London Stock exchange was valued at £10.9 per share. In March 2006, it was up by 45% to a price of £15.8 per share. In the New York stock market, the share was valued at \$39.6 a share and in March 2006, the price was at \$54.4, registering a 37% growth in two years into the merger.

Table 1: Impact of Merger on Share Price

GSK Share Price	USA	UK
Feb-04	\$39.60	£10.90
Mar-06	\$54.40	£15.80
% Change	37%	45%

Source: S&P Research (2005)

GlaxoSmithKline PLC registered the second highest sales turn over in the pharmaceutical industry in the world. More importantly, the return on assets, GSK became number 2. Also as shown in table 2, it became the 18th largest company in the world in Market Capitalization.

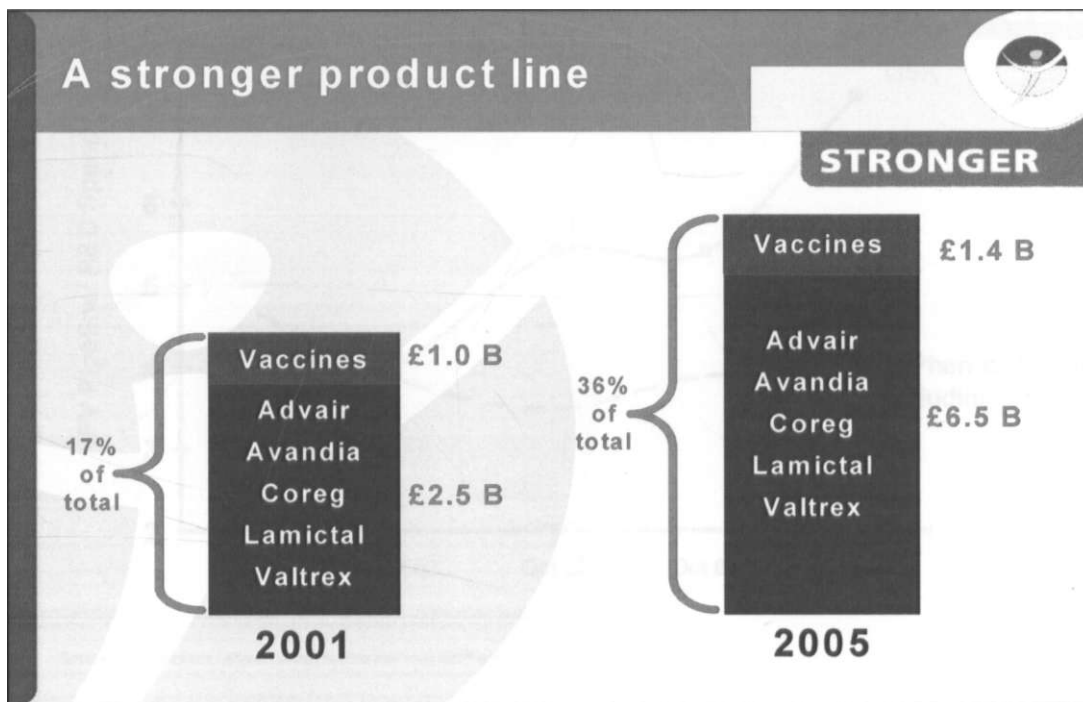
Table 2: GSK Position after Merger

Market Capitalisation		
Position	Company	US\$ (billions)
1	General Electric	370
2	Exxon	350
18	GSK	147
Return on Assets		
1	Mittal Steel	26.5%
2	GSK	15.4%

Source: S&P Research (2005)

A strong product line saw GlaxoSmithKline more than double their sales of some key focus brands as shown in Figure 3.

