

## Dell, IBM clash over M&A executive

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Eager to step up acquisitions, Dell tells its managers to find deals and locks horns with Big Blue over veteran IBM dealmaker David Johnson.

Dell is taking some extraordinary steps in its effort to transform itself from a company that has long relied on organic growth into one that makes aggressive acquisitions.

The computer maker has hired David Johnson, a former mergers and acquisitions executive at IBM (IBM), despite a court order that places strict limits on what he can and can't do at Dell (DELL). In addition, Dell has directed heads of its business units to scout for deals, and even tied part of their compensation to company growth through acquisitions, says a person close to Dell. Any deals would be executed by a central finance team, but tech industry observers say it's unusual to turn divisional executives into deal hunters.

It's imperative that Dell buy companies—possibly in technology services and software—to inject profitable growth into a company whose sales and market share in key areas are sliding, say investors, bankers, and industry analysts. Dell has acquired just 10 companies since 2006, the largest being storage company EqualLogic, purchased for \$1.4 billion in 2007. "They need to keep transforming their business model," says Murray Beach, a managing director at investment bank TM Capital. "The value of making boxes has clearly diminished."

By trying to make Johnson its head of mergers and acquisitions, Dell hopes to add a veteran who did deals for nine years at IBM and who possesses a rarefied set of skills at acquiring and wringing value from companies. "There aren't that many of these people," says Elizabeth Lewis, a partner who specializes in employment law at law firm Cooley Godward Kronish.

### Dell: keeping mum on Johnson's role

Johnson, 55, would be part of an M&A team that's being assembled by Dell, according to bankers and PC industry sources. He worked on all of IBM's acquisitions and divestitures the past several years, including its \$3.5 billion acquisition of PricewaterhouseCoopers' consulting business in 2002, according to a person close to IBM. Johnson possesses "truckloads of information" about companies IBM plans to acquire, this person said. Dell has also retained consultancy McKinsey for advice on acquisitions, according to one investor.

Dell spokesman David Frink confirmed that Johnson is working at Dell, but declined to provide details about his role or other M&A work at the company.

In order to put Johnson in charge of its M&A activities, Dell will need to prove at a June 22 court hearing in White Plains, N.Y., that he can do his job without harming IBM. In a lawsuit filed against Johnson on May 21 in U.S. District Court in the Southern District of New York, IBM says Johnson's employment at Dell would violate a noncompete agreement he signed and would compromise IBM trade secrets—including companies it plans to acquire.

At least until that hearing, Johnson is working at Dell under heavy restrictions. A June 4 court order prohibits Johnson from advising Dell "on any matter concerning business strategy," and requires him to submit to his lawyer a daily log of his activities there, including "the amount of time involved and all persons involved." The court may allow IBM's lawyers to inspect the log. At the June 22 hearing, Judge Kenneth Karas could allow Johnson to continue working at Dell until a decision is reached—or he could issue an injunction barring Johnson from working there until a trial decides the issue.

### Executive bonuses linked to takeovers

Even with those limits, Johnson's employment at Dell is a setback for IBM, says attorney Lewis. "It's definitely a positive for Dell," she says. IBM will eventually need to show that Johnson possesses true trade secrets, not just highly valuable skills, Lewis says, citing a June 9 ruling by a federal judge in Wisconsin that let a former Clorox (CLX) executive begin working for rival S.C. Johnson & Son, despite what Clorox said is sensitive information about its operations known by the executive.

Hiring Johnson isn't Dell's only move to amp up its buyout capabilities. Executives, including enterprise group president Steve Schuckenbrock and public sector group president Paul Bell, have been asked to look for acquisition candidates, and part of those executives' bonus payments are tied to acquisition-related growth in their divisions, says a person close to the company. The plan is tied to a company realization that Dell's prospects for profitable growth through selling more hardware are limited, this person says.

Dell's Frink declined to comment on specifics of the plan, although he says many employees are responsible for bringing good ideas for acquisitions to their managers and that growth is an element of measuring all employees' success.

In addition to building a war chest of \$10.1 billion in cash and short-term investments as of the close of the quarter that ended May 1, Dell has been raising debt to augment its buying power. It raised \$1 billion in bonds on June 10 that it will likely use to finance acquisitions, Kaufman Bros. senior analyst Shaw Wu wrote in a June 11 research note. "Dell needs to take bigger and bolder steps" to compete with IBM, Hewlett-Packard (HPQ), Apple (AAPL), Acer, and Cisco Systems (CSCO), said Wu, who has a "hold" rating on Dell's stock.

#### Tech companies: cheap and willing

Analysts say possible targets for Dell include Palm (PALM), Motorola (MOT), BMC Software (BMC), and Affiliated Computer Services (ACS). Adding consulting expertise now would be a timely move. Microsoft (MSFT) plans to release its Windows 7 operating system in October and computer makers could benefit from businesses' pent-up demand for new PCs running the system—and for the expertise to install it efficiently.

As Dell looks to bulk up, it may benefit because tech companies are willing to deal amid a slow sales environment and depressed stock prices. On June 4, Intel (INTC) spent \$884 million to buy software maker Wind River Systems. Storage companies NetApp (NTAP) and EMC (EMC) are duking it out over Data Domain (DDUP). "Asset prices are getting pretty attractive and certainly we're looking at expanding inorganically," Chief Executive Michael Dell said in a conference call with Wall Street analysts on May 28.

At the same time, it faces a formidable opponent in IBM. Tech companies have been turning to the courts to prevent valuable employees from jumping ship as vendors develop expertise in areas that open new fronts of competition. Last October, IBM sued to prevent Apple from hiring chip expert Mark Papermaster in a case that was eventually settled. IBM and Papermaster agreed to delay his starting date at Apple and agreed that Papermaster would keep sensitive IBM information confidential. On June 3, a California judge blocked former EMC executive David Donatelli from overseeing Hewlett-Packard's storage business, though he continues to work at HP.

Finally, Dell needs to show investors that it has the chops to absorb acquisitions at a faster pace. "Whatever they buy, I hope it's small and easy to integrate," says Jayson Noland, a senior analyst at Robert W. Baird, who has a "neutral" rating on Dell stock. "Large, transformational M&A is going to cause all sorts of risks and uncertainty."

Retaining Johnson and building an M&A team around him could help allay investors' worries. No wonder Dell is going to such extraordinary lengths to keep him.

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