Apply an innovative approach to deriving the value of the synergistic effect

Kalina Kavaldzhieva
UNWE, Sofia, Bulgaria
kalinakavaldzhieva@gmail.com

***Abstract**: Synergistic value is a special value that also includes additional elements of value created by the amalgamation of two or more assets along the value chain. In addition, the synergistic value indicates the value of the combined interest of its participants and is greater than the total value of the individual assets evaluated. The purpose of this article is to analyze the situation of a number of companies generating this part of the synergistic effect. This innovative approach is based on a revenue approach and incremental cash flows are generated. The way in which the value of the synergistic effect is derived is of particular importance for all stakeholders, with the applicable methods being: Cost method and revenue method.*

***KEYWORDS**: ASSET VALUATION, SYNERGISTIC VALUE, MARITAL VALUE, MANAGEMENT, NET PRESENT VALUE.*

1. Nature and development of the problem. .

In optimizing the performance of the enterprise and maximizing the value of the capital, managers strive to present in their financial statements, all assets and liabilities of the company at fair values. through adequate financial and management decisions. However, they do not use value inference through the Synergistic Effect. In this case, different approaches are used in the world practice to determine the "fair value" of an entity (enterprise, firm, unit, etc.). In the case of regulated output through synergies - the importance of the problem is dictated by the principle of fair and fair presentation of assets / performance and balance sheet balance, on the one hand, and the reflection of the added value of synergy in management reports.

The synergistic effect (by Synergos Greek - we act together.) Is an increase in efficiency as a result of integration, mergers of individual parts into a single system as a result of the appearance of a systemic effect). The synergistic effect is formed by the effects of different components whereby the effect exceeds the algebraic sum of the effects of each component taken separately. Synergy can be both positive and negative. The positive effect can be achieved either by increasing revenues or by reducing costs as a result of the integration of the effects of the various components in the economic system. As a result, competitiveness is increased, the efficiency of the resources used is increased, the ability to generate and use new innovative methods and conquer existing markets, as well as the development of new ones, is increased.

The limited conditions under which synergy has the potential to create a competitive advantage are;

1. Synergies should demonstrate a reduction or optimization of costs and an increase in revenue above the cost of acquisition. This is the effect of implementing the strategy. The effect will be reflected on the stability of the company.

2. Synergies must be valuable, unique, scarce, with no substitutes. It is not imitated when competitors who do not own it face additional costs and time to secure it[1]

The quantitative estimates of the synergistic effect are diverse. In the world practice different approaches and methods are used in determining the "value" of an object (enterprise, firm, separate part and others) in the case of equity. Equity represents the size of the owner's share of the property after deducting all liabilities.

According to Weston and Weaver, synergy (efficiency) is due to the wide range of sources presented in adapted Table № 1

The associated costs, including those of the integration process, should also be taken into account in the calculated value of the synergy[2]

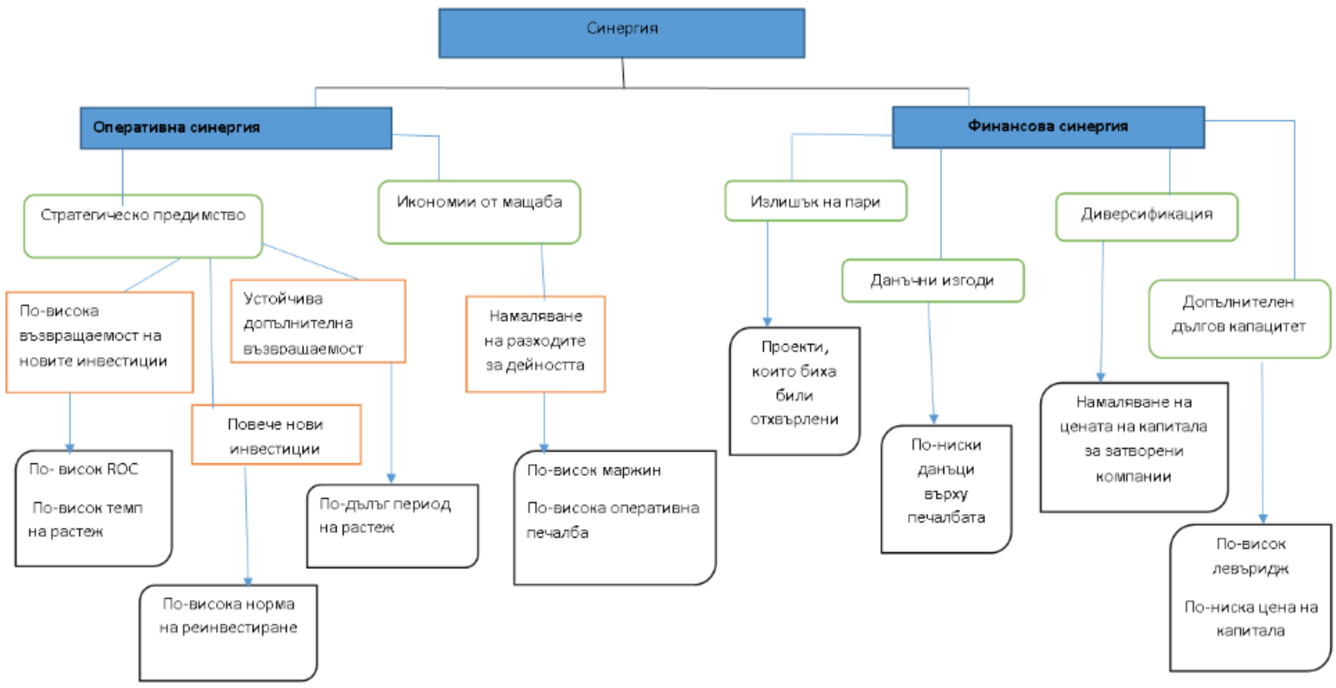
A major problem in accounting for the costs incurred to generate synergy is how to keep these costs in line with the concept of 'value for money".

