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MAKING M&A WORK

Designing a New Business Model

Science or Art?

Why do so many restructuring initiatives fail? The problems sometimes lie not in poor execution, nor even in the implementation of the wrong business model, but rather in a fundamentally-flawed business model design process.

Whether driven by a recent merger or acquisition, a need to consolidate several past acquisitions that have been ineffectively or poorly-integrated, or to reposition the business for the new world ahead, many companies are likely to undertake some kind of organisational restructuring in the coming years.

Major initiatives are not only underway in headline-grabbing areas such as automotive, banking and retail, but even across 'safer' sectors such as pharmaceuticals (Merck, Pfizer), infrastructure (British Telecom, Centrica), and public sector (Royal Mail).

Without wishing to add our voice to the current zeitgeist of seismic paradigm shifts, we are seeing many businesses considering the need not merely to adjust incrementally or improve their current business model, but to fundamentally reassess and rebuild it from the ground up to prepare for a post-recession world that will be very different to that of the past. As Paul Staples, Head of UK Corporate Finance at BNP Paribas states, "Companies have increasingly realised that tactical responses tend to disguise the growing imperative to redesign their business models to achieve sustainable returns within a new economic order. Acquisition assessment criteria are also changing to reflect an understanding that many business models will need to change quite significantly to be successful, and best practice in business process re-engineering and post-merger integration will necessarily respond and adapt to these changes."

There is always pressure to conduct restructuring initiatives quickly and with minimum disruption to the on-going business (also known as 'changing the tyres while the car is travelling at 90mph'). Nonetheless, the current squeeze on capital, cash flow, and boardroom patience is only going to increase the imperative to 'get it right, do it quickly, and keep it cheap', regardless of whether you are chasing new opportunities or just struggling to stay afloat. Failing to find the right balance of quality, time, cost and risk is no longer just an expensive mistake to be fixed later. Consider the recent experience of Chrysler (who initiated a major restructuring programme in 2007 following their demerger with Daimler; 18 months on, some are openly debating whether an 'orderly bankruptcy' might now be their best option); or that of Woolworths, who spectacularly, if not unexpectedly, went bankrupt in late 2008 despite several attempts to restructure the business earlier that year.

So, be it post-deal or otherwise, why do so many restructuring initiatives fail? The problems sometimes lie not in poor execution, nor even in the implementation of the wrong business model, but rather in a fundamentally-flawed business model design process.

Business or Operating Model design initiatives are typically guided by deep, comprehensive, numerical analyses of the external environment, market opportunities, business performance and financial structure, all of which are used to provide a detailed and solidly-justified view of how the business should be organised and operated going forward. While such a fact-based approach is clearly vital to the integrity of the final design, it's not enough. What can be overlooked in the rush for the 'right answer' is the impact of individuals, especially those within the executive team, in ensuring long-term engagement and 'stickiness' of any new Operating Model. Furthermore, such analytically-driven approaches can end up losing sight of the big-picture strategy, objectives or principles underpinning the entire enterprise. In cases where redesign is not about tweaking the existing model but increasingly about starting (almost) from scratch, a content-only approach can be disastrous.

Ultimately, if CEOs are planning to design a new Operating Model for their business, and they intend to do so in collaboration with their executive team or lower levels of management, then the *process* by which people are engaged in the exercise is at least as important as the analysis or hard *content* design that results from the exercise. As any engineer will tell you, there is no single right answer in the design of a complex system (although there are certainly many wrong ones). In any business in which vision, leadership, and engagement make a vital contribution to success (and show me one that doesn't), the *best* design is the one that has the strong support of the team required to execute and sustain the resulting restructuring, not the one that may reflect an optimal design on paper, but which has little executive support.

While perhaps an obvious point in principle, this has several important implications that are often overlooked in the early stages of design.

Many of us can recall cases in which the CEO considers their business strategy to be clear, credible, robust, and fully-supported, while individuals within their Executive Team silently harbour real doubts about its direction or executability.

