7 Industries with More M&A Activity on the Horizon

By Lauren Setar

For a select group of industries, changing market conditions have laid the foundation for continued M&A activity over the next five years.

Heightened competition, increased concentration and potential regulatory changes have been the impetus for the outbreak of merger and acquisition (M&A) activity for various industries over the past five years. As these drivers of consolidation continue, and in some cases intensify, these industries are headed for more M&As over the next five years. IBISWorld examined more than 1,000 industries and identified those that are highly concentrated and in which establishments (i.e. locations) are increasing at a faster pace than the number of enterprises (i.e. companies) in operation – all hallmarks of an industry ripe for M&A activity. To this end, the industries in the technology, healthcare, travel and financial sectors have emerged as standout candidates, as they currently make significant efforts to expand their customer reach, compete effectively in a saturated market and remain profitable.

Wireless telecom and satellite providers seek new customers

Acquiring subscribers has been the primary driver behind the substantial M&A activity for the Wireless Telecommunications Carriers (IBISWorld report 51332) and Satellite TV Providers (51711b) industries. A large subscriber base allows these providers to offer cheaper prices and attain higher margins. Because increased market penetration over the past five years has made customer acquisition more expensive, M&A activity is expected to increase in the five years to 2017 as companies seek to build economies of scale.

For companies in the Wireless Telecommunications Carriers industry, merging eliminates redundant costs and thereby improves profitability. For example, in a situation where two companies operate two separate cell towers to provide service to the same area, consolidating operations can eliminate the costs of one of these towers. The most recent of such pursuits was the proposed acquisition of T-Mobile by AT&T, which was subsequently blocked by the Federal Communications Commission (FCC) as an antitrust measure. To gain the FCC’s approval, the merger would likely involve the companies selling significant portions of their business to smaller firms. With major players already having a significant share of the market, merger activity is primarily expected to come from smaller companies over the next five years. With this, firms can combine spectrum licenses, which are radio frequencies companies bid on to
use, and then sell off extra licenses. Over the five years to 2017, IBISWorld forecasts that the number of wireless subscribers will increase at an annualized rate of 4.1%. Greater demand for wireless data services will likely counteract lagging demand for voice-only services, especially as consumers increasingly use internet-enabled mobile devices. Companies will engage in M&As to compete for their share of these new subscribers.

In the Satellite TV Providers industry, M&As enable companies to expand their coverage. Industry giant DirecTV, for example, has a fleet of 12 satellites from which it broadcasts signals to consumers and expects to acquire another satellite by 2013 to increase services and backup capacity. Additionally, in 2011, Dish Network acquired Blockbuster, which allowed the company to expand its product offerings through the internet. According to the most recent Nielsen research, 147.4 million Americans viewed video online at the end of 2011. This will be an attractive way for industry players to retain customers that are drawn to this market. As a result, in the five years to 2017, companies in the industry are likely to acquire others to increase product and service selections.

**Pharmacies anticipate potential cost increases**

One of the top industries in the healthcare sector undergoing M&A activity is the Pharmacies and Drug Stores industry (44611). The industry is mainly characterized by the growing market domination of Walgreens and CVS. As the market becomes increasingly saturated in the five years to 2017, these players will continue to acquire smaller companies to seek entry into new geographic markets, achieving further market penetration. In addition, pharmacies and drugstores continue to face rising competition from supercenters like Costco and Walmart and mail-order pharmacies because they offer lower-priced options; for example, Walmart offers a month’s supply of generic drugs for $4.00. As such, M&As will be an attractive way for industry players to attain the cost benefits of a larger company and remain competitive.

Also driving M&As, proposals surrounding healthcare reform include revisions to cost calculation methods, which may reduce reimbursement rates and the resulting profit margin on some medications. To account for this change, companies are likely to merge or acquire others to cope with the higher associated costs in the next five years. In addition, pharmacy benefit managers (PBMs), third-party administrators of prescription drug programs, will need to consolidate to attain clout with generic-drug makers, especially as the patents for brand-name drugs expire and generic drugs rise in demand. New coverage guidelines will likely require changes in administration that may increase costs, driving pharmacies to merge with these PBMs to retain bargaining power. Already, a number of significant acquisitions have taken place during the five years up to 2012. In 2007, CVS merged with Caremark Rx Inc., a PBM; in 2008, CVS Caremark bought Longs Drug Stores; and in 2010, Walgreens acquired Duane Reade Holdings. These acquisitions only mark the beginning of what the industry should expect over the next five years, as impending healthcare plans and increased market saturation continue to mold industry’s competitive landscape.