The success of realizing the synergistic effect depends on the correct moment of the transaction - sometimes it is necessary to rush and work with shorter deadlines, and at other times it may be necessary to wait or to work with longer deadlines. . Therefore, identifying the necessary time for synergy to manifest and the likelihood of this occurring are the key points in determining its true value.

***Table № 1** Sources of Synergy in M&A Transactions*

Definicion	***Source Manifestation***
Strategy	Development of a new strategic vision; Acquisition of skills in a new industry; Rapidly entering new markets with new products; Application of a wide range of abilities and management skills in new fields
Economies of scale	Reduction of production and administrative costs due to volume; Combining research and development; Strengthening the distribution system
Reach savings	Expansion of product lines; Providing complementary products
Advantages of scale	Access to high-tech equipment; Significant discounts
Good practices	Operational efficiency; Rapid tactical application; Resource optimization
Market expansion	Market share growth; Access to new markets
New abilities / Skills	Acquisition of capabilities in new industries; Security of rapid development personnel
Competition	Business acquisition before competition; Competition based on EBIT growth
Customers	Developing new relationships with key clients; Satisfaction of needs for a wide range of services
Technology	Entry into technologically dynamic industries; Acquisition of new R&D capabilities, patents
Change in the industry	Deregulation, relief of state barriers to the geographical and product development
Enlargement of Industries	Combining Multiple Small Businesses into One Large (roll up) and take advantage of experienced management
Globalization	International competition; Opportunities for growth outside the local market; Diversification; Access to cheap resources

[1] Grant, R., contemporary strategy analysis: Consepts, techniques, applications, Malden, MA:Blackwell Publishers, 2005
[2] Brealey, R., Myers, S., Allen, S., Corporate Finance, New York, McGraw-Hill, 2005



It is a difficult task to identify revenue synergies that are more difficult to measure than cost synergies (given its intangible nature). For this reason, in practice, revenue synergy is often referred to as soft dollar synergy, and nearly 70% of M&A transactions fail to deliver on their expected values[3].

The synergistic effect depends on markets, competition and customers, respectively, dependent on volumes and prices, which makes it difficult to control by the merged company. The relationship between the two types of synergy (cost reductions can lead to missed revenue) and the combined effect of the two must be observed.

According to Bulgarian Standartds for evaluation (BSV) , section 1, item 1.5.1. "Value" for the purpose of valuation of objects / assets, is the opinion of an independent valuer, reflecting the value and value of the object / asset, expressed in money, for a specific purpose, at a certain point in time. over time and in the context of a particular market and taking into account relevant circumstances in the course of the valuation.

In the specific report it is necessary to indicate the value of the Synergistic effect, which in the separate evaluation standards is as follows:

The value of a going concern or separate entity is not a value standard (standard) but an assumption of the state of the venture at the time of the valuation. It is the value of an enterprise or a proportion of it that is considered as a viable economic entity. The relationship between synergy and the value of the merged company[4]

2. Sequence of application of the approach in the practice.

The synergistic value is derived by applying all appropriate and applicable approaches and methods, taking into account the elements of complementary and integrative activities and factors that can form a pooled interest and create additional benefits.

This is the value of the Synergistic effect of the financial investments made. A number of factors affect the size and shape of the original price of the transaction, their importance being determined by the specifics of the transaction.

Some factors are quantified (eg synergy), while others are fully subjective.

Based on BSV Part II, Section Five, "Specific and specific requirements for the assessment of MSW are recorded in section 6.3:

* The value of reputation may vary depending on the purpose of the valuation and include elements such as:

* Enterprise-specific synergies resulting from a business combination (such as reduced operating costs, economies of scale, or product mix dynamics),

One of the main approaches used is the estimation of the market values of the individual elements involved in the synergistic effect evaluation system. Avdonina S. In this case, the synergistic effect is a consequence of the integration of the activities of different companies and activities in a single integrated management and management system. This has an impact on the value of the company. By principle, there are three main approaches to assessing Companies:
being. This method is applicable to countries with developed stock markets;

❖ **Income approach.**

It is based on the enterprise's potential to generate income and profits. Different valuation methods may be applied based on projected flows and financial results.

3. Results from the practical application of the approach.

For Company X combining 4 companies, the calculated effect by the two methods shows the following.

