# US and Europe split on GE takeover of Honeywell

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The proposed $42 billion takeover of Honeywell by the giant US conglomerate General Electric has become a focus for intensifying trade antagonisms between the European Union and the US.

General Electric, one of the world's largest companies, is the owner of brands such as Hotpoint and is also the world's largest maker of jet engines. It employs more than 197,000 workers—with 85,000 in Europe alone.

Honeywell has more than 100,000 employees, and manufactures products for the aerospace industry, also making industrial automation and control systems and is a supplier to the automotive sector.

Both companies are listed on the exclusive Dow Jones stock market index of 30 top firms, but their recent fortunes have differed widely. In April, Honeywell's profits were down 91 percent and the company announced 6,500 job losses worldwide. In contrast, GE's profits rose by 16 percent in the first quarter of the year, despite an economic slowdown, reaching $3.017 billion for the three-month period.

General Electric's planned takeover of Honeywell was agreed in October, and would be the largest in industrial history, increasing GE's size by nearly a third. It was launched after GE broke up merger talks between Honeywell and United Technologies (UTC) and faced off competition from US company Tyco and Germany's Siemens.

US anti-trust investigators approved the GE-Honeywell deal in May, with the minor proviso that the merged group sold off a helicopter engine business. But there is little chance that the European Commission will allow the takeover to go ahead, despite intense lobbying by the Republican administration in the US.

The Commission is the regulatory body of the European Union (EU), and can block or force changes to company mergers and takeovers, even when they are not by European firms. EU law requires that all companies, regardless of where they are based, notify the Commission about planned mergers if their combined worldwide annual sales exceed five billion euros ($4.3 billion) and at least 250 million euros ($215 million) worth of their business is done among the 15 EU nations.

The Commission has made plain its fears that the combined group would hold too high a share of the world's aerospace markets. GE and Honeywell together would possess a near-monopoly on engines for large regional jets, and its competitors such as United Technologies and Rolls Royce have urged regulators to insist on business divestments and/or restrictions on its marketing. The Commission responded by drawing up a 140-page statement of objections to the deal, stating that GE was using its financial might to sway airlines and aircraft manufacturers to choose GE engines and demanding the company divest itself of some of its aerospace operations worth more than $6 billion a year.

If the Commission does decide to block the deal, it will mark the first time European regulators have rejected a merger between US companies that has been approved by the US Justice Department.

GE's Chairman Jack Welch met with the EU's Commissioner for Competition Affairs Mario Monti for two days last week and proposed to sell off Honeywell's aerospace business worth $2.2billion, far less than the divestitures being demanded by the Commission. GE said that it was willing to dispose of its regional jet business and parts of Honeywell's avionics systems, but rejected the EU's request to spin off GE Capital Aviation Services, or GECAS, the company's highly profitable financial and airplane leasing arm. Monti said the Commission would be willing to accept smaller divestments in the aerospace industry, if the two companies would entertain "a structural commitment to modify the commercial behaviour" of GECAS. However GE subsequently issued a statement declaring it was "not optimistic that its proposal will meet with European regulatory approval." Welch was barely able to disguise his anger, telling reporters, "I wanted to complete the transaction but we have always said there is a point at which we wouldn't do the deal. The Commission's extraordinary demands are far beyond that point. This shows you are never too old to get surprised." He added that "The European regulator's demands exceeded anything I or our European advisors imagined, and differed sharply from antitrust counterparts in the US and Canada."

The EU has until July 12 to decide whether to reject the takeover, but the fact that it was expected to do so helped provoke a sharp fall in US share prices last week. On June 14, the blue-chip Dow Jones industrial average tumbled more than 100 points in the first hour of trading, shortly followed by the Nasdaq composite index. Falls in Honeywell and GE shares accounted for over a fifth of the Dow's losses and there is a clear danger of bigger losses to come. Hedge funds and investment banks could face massive losses if the takeover fails. Risk arbitrageurs, who make money by exploiting the difference in share prices between two companies involved in a merger or acquisition by buying shares in the target company, hold an estimated one-quarter to one-third of outstanding stock in Honeywell—200-300 million shares. A sell off would wipe out an estimated $3 billion.

During his first visit to Europe last week, US President George Bush made a special point of expressing his anger at the Commission's decision. Before giving a major foreign policy speech in the Polish capital of Warsaw, Bush told reporters, "I am concerned that the Europeans have rejected it [the merger]." He warned that America "has a strong interest in fair treatment" of GE and Honeywell. The president's remarks were endorsed by US trade representative Robert Zoellick. The US administration also raised the GE-Honeywell case at a meeting with EU leaders in Gothenburg, Sweden.

Commerce Secretary Donald L. Evans, speaking to reporters at the Paris Air Show last week, urged the Commission to make a more positive assessment, while Zoellick told reporters that although the Bush administration did not wish to question the EU Commission's sovereign powers, Washington was troubled by the apparent impasse between the Commission and the two companies.

In response, Monti denounced "political pressure" from Bush and other members of his administration, and insisted the merger would be judged strictly on legal and economic merits. "I deplore attempts to misinform the public and to trigger political intervention," he said. "The nationality of the companies and political considerations have played and will play no role in the examination of mergers, in this case as in all others."

Monti's statement is disingenuous. Nationality clearly does matter when dealing with such a massive commercial venture. A negative decision by the Commission would clearly reinforce protectionist sentiments in the US and possibly escalate into a full-scale trade war.

The aerospace industries are a central arena for trade conflicts between the US and Europe. At the Paris Air Show, Europe's main aircraft manufacturer Airbus announced that it had beaten off its US rival Boeing to secure a $9.4 billion order for 111 planes from the US-based leasing company ILFC, including a commitment to buy five A380 super jumbos, which will be capable of carrying up to 800 people each. Airbus's military division was also given a memorandum of understanding by EU defence ministers that they would buy 212 A400Ms, Europe's first heavy-lift military cargo plane for a number of years, with contracts to be signed at the end of September.

Boeing vice-chairman Harry Stonecipher followed Bush's statement, accusing Airbus of forcing the European Commission's hand by opposing the merger of GE and Honeywell. He warned in an interview with *Le Monde* newspaper that the dispute could spread into the commercial arena. "The US approved this merger and if Europe rejects it, what will happen? You don't exactly become friends," he said. Boeing's vice-chairman called Europe's plans to procure more than 200 new transporters made by Airbus, the A400M, economically "absurd" when US planes could be built more cheaply.

Noel Forgeard, Airbus chief executive, responded angrily, stating that he had held extensive talks with the Commission and Jack Welch, General Electric's CEO, and had raised no formal objections to the merger. He accused Stonecipher of threatening the Brussels competition authorities and of making "highly inappropriate political comments" against the French president and France's national security.

Republican Senator Phil Gramm told CNBC news, which is part owned by GE, "I think this is something that's troubling, something we need to look at. It's a very real question what power the EU should have in dealing with two companies that are fundamentally American companies." Meanwhile two leading members of the US Senate's antitrust subcommittee, Chairman Herb Kohl and ranking minority member Mike DeWine, have said they plan to examine why American and European antitrust officials reached such different conclusions. They expressed concern about the effect of the EU's stance on other US businesses, warning that divergent positions between the EU and America would "hinder the development of free and open markets and will impede efforts by American companies to expand into the global marketplace."