Figure 3: Stronger Product Line

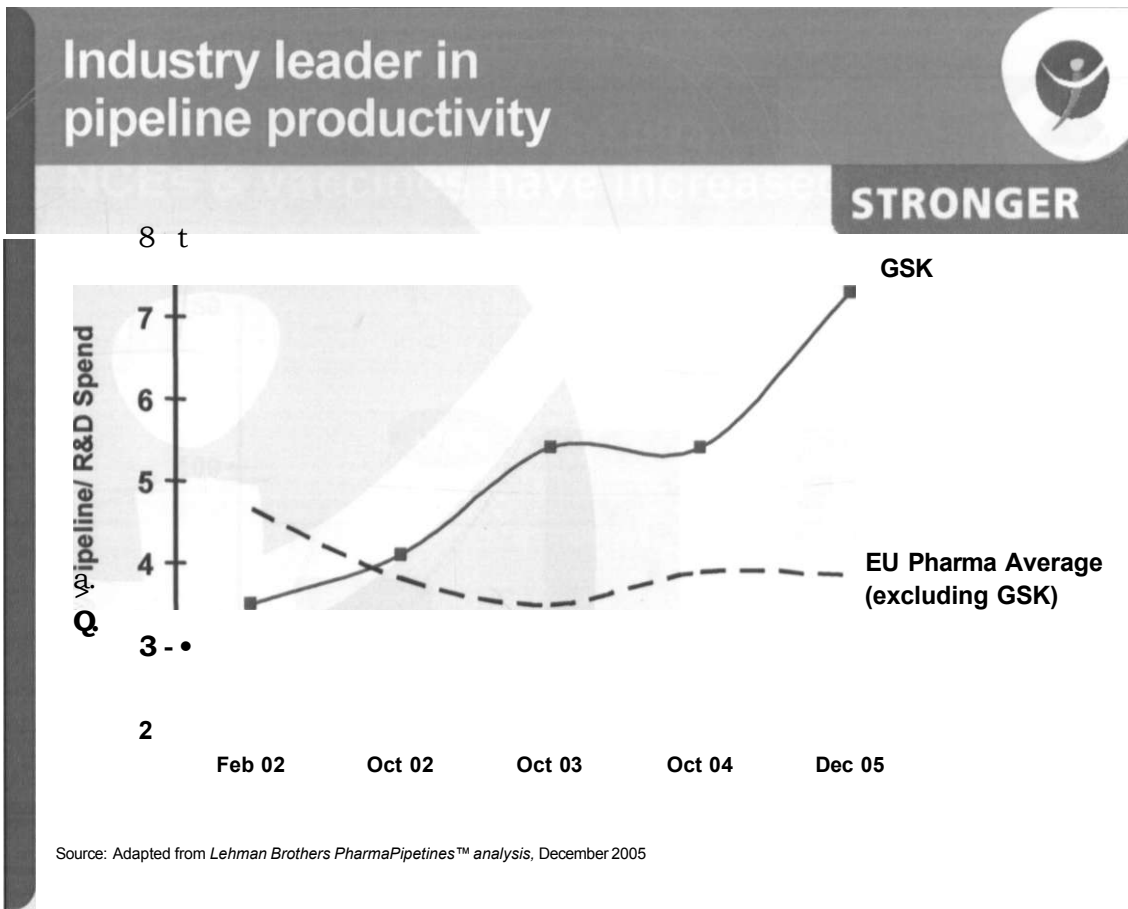


Source: S&P Research (2005)

This group of products contributes 36% of the company's sales, which moved to £8 billion in only a few years after the merger.

The capability of a pharmaceutical firm to introduce new products to the market, quickly, depends on the investment towards research and development activities. Research & Development productivity went to an all-time high for GSK, performing well above the industry average as shown below in Figure 4. GlaxoSmithKline came from behind to become an industry leader in only a few years.

Figure 4: Research & Development Productivity



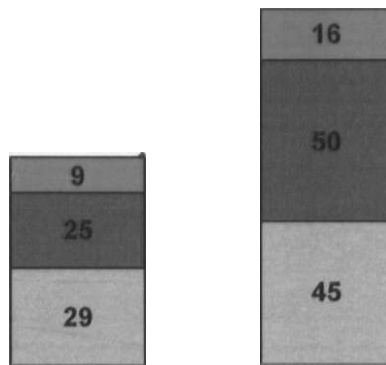
Source: S&P Research (2005)

Product or new chemical entities pipeline are those products that have been discovered to have commercial viability as well as make a contribution to human health. With a strong research and development facility, new molecules are being discovered, and the company's pipeline of products is getting bigger, than it was before the merger - in terms of new chemical entities (NCEs) and vaccines. Figure 5 shows the position in terms of the number of products in the pipeline in 2001 compared to the number of products in the pipeline in 2005. This translated to 76% growth in 4 years.

