Rock-Tenn, Wendy's/Arby's merge separately, one changes lanes

By Jeremiah McWilliams
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One Atlanta-based company sells roast beef sandwiches and the Frosty. Another makes folding cartons for fast food.

That's where the similarities end for Wendy's/Arby's Group and Rock-Tenn Co. Both made big mergers and acquisitions news over the past week and a half, for different reasons.

Rock-Tenn, built on a string of business consolidations over the past 113 years, just proposed its largest yet: a $3.5 billion takeover of Smurfit-Stone, a larger producer of containerboard, the stuff that makes moving boxes. If approved, the deal will triple Rock-Tenn's size.

Ten miles to the west, leaders of Wendy's/Arby's have encountered the flip side of a merger. They want to break up the company less than three years after pulling the two brands together.

The divergent paths underscore the difficulty of crafting a successful merger or takeover. Such deals create some of the diciest issues in American business: cultural clashes, loss of talented employees and financial benefits that prove elusive. Tread carefully in the minefield, experts have said.

"You know how 75 percent of all people consider themselves above-average drivers? Well, 75 percent of executives probably think they're above-average deal-makers," said Marc C. D'Annunzio, a member of the Siavage Law Group in Atlanta. "Which is impossible."

Rock-Tenn traces its roots back to Rock City Box Co., which was founded in Nashville in 1898. Thirty-eight years later, a Baltimore businessman named Arthur Newth Morris started the Southern Box Co., which bought Rock City in 1944, in the midst of World War II. In 1973, Morris' company merged with a 56-year-old Chattanooga firm called Tennessee Paper Mills to form Rock-Tenn Co.

From its headquarters in Norcross, Rock-Tenn operates in quiet. That's the low-profile nature of the packaging business, chief executive Jim Rubright said.

"All of our customers have a brand identity or a product identity, but ours doesn't," he said. "The general public doesn't know the hundreds of times they touch our products, and they don't know us. Our advertising budget is zero."

That dark-horse approach might be harder to pull off now. Rock-Tenn, adept at churning out and managing cash and paying off debt quickly, is "an emerging industry thoroughbred," Deutsche Bank analyst Mark Wilde said.

It's risky for a company such as Rock-Tenn -- which has less experience in producing containerboard than does Smurfit-Stone -- to buy an industry leader in that segment, said Mark Connelly, an analyst with Credit Agricole Securities. But Rock-Tenn got a good enough deal to protect itself even if prices for its products fall, Connelly wrote.

Rubright insists his company is not looking for "fixer-upper" assets. He likes the fact that Smurfit-Stone invested $550 million in its facilities recently, but added that those plants could be made more efficient.

"We want to be the most respected company in the industry," he said. "We're always looking for very good companies."

Rock-Tenn has completed about a dozen acquisitions stretching back to 1973, including Gulf States Paper in 2005 and Southern Container Corp. in 2008. Those deals helped put it in the big leagues. Its latest will be the boldest yet.

In recent years, Smurfit-Stone has been dogged by a reputation as the packaging sector's most troubled company. Smurfit-Stone emerged from Chapter 11 bankruptcy in 2010 and had no permanent executive-level leadership at the time of Rock-Tenn's takeover bid. The state of limbo hurt morale, as speculation swirled that the company's board was looking for takeover bids.

Rubright said he is encouraged that a number of Smurfit-Stone's leaders plan to stay with the combined company and help run the industrial operations. "These are very strong people that we know, and we've spoken with, and we're counting on them to stay with us," he said. "We think it's very important."

Wendy's/Arby's faces the mirror-image task: how to untangle two big brands. The company has more than 10,000 restaurants, making it one of the country's largest fast-food chains and one of Atlanta's most recognizable brands. Its headquarters west of Perimeter Mall sports a large red Arby's logo, visible for blocks around.

That sign notwithstanding, the company now wants to focus on Wendy's. The brand dates back to Columbus, Ohio, where Dave Thomas' opened his first "Wendy's Old Fashioned Hamburgers" in 1969. The parent company is spending millions to rehab Wendy's menu and stores, and plans to open new restaurants in Argentina. But it will do so without Arby's. Analysts say $600 million or more might be sought for the brand.