**Travel sector to expand market reach**

Over the next five years, major operators in the Travel Agencies industry (56151) are expected to merge with and acquire global, regional and local websites to improve their geographic spread, strengthen their product and service mix...
and achieve greater economies of scale. The expansion of brick-and-mortar agencies into the online market, which offers relatively high-profit and low-cost transactions, will allow companies to improve revenue and capture a larger share of total bookings and reservations. Major player Sabre Holdings Corporation, for example, has experienced growth over the past five years partly due to strategic acquisitions of a number of online travel booking sites.

Smaller companies in the Car Rental industry (53211) are also ripe for acquisition. The largest companies in the industry enjoy national brand recognition, relationships with airlines and hotels, while smaller companies carve out a market or geographic niche those larger companies find attractive. Most recently, in November 2012, Hertz Global Holdings was cleared by US antitrust regulators to purchase Dollar Thrifty Automotive Group, which gives the company larger market share and a diversification of branding ranging from lower-priced leisure brands to premium flagship brands. Although the soon-to-be “big three” car rental agencies, Enterprise Rent-A-Car, Hertz Global Holdings and Avis Budget Group will not likely merge or be acquired, smaller companies will likely become targets for M&As as larger agencies push to make inroads into the leisure and low-cost markets. However, Federal Trade Commission approval will continue to be an ongoing issue for any proposed acquisitions by the “big three”.

On the other hand, car sharing is a potential growth area for the industry, making companies like ZipCar more attractive. Concentration is expected to continue increasing during the next five years, especially as mergers increase among smaller players operating within the same regions. Increased M&A activity at the bottom of the market will allow some of the smaller players to become larger. For example, as part of the Hertz-Dollar Thrifty deal, U-Save will be acquiring Advantage from Hertz.

**Commercial banking recovers from mortgage crisis**

In the wake of the subprime mortgage crisis, four out of the top five banks in the Commercial Banking industry (52211) have either merged or acquired large banks struggling with losses associated with the crisis. Since the fallout and the subsequent restructuring, it has become more important for companies to undergo M&A activity to survive in the changed landscape. Merger activity in the financial services industry produces larger, better-capitalized and more geographically diverse companies capable of offering a wider array of financial products and services at more competitive prices. To cater to a larger market of people in the next five years, banks will continue to expand product offerings through acquisitions in the five years to 2017. Because the industry’s services range from consumer refinancing activities to depository services to agricultural loans, firms can purchase companies specializing in one area to diversify their product offerings.

Significant restructuring following the subprime mortgage crisis allowed some large commercial banks to make acquisitions, increasing the industry’s market share concentration. Wells Fargo, for example, acquired Wachovia in 2008 and, as a result, became the nation’s largest mortgage lender and the second-largest diversified services firm in the United States in term of deposits. The acquisition also included Wachovia’s financial advisory division, allowing Wells Fargo to expand.

Similarly, in the Financial Planning industry (52393), companies earn new
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Building on the foundation
For these industries, the rise in M&A activity will not let up going into the next five years. For some companies, consolidation will be primarily underpinned by a desire for increased market penetration and brand awareness, but for others, it will be the distinction between success and being forced to exit their respective industry. This will be especially true among smaller companies needing to remain competitive in an industry dominated by only a few major players. As these industries approach saturation, mergers and acquisitions will continue to rank as one of the most effective and quickest ways for operators to attain more customers, cut costs, increase bargaining power and, ultimately, become more profitable entities.

Wells Fargo’s 2008 Wachovia acquisition, for example, included the company’s financial advisory division. In 2009, Bank of America purchased Merrill Lynch & Co. in an all-stock deal worth $50.0 billion. The acquisition made Bank of America a major player in the industry after acquiring Merrill Lynch’s 16,700 advisers and more than five million clients. Also, Ameriprise Financial expanded its operations with the purchase of H&R Block’s Financial Planning Business, helping it increase its presence in California, Texas and Florida. M&A activity in the financial sector is anticipated to continue as companies expand service offerings in order to broaden client bases.

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