Figure 5: Products in R&D Pipeline

**GSK's pipeline - 2001-2005
NCEs & vaccines have increased 76%**

STRONGER

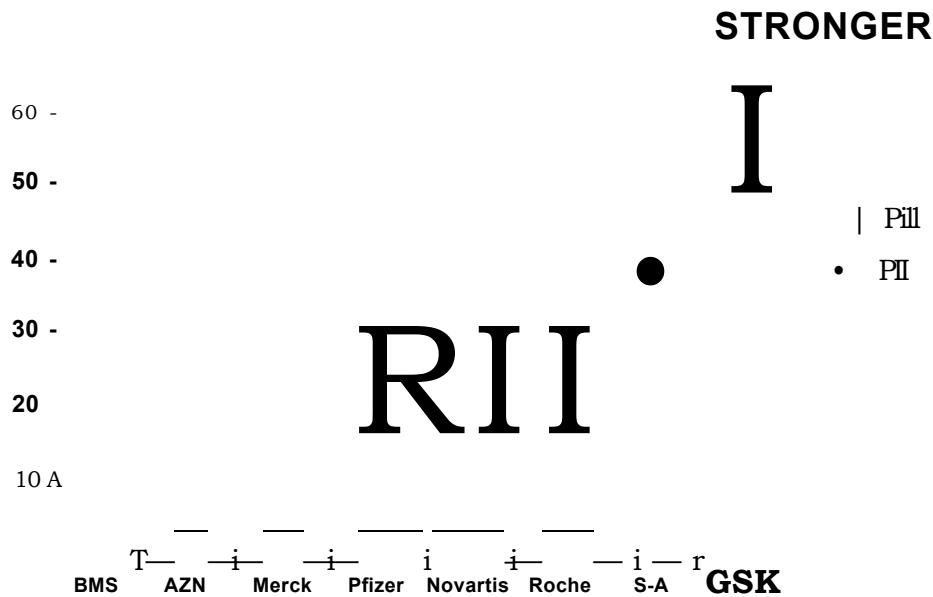
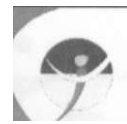


Source: S&P Research (2005)

GlaxoSmithKline Pic has a leading late stage pipeline in the industry as shown by the graph in figure 6 below. GlaxoSmithKline leads in the number of products in the late stage pipeline compared to its competitors. The late stage pipeline products are those that have the greatest market opportunity and show the most positive results in clinical trials. Hence these products are likely to be launched in at most 3 to 5 years.

Figure 6: Position in Late Stage Product Pipeline

GSK has a leading late-stage pipeline



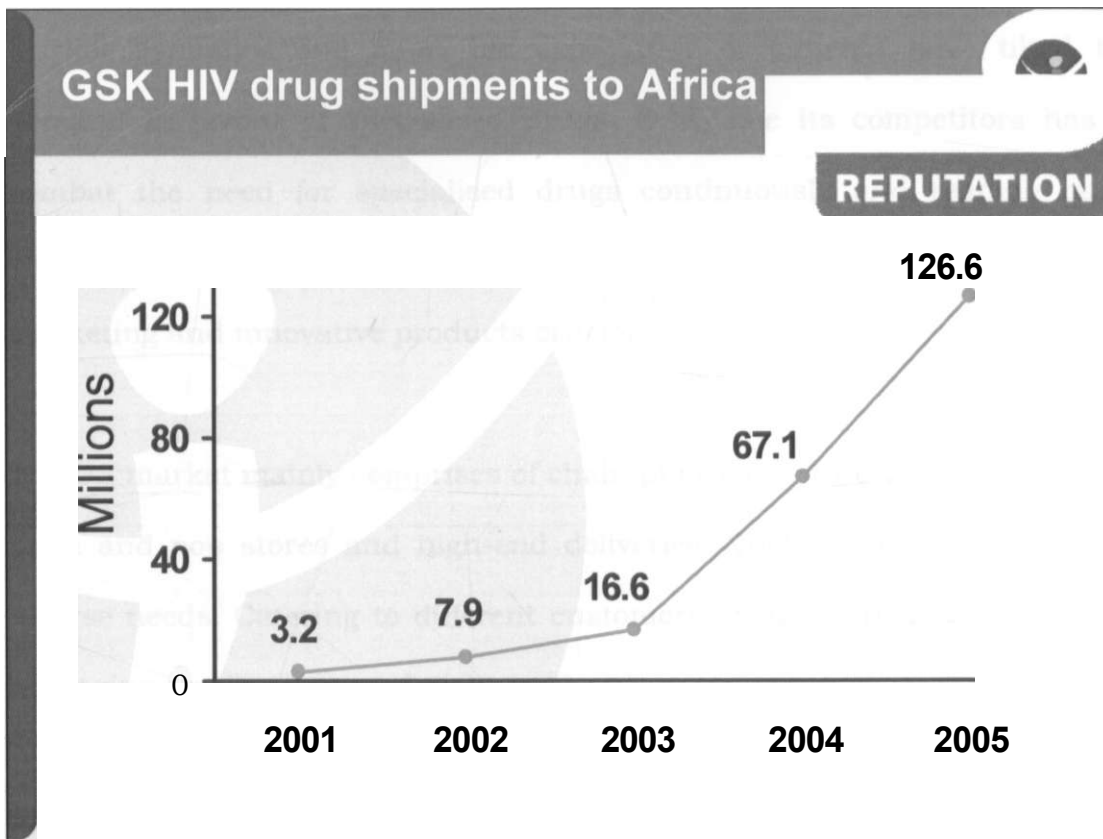
Source: Lehman Brothers Pharma Pipelines 2005