Pushing past this issue and avoiding the hard discussions is a false economy: This 'pain later' approach invariably leads to the eventual unravelling of the entire exercise.

Ensure the executive design team is rock-solid in its understanding and support of the business' vision and strategic plan:

Many of us can recall cases in which the CEO considers their business strategy to be clear, credible, robust, and fully-supported, while individuals within their executive team silently harbour real doubts about its direction or viability. More commonly, a robust strategy may be clearly understood by the CEO or top team, but is subject to multiple interpretations even among those managers tasked with delivering it.

The first step in any restructuring process is therefore to ensure clarity, consensus and support for the group's strategy and objectives across the design team, not in a way that presumes agreement up-front, but instead actively stress-tests this commitment. If a common view of strategic priorities and objectives is not shared, stop the design process and take as long as is necessary to address their concerns, get them on board, or if necessary remove them from the process.

It can be extremely tempting in such situations to push ahead regardless, hope that the process itself will build the necessary support, and so avoid facing some early hard questions and decisions. This is a false economy; this 'pain later' approach invariably leads to an unravelling of the entire exercise, usually not immediately, but often just before the final model is approved. As one FTSE100 finance director said to me post-merger, "We don't believe in the corporate strategy, nor do we believe in our CEO's ability to execute it. Until we do, everything that follows will be built on a foundation of sand."

Establish clear objectives, ground rules & leadership:

Collaborative Operating Model design is in fact an extremely, personally, emotive exercise. What you are in effect doing is asking individuals to work in an open team to make recommendations and decisions that directly impact their own roles, responsibilities, level of authority and long-term career prospects. For such an exercise to have any chance of success, the process must be strongly sponsored and tightly facilitated, so that everyone knows and accepts:

The purpose and (specific, measurable) objectives of the restructuring exercise;

The process by which new designs will be assessed, developed, debated, and approved;

Business areas and aspects that are open for debate vs. those that are off-limits;

Sponsor, team and individual roles in the process; especially how decisions will be made;

The solid intent to execute whatever is ultimately approved;

How log-jams, disputes and areas of uncertainty will be resolved.

Such questions are often best addressed through a simple set of bulleted 'guiding principles' for design; better still, have these principles developed by the team, as a team, at the start of the process. These guiding principles can then improve teamwork, and help the team avoid poor design practices or decision making, in the same way that a clear business strategy and solid business analysis will help them avoid subjective, 'faith-based' (i.e. irreconcilable) differences when debating options.

Pick the right team, and be mindful of team dynamics during the process:

If a collaborative process is to truly build engagement through active participation, those tasked with the design and decision-making must represent the future leaders of the business, both divisionally and functionally. Admittedly there can be some iteration required as executive roles and reporting structures can be confirmed as part of the process. Nonetheless, work hard to avoid the use of e.g., team members who have no direct relation to the business area in question, despite their ability to lend objectivity to the process (good intention, bad end-result); a corporate-heavy team designing an Operating Model for a different part of the business; a mix of

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senior and junior staff (in which some will feel more equal than others); a team representing only one side of a merger or acquisition; or a consultative/ advisory team (internal or external) with no 'skin in the game'.

Where necessary, take some time up-front to accelerate relationship- and team-building, especially in post-M&A scenarios in which both sides may have no knowledge of the other, or worse still may have been openly-antagonistic competitors the previous month. Take the team 'pulse' regularly (conducting self-checks both as a team and individually) and identify and address emerging team issues immediately, before a dissatisfied team member disengages from the process, thereby making the final design considerably harder to implement.

As you proceed through analysis, team assessment of options, and decision-making, perhaps iterating through lower levels of detail, take each phase one step at a time, ensuring genuine team commitment to the output of that phase before proceeding to the next (a simple *Outstanding Issues* Register can help the team move forward without feeling the need to agree on every non-material issue, provided there are clear rules on how to define what is considered 'material').

