

WHITE PAPER

What makes Mergers and Acquisitions Succeed or Fail?

**Sustainable Financial Returns through
Effective Leadership and Communications**

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What Makes Mergers & Acquisitions Succeed or Fail?

We have all read in the business press about various high profile mergers and acquisitions and their respective impacts in the market place. Some are seen to be a success and others are seen to be failures. Why is this?

This white paper outlines the main recurring themes that influence the success of mergers and acquisitions.

Signing the Deal is not the end – it is just Beginning:

Traditionally the focus of work has been on pre-deal activities such as due diligence and contract negotiations. This work is very important and crucial part of the transaction process.

However, it is worth remembering that, at the time the deal is signed, all the benefits expected from the deal are on paper only, and have not yet been tangibly realised in terms of growth and ongoing synergies and returns for stakeholders.

It is the post-deal Integration activity that determines how well the business realises the tangible returns from the deal.

Recent research by AT Kearney identified Integration execution as critical to the success of any merger or acquisition transaction. The next three highest ranking factors were professional integration management, integration approach, and communications.¹

All of these success factors demonstrate the importance of post-transaction integration and the need to engage professional specialists in the field.

Have a Clear Strategy:

It is important that a business has a clear strategy for growth, with clear delineation between how growth will be derived organically and via mergers and acquisitions.

This would also include profiles of ideal merger and acquisition target businesses that align with the overall growth strategy. The profiles would include size (market, sales, employees, etc.), product/service lines, customer base, market demographics, brand presence, how benefits will be identified and measured, and required price multiple/rate of return.

Without this clear strategy businesses tend to acquire target businesses that are not the “right fit”. This in turn leads to an erosion of ROI and other key ratios, difficulty in realising synergies, and less than seamless integration.

In the case of mergers and acquisitions that succeed there is always a well planned strategy to which the transaction is firmly aligned.

¹ Source: “Three Years After the Marriage – Merger Integration Revisited” © 2008 AT Kearney. All rights reserved.

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Strong Leadership:

It is important that there is strong leadership in place to drive the growth strategy.

This is particularly important in mergers and acquisition there are two Boards and two senior management teams coming together. Individually they will have different views on the merits of the transaction and their own agendas. This means they will have differing levels of engagement in wanting to make the transaction a success.

A strong leader is needed to galvanise the leadership team. This would normally be the CEO of the post-transaction business. The business must act swiftly in appointing the new board and senior management team, engaging, motivating and incentivising them to be part of making the transaction a success.

In research Leadership is consistently cited, along with integration execution, as the primary critical success factors in determining a merger or acquisition's success.¹

This strong leadership flows through to the Integration project. One of the recurring key factors why integration projects fail is a disengaged Steering Committee. The Steering Committee would comprise CEO as the chair and overall sponsor and senior management team, each of them acting as sponsors for specific project streams.

Focus on Growth not just Cost Reduction:

This is an extension of the need for clear strategy. The most obvious synergy opportunities often relate to cost reduction because, after the transaction, there is no need for duplicated IT systems and business processes, duplicated roles and departments (e.g. IT, accounts, purchasing), two Boards or two sets of senior management.

Cost reduction is important but far greater returns from the deal are in identifying opportunities for growth arising from the transaction. This may come from opportunities such as expanding customer base and market share, expanding the range of complementary product and service lines, and gaining competitive or first mover advantage.

Research shows that 67% of respondents quoted growth strategies as part of their overall merger objectives compared to only 24% quoting cost reduction measures.¹

It is worth remembering that that there is a limit to the extent that costs can be reduced, whereas the extent to which growth can be achieved is unlimited. Furthermore, it is very difficult to grow a business but cutting back on investment in staff, technology and other capital.

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Understand the Full Meaning of “Integration” in all its forms:

Successful Integration takes many forms. There are the traditional tangible forms such as integration of IT systems and business processes, and there are other more intangible forms such as cultural integration and brand alignment.

In successful mergers and acquisitions the business addresses “Integration” in all of these forms: -

Traditional Forms of Integration (more Tangible)

- ✓ Systems Integration
- ✓ Business Process Integration

Other Important Forms of Integration (more Intangible)

- ✓ Cultural Integration
- ✓ Customer Integration
- ✓ Brand Alignment
- ✓ External and Internal Communications

Traditionally the focus has been on the tangible such as Systems Integration but consider this - usually in an acquisition the largest asset “purchased” is Goodwill. So what is Goodwill? It’s the business’ people and customers.

Therefore, addressing the other important forms of integration - Cultural Integration, Customer Integration, Brand Alignment and Communications - will protect the value of goodwill.

The British Institute of Management, Watson Wyatt, and many other researchers have all come to the same finding – “Culture Clash” is the reason why most mergers and acquisitions fail,

stressing the importance of Cultural integration and Internal Communications.²

Inconsistent branding following the Hewlett-Packard and Compaq merger led to brand confusion from customers and loss of identity by Compaq employees.² This stresses the importance of Customer Integration, Brand Alignment and external communications. It also demonstrates the close relationship between internal cultural integration and external brand alignment.

Therefore, a disciplined approach to “Integration” in all its above forms will therefore not only preserve the value of the underlying tangible assets, but also goodwill, which will position the business to maximise returns from the transaction.

Do Not Underestimate the Effort Involved in Integration:

The amount of effort involved in fully integrating the post-transaction businesses should not be underestimated. It is a full-time project lasting for several months requiring a large amount of internal and external resources.

This amount of effort is often underestimated and businesses seek to resource the integration activities using internal staff, sharing their time between the project and their line roles, without a clear project structure.

This can lead to the disruption of business-as-usual as the business becomes inwardly focussed on the integration. Customer service levels drop and staff become stressed. This in turn leads customer and staff attrition and opportunity for competitors to take advantage, again

² Source: “Achieving Post-Merger Success” by J Robert Carleton and Claude S Lineberry. © 2004 John Wiley & Sons Inc.

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eroding the value of the goodwill purchased in the transaction.

Successful post-transaction integrations are achieved by engaging specialists with proven methodology to run a structured project, with the optimal combination of experienced internal and external subject matter experts, with full engagement and sponsorship from senior management.

Expected Synergies and Returns must be Realistic:

The flurry of Private Equity driven transactions in 2007 has resulted in many financially highly-leveraged acquisitions, making it essential for the synergies to be realised from those transactions to service the debt that has funded them.

The temptation during pre-deal activities is to over-estimate the value of the synergies. This is especially so when the pre-deal advisors are not going to be involved in post-deal activities and therefore do not have any consequential responsibility realising the synergies they have estimated.

Unrealistic synergies will lead to lower than expected ongoing returns to stakeholders, erosion of key ratios such as

ROI and asset turns, and a consequential write-down of purchased goodwill.

Expected Synergies and Returns must be discretely Measurable:

Often businesses do not put a mechanism in place to identify, track and report on the specific synergies from the transaction,

Instead the business reports on overall performance, which means that if the growth in overall returns from synergies are not as high as expected, then the business cannot specifically identify why.

The key is, as part of integration planning, to identify how each individual synergy will be captured measured and where the data will be sourced from. The appropriate accounting processes can then be put in place to capture and report on each specific synergy.

This not only provides visibility on how much realised synergies are impacting overall performance but also identifies which specific synergies require attention if returns are less than expected.

Mergers and acquisition success is not an exact science but is always achievable with the right approach. The key is to understand all the above different ingredients that contribute to the success and engage post-transaction integration specialists.