Source: S&P Research (2005)

In terms of keeping the work force motivated, as evidenced by an internal survey carried out in 2005, 83% of the workforce indicated that they are proud of working for GlaxoSmithKline Pic (GSK, 2001).

In terms of reputation, GlaxoSmithKline took the high ground with the HIV drug distribution program in Africa. It increased the HIV drug shipments to Africa. One hundred and twenty-six million tablets were shipped to Africa in 2005 and GlaxoSmithKline Pic is the number one supplier of at-cost HIV drugs in Africa, more than all the generic companies put together (GSK, 2001).

Figure 7: Growth in Reputation in Supply of HIV drugs to Africa



Source: S&P Research (2005)

4.4 Challenges of the GSK Merger

With the spate of mergers and acquisitions, GSK faced three major integration challenges. Integrating the separate identities, integrating different strategies and integrating the packaging and manufacturing operations of Glaxo, Burroughs Wellcome, Beecham, SmithKline Beckman and Block Drug Company. The challenges were manifested in the various ways.

Market dynamics and short life expectancy of patients have tilted the demand in favour of specialised drugs. GSK, like its competitors has to combat the need for specialised drugs continuously and reaping quick rewards. Such market forces alongside a changing industry make creative marketing and innovative products crucial.

The US market mainly comprises of chain pharmacy stores, more traditional mom and pop stores and high-end deliveries. Such diverse markets have diverse needs. Catering to different customers brings forth the challenge of managing small volumes of niche packages.

Frequent merger and acquisition activity implies complicated paper work (re-registration and labelling) compliance with regulatory frameworks of different countries. With over 250 legal entities across the world, printing and other associated challenges emerge with different names that have to appear on different products distributed in different countries. The

complexity increased manifold with the mergers owing to labelling changes. Moreover, different markets have different schedules on when GSK must incorporate the labelling changes.

Different departments could always make different packaging design changes. Communicating packaging specifications, graphics and artwork changes across the entire pharmaceutical organization was challenging if not an insurmountable task.

One of GSK's products, Aquafresh Floss'N'Cap (AFNC) is symbolic of the typical outsourcing challenges. AFNC has a flip top containing dental floss and toothpaste in the tube. AFNC had three custom designed sub assemblies outsourced to three different suppliers. The suppliers worked in sequence on the custom designed cap. Once the package reaches GSK, only filling of the tube with toothpaste remained. Coordinating with these three cross Atlantic suppliers, especially outside GSK's manufacturing facilities was a challenging task.

GSK had a bad experience early on with supply disruptions from a single-source supplier. Almost a decade ago, one of its sole resin supplier's plants exploded. It had no alternate suppliers and consequently had to lose market share not to mention customer goodwill, as customers have to do without critical drugs or life saving devices. GSK wanted to eliminate such situations. The challenge was not only to find alternate suppliers but ones

who complied with the FDA regulations and supplied in time.

On the major machinery and equipment side, GSK's goals were different though. It wanted to limit the number of machinery suppliers to better familiarise with the manufacturer's equipment and establish partnerships with machine suppliers who offered total packages when compared to independent system integrators.

The foremost challenge in production operations was synchronising with different manufacturing locations and multiple suppliers. With different packaging and assembly lines, implementing automation and advanced technology or process improvement programmes was a huge challenge. Other considerations were quick machine setup, minimum production stoppages, better equipment availability and flexibility besides handling innumerable design changes.