- Total value of separately combined assets - EUR 3180 thousand.
- Synergistic value of these assets - EUR 3720 thousand

[3] Early, S., Mergers and Acquisitions: New McKinsey Research Challenges Conventional M&A Wisdom, Strategy &Leadership, volume 32, issue2, 2004, p.4-11
[4] Damodaran. A., The value of synergy, New York, Stern School of Business, Working paper, 2005

BVS	ESV	IVS
Synergistic value is a special value that also includes additional elements of value created by the merger of two or more objects / assets. The synergistic value indicates the value of the pooled interest and is greater than the total value of the individual assets / assets evaluated.	Synergistic Value (also known as Marital Value) "An additional element of value created by the amalgamation of two or more interests when the value of the combined interest is greater than the total value of the two original interests" (IASB, 2007, p. 88 and 414) EVS 2 ESTIMATED BASES OTHER THAN MARKET VALUE 4.3.5. Synergistic value - this is a separate type of special value that valuers often encounter, and is also known as 'marital value'. 4.3.7. Comment - when a special value arises when a pooling of interests results in a greater value than the aggregate value of those interests, which are assessed separately, this value is often described as "synergistic value" or "marital value". The terms of the engagement and the valuation reports must clearly state that such values are required or will be provided and the market value should also be taken into account to determine the difference between the two bases.	70. Value Base as defined in IAS - Synergistic Value 70.1. Synergistic value is an additional element of value created by the combination of two or more assets or interests, where the combined value is greater than the sum of the individual values. If synergies are only available to one particular buyer, then the synergistic value will be different from the market as it will reflect specific characteristics of the asset that have value only for a particular buyer. This added value over and above the sum of relevant interests is often called "marital value." **180.** Subject-specific factors 180.1. For most value bases, factors that are specific to a particular buyer or seller and are not available to participants are usually excluded from the baseline valuation. Some of the subject-specific factors that may not be available to participants are: (a) the added value or reduced value resulting from the creation of a portfolio of similar assets, (b) unique synergies between the asset and other assets held by the entity, (c) legal rights or restrictions with respect to the entity alone, (d) tax breaks or burdens unique to the entity; and (e) the ability to use the asset in a manner unique to the entity. **190.** Synergies 190.1. Synergies describe the benefits of combining assets. When synergies are available, the value of one group of assets and liabilities is greater than the sum of the values of the individual assets and liabilities, which are self-assessed. Synergies are usually associated with cost reductions and / or increased revenues and / or risk reduction. 190.2. Whether synergies should be taken into account in the valuation will depend on the basis of value. For most value bases, only those synergies that are available to other actors should be considered (see the statement on entity-specific factors in paragraphs 180.1-180.3). 190.3. The assessment of whether synergies are available to other actors may be based on the amount of synergies and not on the specific way to achieve that synergy.

Table № 2 *Determinants of the size and payment of the bid price* [5]

	Factors affecting size	*Payment (money, shares, debt)*
For the acquiring company	Expected net synergy Expected contribution of the target to the net synergy Tendency to share net synergy with the target company Availability of alternative investment opportunities Existence of competition for the transaction Presence of defensive tactics of the target Transaction transparency requirements Expected control value	Current debt capacity Cost of debt financing Amount of diluted net earnings per share (when exchanging shares) Transaction size Risk Sharing (Payment by installments) Degree of overvaluation of the acquiring company's shares
About the target	Existence of competition for the transaction Expected contribution of the target to the net synergy Deal type (friendly or hostile) Effectiveness of defense tactics Amount of potential tax liability (increases final cost) Target company value Availability of alternative investment opportunities	Attractiveness of the shares of the acquiring company Shareholders' preferences for cash payment Amount of potential tax liability (preferred stock exchange) Target company growth potential (strategic value and additional premium)

[5] DePamphilis, D., Mergers, acquisitions, and other restructuring activities: An integrated approach to process, tools, cases, and solutions, Elsevier,San Diego, 2012

❖ **Expensses approuch**: The main method in applying this approach is the Net Asset Value Method. The value in this case is a function of both the market value of the assets and the market value of the liabilities. The value of the Synergistic effect can be determined by the difference between FV $equity_1$ - FV $equity_2$, where

FV $equity_1$ – Fair Value of equity before investment;

FV $equity_2$ - Fair Value of equity after investment

In this case, this method is not applicable in the absence of complete accurate and objective information about the state of the assets and liabilities of the company.

❖ **Market approach**.

The Market Analogues method is applied. This method is specific and requires thorough research and information about companies - analogues for which there is complete, accurate and objective information about the transactions performed. In this approach, as in the previous one, it is necessary to determine the difference between the GCC1 - GCC2.

This method is not applicable due to the lack of information on analogue enterprises, both for the period before and for the time

4. Conclusion

Determining the value of the synergistic effect of acquiring financial assets using the income approach is appropriate and accurate for companies with a large number of companies.

In determining the value of the Synergistic Effect, taking into account all known facts and circumstances related to the activity and prospects, including the state of the company's markets, it can be considered as a good decision.

The result obtained by this method shows in value respect better results using the synegic approach.

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