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## EBay on the Prowl

Its track record on acquisitions is mixed, but the e-commerce titan is about to go shopping again

by [Catherine Holahan](#)

Electronic-commerce giant eBay ([EBAY](#)) epitomizes the buying spree reshaping the tech landscape, and its mixed record on mergers presents a case study in what would-be acquirers should and shouldn't do to ensure a takeover succeeds.

Like many companies in techdom, eBay has a wad of cash, zero debt, and is looking to fill product gaps by snapping up smaller, nimbler companies on the cheap. "EBay is a strategic player and has a lot of cash, so that is why it could be viewed as more of a buying opportunity for us," says Lorraine McDonough, eBay's mergers chief. The company has about \$5 billion on the balance sheet and anticipates generating an additional \$2.3 billion to \$2.4 billion in free cash flow by the end of the year. Other big tech acquirers, including Microsoft ([MSFT](#)) and Cisco Systems ([CSCO](#)), are also flush with cash, though Microsoft has said it would use debt to finance its proposed acquisition of Yahoo! ([YHOO](#)).

### THE SUCCESS OF IBAZAR

And like its peers, eBay is turning to acquisitions to fuel growth. Speed to market in the tech industry is key, where the first company not only grabs early adopters but can develop a new, improved version often before competitors can catch up to the original offering. As its core U.S. shopping business has slowed, eBay has turned to acquisitions to enter new, higher-growth markets.

By buying during a downturn, techdom is bucking the tendency among other industries to hoard cash when the going gets rough. Worried about their declining share prices, companies wait to make deals. "You don't go remodel your kitchen when you are feeling poor, you do it when you feel wealthy, and companies feel wealthy when the stock is doing well," says Anant Sundaram, an M&A expert at Dartmouth College's Tuck School of Business.

Indeed, some of eBay's best deals have come amid market turbulence. In 2001, as the air began escaping from the tech bubble, eBay acquired European e-commerce site iBazar for about \$125 million. iBazar had planned an initial share sale and saw itself as

an eventual eBay competitor. "We were going to build this business and we were going to IPO, but then the bubble burst and the IPO prospect became extremely distant," says Andre Haddad, iBazar's founder. Now eBay is the leader in many of iBazar's original European markets. More than half the revenue from eBay's shopping sites comes from outside the U.S.

## **INTEGRATION ISSUE**

Not long after eBay bought iBazar, it acquired online payment service PayPal. The \$1.5 billion purchase, made in 2002, has paid off in spades. With PayPal, eBay found an almost ideal complement to existing businesses. Millions of people use eBay to buy and sell. PayPal gave them an easy, relatively secure method for making payments and carrying out transactions online.

Skype, on the other hand, exemplifies a deal gone wrong. eBay purchased Skype for \$2.5 billion in 2005, hoping that Skype's calling services would help shoppers easily connect with sellers, getting the answers needed to complete a transaction. The service, however, didn't pay off as planned. In 2007, eBay took a \$1.4 billion charge against the purchase. "We are happy to have the earnout behind us, and I think that will allow us to focus more on potential synergies that we have been slow to develop and disappointed with to date," McDonough says.

The Skype example illustrates the risks of any acquisition-heavy strategy. There's always a risk of overestimating benefits and overpaying, particularly when competitors are also interested in the target. Though those risks lessen in an economic downturn, they don't go away. There's also the problem of integration. Not only must an acquirer meld a new company's technology and culture with its own, but it also must import its desired changes and business models without scaring off the target company's clients.

## **SHOPPING CORE**

Perhaps nobody understands the challenges of integration better than iBazar's Haddad. iBazar's community, accustomed to free transactions, revolted after eBay began demanding fees. "It was very hard," Haddad says. "We had a seller strike... we had lots of negative PR. I had lots of notes from people saying, 'You betrayed us, you sold to the big company.'" Haddad stuck around to help the enlarged company manage the PR nightmare. He's now CEO of eBay's Shopping.com business.

But keeping top talent isn't always a given. Should Microsoft succeed in clinching the Yahoo deal, it may need to strive to keep the target company's best people. Luring valuable staff was a big motivation for eBay's January purchase of Fraud Sciences for \$169 million. "It was an acquisition for great technology as well as a fantastic group of talented engineers," McDonough says.

Analysts see several additional targets for eBay this year that look like good deals. Overstock.com ([OSTK](#)), an online retailer that sells surplus merchandise at a discount, has declined 75% from its Oct. 31 high, to \$9.50 a share. "It looks like a great bargain," says [American Technology Research](#) analyst Tim Boyd. (Overstock is adamant that it is not for sale.)

McDonough is quiet about eBay's potential targets, but it's clear she has many in mind. In particular McDonough says eBay will look for businesses that can support the core shopping site. For that, it's going to do a bit of shopping itself.

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