Technologies, for example RFID in anti-counterfeiting are largely untested or simply not the best. GSK has RFID supply chain projects planned but faces a tough test with respect to being the first mover in investing huge sums into the technology or adopt a wait and watch policy. GSK may lose out in both cases owing to failure of the relatively new technology or lose out to competitors who can gain significantly by adopting the technology faster.

The most fundamental challenge of any alliance or merger is cultural. Mergers, acquisitions, and alliances involve blending people of different corporate cultures and even various national cultures into one company, which tends to complicate matters further. Instead of melting everyone together, a leader must capitalize on the cultural differences between employees and try to diminish the psychological distances between them.

The 2000 merger of SmithKline Beecham and Glaxo Wellcome into GlaxoSmithKline was to have employees thinking and behaving as GSK people and not Glaxo people or SmithKline people. They had to decide and collectively answer some very fundamental questions from the start.

4.4 Overcoming the Challenges faced

To counter the challenge of supplying to a multifaceted US market and low volume niche markets, GSK implemented the late pack customisation programme. While typical production runs were up to 30,000 numbers for cost effectiveness, GSK could effectively produce as low as 100 or 500 packs at a time with this programme. For instance, basic boxes were volume filled with blisters at the pack site and shifted to the two distribution centres in Europe. At these centres, clear labels were printed online with country related information and applied automatically. Even country specific folded leaflets were attached automatically. Quality was ensured with three two-dimensional bar codes, one pre-printed on the box, the other pre-printed on the leaflet and another printed online on the label. Online inspection on the

codes could be performed at one go owing to their inline position.

With more than 36,000 SKU's and a six-month life cycle of its products, handling packaging specifications, associated graphics and artwork changes was an enormous task. Standardizing the packaging changes was another major obstacle. GSK developed the Global Pack Management (GPM) to handle this complexity (currently in use for its prescription products). The GPM programme focussed on four major issues. Packaging changes were standardized using global training and implementation programmes. A pack catalogue was developed and all employees were given access to a central and current set of all GSK's packaging information. This would help foster idea sharing while achieving packaging optimisation simultaneously. Central artwork development was created. Accordingly, only four centres (strategically chosen at US, UK, Italy and India) were to service the packaging graphic needs of all products. Earlier, 250 centres performed the same activity. A uniform and centralized information technology system was developed to help streamline workflow. Since all the employees use the same central applications (For example, GSK adopts the graphics industry standard Apple Macintosh computers and software) it ensures uniformity. There are no serious encryption issues, if packaging artwork is transferred between similar standard systems.

According to FDA regulations, all drug companies in the US must print and attach labels to every product going into the market. So, any label or leaflet

change can take up to a year to reflect with pharmacy stores first emptying existing inventory. Working along with the Pharmaceutical Research and Manufacturers of America (PhRMA), GSK has been striving hard to push forward its paperless labelling initiative. The aim of paperless labels and electronic leaflets was to prescribe information to healthcare professionals electronically. This helps instant update as any change in the leaflet/label is reflected automatically. Patient safety is the ultimate goal of GSK.

GSK has been working on developing online printing that matches the speed of the packaging line and prints at the desired quality level. Efforts have been on to keep costs of online printing down.

GSK realized the importance of finding and qualifying multiple suppliers to avoid any supply disruptions. For instance, for its popular Advair Diskus device, GSK has three suppliers, two in Europe and one in the US. The goal was to have enough capacity globally with all suppliers producing identical components with identical tooling on identical machines. Meeting strict regulations is of prime importance. Communication can play a vital role in establishing coordination among multiple suppliers. GSK uses an electronic CAD package. The CAD package has drawings indicating minor details and any subsequent or ongoing review to every component to overcome communication gaps if any.

GSK limits the number of equipment suppliers to minimise downtime. For instance, on one packaging line it has one supplier Schubert's four robotic systems. The robots do the cartooning and case packing as well. In response, Schubert offers GSK the benefit of assigning a dedicated team that works for GSK alone. The team also has an office in GSK's plant itself. Healthy supplier relationships have helped GSK minimise downtime. Moreover, all equipment from a single supplier facilitates a better understanding of the equipment functioning, than having disparate machines for same tasks. Thus training costs are also less.

Furthermore, GSK uses a central TIPS production management system that minimises downtime. The system tracks downtime data allowing for ongoing production improvements. GSK is able to maintain product quality with vision cameras and online inspection using bar code scanners. GSK prefers to be the rapid follower instead of being bleeding edge with respect to technology adoption. Instead of using 'packaging only' lines, GSK uses lines, which are integrated to do final assembly and packaging also.