Take an holistic view of your Operating Model:

Business restructuring is about much more than financial projections and organisational charts and if either of these appears in detail in the early stages of your design, you may have a situation in which the cart is leading the horse. Whether your design approach is 'bottom-up' or 'top-down' (and both can work under the right conditions), consider all aspects of an Operating Model as you proceed, paying specific attention to the interrelation of each.

There are no generalised rules regarding the degree of sophistication or techniques used to consider each aspect, so be guided by your business strategy and restructuring objectives to decide how much detail, time and effort may be necessary for each. It can be tempting to insist on a deep, uniform level of detail to be provided for every area, and so descend into a rat hole of analysis and design (especially in areas such as process and culture, where for some the assessment and design tools can become more important than the information or insights they convey). Be prepared to regularly challenge the relevance of each step and decide 'that's enough detail for what we need right now'; conversely too little detail in an area pivotal to your strategy or objectives can be equally dangerous (albeit easier to spot).

The point is to ensure that your Operating Model design is being *guided* by the data, not *driven* by it: use your preliminary strategic rationale, assumptions and debates to determine where further detailed analysis is warranted, as opposed to conducting weeks of detailed analysis before beginning any group discussions. This will help ensure that your data analysis efforts remain fast, focused and relevant.

To illustrate the interrelation between different aspects of an Operating Model, consider an example in which your strategy dictates a move to on-line promotion and provision of your products via the internet: how will this play into the current market

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perception of your brand and reputation? What are the implications to your existing Sales, Marketing, Order Processing and Supply Chain groups? What new processes and technologies will be required to support the demands of your new e-customer base? What new organisational capabilities will your business require to manage this new mechanism as new IT platforms & technologies emerge? How will your current organisational culture respond when faced with these new demands on your business, and will aspects of it need to change? What new measures and incentives might you need to establish to encourage the right behaviours? And of course, how should functional groups, individuals, roles and responsibilities be organised, and what is the financial model that justifies this new route to market. The value of the exercise comes not from a deep and detailed response to each of questions, but rather from a concise, experience-driven view that can be used to highlight internal conflicts in the model (i.e. new processes or measures that will undermine desired behaviours; cross-functional processes that map poorly to the organisational structure), and that can be translated into concrete actions for your restructuring plan.

Keep it simple:

The best top-level Operating Model documents typically contain no more than 20 to 30 pages of clear, simple (often bulleted) principles, structures and decisions. It should be easy to read, easy to understand, and therefore easy to communicate and build plans around – that is after all the purpose of the document. Brevity also enforces clarity of thought: if a principle or decision within your Operating Model requires 20 pages of words and data to explain, the likelihood of its successful execution is slim at best.

Ultimately, a collaborative, well-facilitated Operating Model design process represents an excellent way to build the team that will be responsible for taking the restructured business forward, while also learning about the participants themselves and how they will behave within the new business. If done well, it is possible to create an environment for debate and decision-making in which individuals will openly agree to a design that is best for the business, even if not for their own long-term career within the business. If you see such behaviour, you know you have hit the mark, and are likely to find implementation of your restructuring considerably easier. It will also shine a spotlight on those prepared to constructively compromise in the interests of the a reshaped business, as opposed to those more interested in protecting their own territory and the *status quo* – highly-useful perspectives as you move together into implementation.

ABOUT THE AUTHOR

Carlos Keener is a specialist in M&A Integration, and the founder of Beyond the Deal, a business that provides acquisition and integration strategy, planning and execution support to clients worldwide. In addition to leading M&A and integration programmes, Carlos advises businesses on corporate and acquisition strategy; enterprise operating model design; integration strategy, planning and execution; and turnaround of poorly performing acquisitions.

Before establishing Beyond the Deal in 2001, Carlos was a senior consultant at PricewaterhouseCoopers, and a senior manager within Accenture's Corporate Strategy and M&A practice. Based in the UK, Carlos' work has taken him across Europe, the US, Africa, Latin America, the Middle-East, and the Far-East.

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