What went wrong? Blair Chancey, editor of *QSR*, said the rise of Panera and similar sandwich establishments stole some of the thunder at Arby's. Meal prices in the $7 range became increasingly difficult to pull off as Americans cut their meal budgets. Vicki Bryan, a bond analyst at Gimme Credit, said the brand's marketing doesn't target an identifiable niche.

"They had a lot of competition coming from a lot of different angles," Chancey said.

The parent company's share price has hovered around the $4-$5 range for two years. Nelson Peltz, Wendy's/Arby's chairman and architect of the deal in which the smaller Arby's operation merged with Wendy's, grew impatient and publicly put Arby's up for sale on Jan. 20.

"So ends more than a decade of recycled strategies and numerous management changes that failed to jump-start the struggling brand," Bryan wrote.

In ironic timing, Arby's recently posted better results. Sales grew in the fourth quarter at restaurants that were open at least a year. It was the first time since the merger that the Wendy's and Arby's brands both accomplished that feat. Those results will probably improve the prospects of an Arby's sale, said analyst Sara Senatore. But profit margins have narrowed, and that is worrisome.

"Maybe it's better to acknowledge your mistake" and break up the company, Chicago analyst R.J. Hottovy said. "Peltz has never been shy about doing a deal."

Business school libraries are littered with major deals that failed in spectacular fashion. AOL Time Warner, the leading example for what local corporate and securities attorney Sandy Smith called "the agony of victory," split apart after the old and new media wings failed to work together.

Among some loyal Chicago shoppers, Macy's never recovered from the backlash after it bought Marshall Field's and replaced the retailer's green and white logo with the red Macy's star.

German automaker Daimler might have made better cup-holders than Chrysler, but when it came to decision-making, "They weren't very good," said Usha C. V. Haley, professor of international business at Massey University in New Zealand. American executives felt their German counterparts cut them out. DaimlerChrysler no longer exists.

The takeover of Anheuser-Busch by cost-cutting Belgian brewer InBev precipitated what once seemed impossible: a grassroots boycott campaign in Anheuser-Busch's hometown of St. Louis.

Bankers, lawyers, consultants and executives often fail to adequately plan the post-merger integration, Haley said. They are skilled at accounting for physical and financial assets, but often not as good at the soft skills that help them retain talent. "They are bean counters," she said, "but they are counting the wrong beans."

In any case, buyers are more disciplined than they used to be, industry experts say. Back in the go-go days of the late 1990s, executives at acquiring companies might spend only 12 hours in windowless "data rooms" with their lawyers and accountants, poring over a seller's books. The timeline was compressed; the pressure to buy, intense.

But less generous credit markets forced potential buyers to slow down and put more time into due diligence. By their own choice or not, buyers now have more time to poke and prod. That is showing up in the results. Corporate deal-makers outperformed their non-acquisitive peers on a global basis in the fourth quarter of 2010, according to Towers Watson, a global professional services firm. Companies completing two or more deals over the past 30 months fared even better.

"Practice makes perfect: you learn how to add value," said David Hinkel, a senior consultant at Towers Watson. "One person's damaged brand is another person's opportunity."

Name: Rock-Tenn Co.

Profile: One of North America's biggest manufacturers of paperboard, containerboard and consumer and corrugated packaging.

2010 sales: $3 billion

Employees: 10,400 (400 in Atlanta)

Locations: United States, Canada, Mexico, Chile and Argentina

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Name: Wendy's/Arby's Group

Profile: The third-largest fast food company in the United States, with more than 10,000 restaurants. As of Oct. 3, 2010, Wendy's had 6,554 restaurants and Arby's had 3,662.

2010 sales: $3.4 billion (2010)

Employees: 67,500, including subsidiaries. (520 in Atlanta)

Locations: United States, 24 countries and U.S. territories

How we got the story

Reporter Jeremiah McWilliams talked to professors, analysts, consultants, authors and executives at a range of companies. His reporting covered the restaurant, paper, beer and soft drinks industries, among others. He read research from Wall Street analysts and transcripts of earnings calls. For good measure, he sampled fare from Wendy's and Arby's.