GSK's efforts as illustrated above have been successful. Organisations can follow its Supply Chain Management strategies as they truly extend the value of product, packages, plants and people.

CHAPTER 5: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

The study managed to document the process of the merger and also established that the merger was a success and the objectives of the merger were met as follows:-

5.1.1 Documenting Glaxo Wellcome and SmithKline Beecham merger process.

The first objective was to document the process of the Glaxo Wellcome and SmithKline Beecham merger. The study found that this was a merger where neither set of shareholders receives a premium over the market value of their shares before the transaction is announced and was termed as transaction of equals. On completion, GW shareholders held approximately 58.75% of the issued ordinary share capital of GlaxoSmithKline and SB shareholders held approximately 41.25%.

The two companies merged under a new holding company which enabled them to have a substantial stamp duty saving, supported the concept of a merger of equals which would not have been the case if one company had purchased the shares of the other. GW and SB became wholly owned subsidiaries of GlaxoSmithKline when the scheme became effective and it was not necessary to file a registration statement with the US Securities and Exchange Commission to effect the merger.

The merger also involved Shareholder approvals. Scheme approved by a majority in number in value of the shareholders or class of shareholders voting where existing shares were cancelled, GW and SB became subsidiaries of GlaxoSmithKline, shares were issued, scheme became effective, shares issued after the effective date automatically exchanged under the articles of association for GlaxoSmithKline.

There was reduction of capital where the share capital of the companies was reduced by cancelling and extinguishing all the shares then in issue. On the reduction taking effect, creation of new ordinary shares equal to the number of scheme shares cancelled. The new shares were allotted and issued credited as fully paid to GlaxoSmithKline. The directors of the companies were authorised under section 80 of the 1985 Act to allot the new ordinary shares.

5.1.2: Establishing whether the merger objectives were met.

The second objective of the study was to establish whether the merger objectives were met. The study found that the merger was a success and the merger objectives were met. One of the objectives of the merger was to combine skills and resources and the study found that the £114 billion merger created a giant with an estimated global market share of 7% of the world pharmaceutical market. In achieving this strategic intent, the

company has performed well as per expectations. The results of the merger were noted as follows:

In 2004, the GlaxoSmithKline share price in the London Stock exchange was valued at £10.9 per share. In March 2006, it was up by 45% to a price of £15.8 per share. In the New York stock market, the share was valued at \$39.6 a share and in March 2006, the price was at \$54.4, registering a 37% growth in two years into the merger.

GlaxoSmithKline PLC registered the second highest sales turnover and on the return on assets in the pharmaceutical industry in the world as well as becoming the 18th largest company in the world in market capitalization.

A strong product line saw GlaxoSmithKline more than double their sales of some key focus brands. This group of products contributes 36% of the company's sales, which moved to £8 billion in only a few years after the merger.

Research & Development productivity went to an all-time high for GSK, performing well above the industry average. GlaxoSmithKline came from behind to become an industry leader in only a few years. With a strong research and development facility, new molecules are being discovered, and the company's pipeline of products got bigger, than it was before the merger. Product or new chemical entities pipeline grew by 76% in 4 years.

GlaxoSmithKline Pic has a leading late stage pipeline in the industry compared to its competitors.

In terms of keeping the work force motivated, as evidenced by an internal survey carried out in 2005, 83% of the workforce indicated that they are proud of working for GlaxoSmithKline Pic.

In terms of reputation, GlaxoSmithKline took the high ground with the HIV drug distribution program by increasing the HIV drug shipments to Africa more than all the generic companies put together.

Though there were challenges experienced GSK overcame the challenges of the merger by Countering Market Dynamics, Countering Packaging Complexities through Global Pack Management, Paperless labelling/electronic leaflets, and Online Printing.

GSK realized the importance of finding and qualifying multiple suppliers to avoid any supply disruptions. For instance, for its popular Advair Diskus device, GSK has three suppliers, two in Europe and one in the US. The goal is to have enough capacity globally with all suppliers producing identical components with identical tooling on identical machines. GSK limited the number of equipment suppliers to minimise downtime.

5.2 Conclusions

Despite the fact that mergers have their own pitfalls, certainly some mergers are a perfect fit of two companies which complement each other's strengths, have obvious benefits and enable the companies to make massive economies of scale. They have all outgrown their home market and feel the need to expand by mergers and acquisitions so that they can compete and even triumph on the world stage. This enables them to win customers and new business while keeping costs down and still fund the billions necessary for research and development. In the case of the GSK merger, all the above benefits accrued.

The objective of this study was to document the process and establish whether the objectives of the merger were met. It is evident from the findings that the process was elaborate and much organised. It has also been established that the objectives of the merger were achieved and the merger was very successful.

The GSK merger may therefore serve as a case to be used by other companies aspiring to adopt the merger strategy.

5.3 Recommendations for Further Study

This study recommends that further research be undertaken to determine the survival of mega mergers and establish the reasons for their post merger survival or death. Since the GlaxoSmithKline merger, other mergers have since taken place in the pharmaceutical industry. It would be interesting to

establish how such new mergers may have affected this merger and others within the industry.

5.4 Limitations of the study

Several limitations were encountered during this study. The merger process was controlled from the United Kingdom and the people directly involved in the merger are located there. However, it would have been very costly to travel to the United Kingdom to obtain my interviews, not to mention that getting appointments for interviews would have been very challenging.

Many people who were with the company then have since left to pursue other interests elsewhere. I therefore had to contend with interviewing local current management who helped piece together relevant merger information verbally and from data published in the internal employee magazines.

REFERENCES

- Andrews, K. R. (1971), **The Concept of Corporate Strategy**, Dow Jones-Irwin Inc., Illinois.
- Ansoff, H. I. (1965), **Corporate Strategy: An Analytical Approach to Business Policy for Growth and Expansion**. McGraw-Hill Inc., New York.
- Ansoff, H.I. & McDonnell, E.J. (1990), **Implanting Strategic Management**, Second Edition, Prentice Hall, Cambridge.UK
- Banerjee B. P. (1999), **Corporate Strategies: A Comprehensive handbook Based on the Indian Experience**, Oxford University Press.
- Barnett H. J. and Wilsted D.W. (1989), **Strategic management: Text and Concepts**, PWS-KENT Publishing Company, Boston.
- Birkett, Kirsten (2001), **Inside The Glaxo Wellcome And Smithkline Merger**, Legal & Commercial Publishing Limited, London
- Capon N., Farley U. J. and Hulbert M. J. (1987), **Corporate Strategic Planning**, Columbia University Press, Columbia
- Cooper D.R. and Emory C. W., (1995), **Business Research Methods, Fifth Edition**, The McGraw-Hill Companies, Inc.
- Edward B. Roberts, (1980), *New Ventures for Corporate Growth*, **Harvard Business Review**, July- August, Volume 58, Number 4.
- Ellis J. and Williams D. (1983), **Corporate Strategy and Financial Analysis: Managerial, Accounting and Stock Market Perspectives**. Financial Times Pitman Publishing, Great Britain
- Grant, R. M. (1998), **Contemporary Strategic Analysis: Concepts, Techniques, and Applications**. Blackwell Publisher, Massachusetts, 3rd Edition.
- GSK Corporate Communications (2001), **Emerge Magazine**[^] Issue 10, March
- GSK Corporate Communications (2000), **Emerge Magazine**, Issue 10, May
- GSK Corporate Communications (2000), **Emerge Magazine**, Issue No. 2, April

- GSK Corporate Communications (2000), **Emerge Magazine**, Issue, July
- GSK Corporate Communications (2000), **Emerge Magazine**, Issue, November
- GSK (2001), **Creating The Global Leader In Pharmaceuticals** (GSK, 2001)
- Hera, Gruppo (2007), **Steps in a Merger**, www.gruppohea.it/gruppo
- Hofer C. W. and Schendel D.(1978), **Strategy Formulation: Analytical Concepts**, West Publishing Company.
- Johnson G. and Scholes K. (1999),**Exploring Corporate Strategy, Fifth Edition**, Prentice Hall Europe, 1999.
- Kay, J. (1993), **Foundations of Corporate Success: How Business Strategies Add Value**, Oxford University Press.
- Koigi, A. N. (2002), *Implementation of a Strategic Alliance: Experience of Kenya Post Office Savings Bank and Citibank. MBA Research Project (Unpublished)*, School of Business, University of Nairobi.
- Lee T.H., Fisher J. C. and Yau, T.S.(1986), Getting things done: Is your R 86 D on track?, **Harvard Business Review**, January- February, Volume 64, Number 1.
- Lynch R. (2000), **Corporate Strategy, Second Edition**, Aldersgate Consultancy Limited.
- Owuor, T. O. (2004), *Strategic Alliances and Competitive Advantage: A case of major oil companies in Kenya. MBA Research Project (Unpublished)*, School of Business, University of Nairobi
- Pearce, J. A. & Robinson, R.B. (1991), **Strategic Management: Formulation Implementation and Control**, Fourth Edition, Richard D. Irwin Inc.
- Pearce, J. A. & Robinson, R.B. (1997), **Strategic Management: Formulation Implementation and Control**, Sixth Edition, Irwin McGraw Hill.
- Pfeffer, J. (1972), *Merger as a response to Organizational Interdependence*, **Administrative Science Quarterly**: 382-394.
- Porter, M. E. (1998), **Competitive Advantage: Creating and Sustaining Superior Performance**, The Free Press.

- Quin J. B., Mintzberg H, and James R.M. (1988), **The Strategy Process: Concepts, Context and Cases**, Prentice-Hall International, Inc.
- Rappaport A. and Sirower M. L., (1999), *Stock or Cash? The trade offs for buyers and sellers in mergers and acquisitions*, **Harvard Business Review**, November- December, Volume 77, Number 6.
- Roberts E.B. (1980), *New Ventures for Corporate Growth*, **Harvard Business Review**, July- August, Volume 58, number 4.
- Rowe A. J., Mason R.O., Dickel K. E., Mann R. B. and Mockler R.J. (1994), **Strategic Management: A Methodological Approach, Fourth Edition**, Addison-Wesley Publishing Company, 1994.
- Straub, Thomas (2007), **Reasons for frequent failure in Mergers and Acquisitions: A comprehensive analysis**. Wiesbaden: Deutscher Universitätsverlag.
- Thompson A.A. Jr and Strickland A. J. (2003), **Strategic Management: Concepts and Cases**, Thirteenth Edition, Tata Mc Graw-Hill Publishing Company Limited, 2003.
- Wachira, C.W. (2002), *Strategic Alliances in Pharmaceutical Drug Development: A Case Study of Three Strategic Alliances at Eli Lilly and Company*. **MBA Research Project (Unpublished), School of Business, University of Nairobi**

Appendix 1: LETTER OF INTRODUCTION

June R. Wangari,
P.O Box 78392, 00507,
Nairobi.

GlaxoSmithKline Ltd,
P.O Box 78392,
00507,
Nairobi.

Dear Sir,

RE: INTERVIEW FOR MANAGEMENT RESEARCH PAPER

I am a postgraduate student currently studying for an MBA at the Faculty of Commerce, University of Nairobi. I am currently conducting a management research project in partial fulfilment of the requirements for the Masters in Business Administration degree.

GlaxoSmithKline is the main focus for this study. The choice is based on the perceived success of the merger that took place in 2001. I kindly request your assistance by availing your time for a short interview which will be based on the interview guide herein enclosed.

The information you give me will be treated with utmost confidentiality and will be used solely for this research. A copy of the final report will be made available for the company's resource centre.

Your assistance will be highly appreciated.
Thank you

Yours Sincerely

June R. Wangari

Appendix 2: Interview Guide

TOPIC: Growth Through Mergers: A Case Study Of Glaxosmithkline Pic.

SECTION A: COMPANY PROFILE:

When did Glaxo Welcome and SmithKline Beecham merge?

Who are the principal shareholders?

How do you define your core business?

How many employees are currently in GlaxoSmithKline Pic?

How does the organization structure for GlaxoSmithKline look like?

In how many countries does GlaxoSmithKline operate?

What is the strategic intent or positioning that GlaxoSmithKline intends to achieve?

How has your firm's performance been in achieving this strategic intent or positioning in the market?

SECTION B: MERGER PROCESS

When was the proposed merger first announced?

How long did it take from the first announcement of the merger to the completion of the merger?

What type of merger was it? ____

What factors led Glaxo Wellcome and SmithKline Beecham to merge? _

What benefits did the new organization expect from the merger?

What strengths did each company bring into the merger?

How was the merger implemented in the various operations globally? _

SECTION C; EVALUATION

How has the organization performed against the desired benefits?

What challenges did the merger process face?

How did the two organizations overcome these challenges?

How does the future look like for GlaxoSmithKline?