Planning & Preparing for Integration

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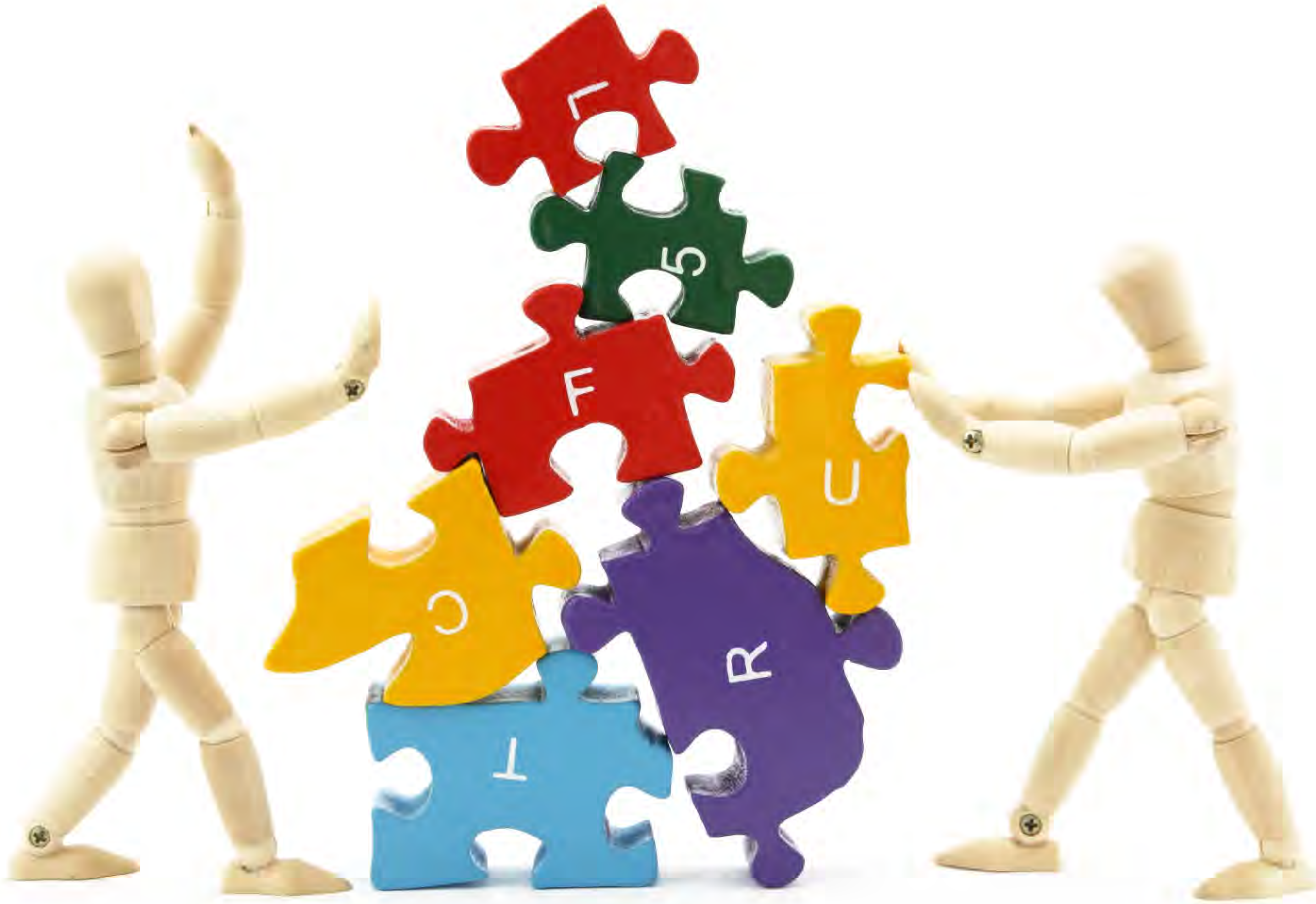

Mergers and acquisitions often fail because an inappropriate integration strategy is chosen or – worse still – no conscious strategy is adopted, leaving the final form of the combined organisation to shape itself.

Carlos Keener, *a Criticaleye Advisory Partner in the area of post-merger integration, takes questions from the Criticaleye Community on how to plan and prepare for integration in the realisation of real M&A value*

When in the pre-deal process should you start considering integration? Where/how do you start?

The classic answer is when you think the deal is more likely to happen than not. Naturally, I disagree as the issue with this question is that it implies there is a time when you're not thinking about it and, as integration is the time when you're actually getting the value from the acquisition, that is dangerous.

You need to be thinking about integration all the way back to your acquisition strategy. That doesn't mean that you must pour in major resource that early, but it's about asking the right questions from that stage.

A good example of this is one of our own pharmaceutical clients. They operate a very iterative based approach to integration planning, pre-close, centring everything on a risk and assumptions log. This gives them a view of all of the unknowns that crop up as they start thinking about their acquisition strategy and then go into identifying targets and looking at them.

They also get the right people around the table pre-deal who are most likely to be knowledgeable around and impacted by integration. In other words, not just corporate finance and strategy, but also HR, supply chain, IT and operations.

They then run their target assessment and due diligence process in time-boxed iterations, essentially working out what they don't know or what their assumptions are. They use due diligence to test those assumptions then get everyone around the table to refine thinking around the operating model and outlined integration plan. They then revert and investigate further.

In this way, it becomes clear that the deal is either obviously wrong or looks more likely to happen than not. If the deal looks likely, then they've already got an outline plan and an outline operating model from which they can not only start planning but also proceed into the traditional legal and financial due diligence negotiations.

How can you prepare management teams (your own as well as those in your newly-acquired business) to deliver value through integration?

We see some things that don't often get picked up, which cause people problems. The first is to look at this from an individual as opposed to a group perspective.

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Fundamentally, managers are people who have the same fears and uncertainty as the rest of the business, and so they need to be treated as individuals as they go through this, especially the middle managers who are really responsible for delivering integration.

There is a lot of value in, for example, understanding the context in which a manager is doing his job. The classic case is the excellent manager of an acquired firm who suddenly stops performing, because the context in which she is working has changed. This person either has either just come into a large amount of money because he's just been bought, or she's now in a different environment, with different responsibilities with different prospects. You need to understand the context or the environment in which people are working, and how that will change their level of engagement and motivation post acquisition.

The other simple thing to consider is what actually is engaging your managers - or what's likely to engage them in the new business (or in the integration)? It's rarely (just) the money but rather about the other potential things around status, responsibility, location, prospects, etc.

As far as a process of how you prepare management, we see a lot of success in companies that take a collaborative approach to setting the vision, building the business model and planning for integration, rather than just giving it to the back office. There are ways you can do this that really build their engagement into what happens, and prepare them for what's coming. It also stress tests them, giving you a clear view on who is up for it and who isn't.

Then there are some practical things. This may be the most stressful thing they go through in a career, so give them coaching through the process if they need it. Buddy them up, either with people from the acquiring firm, or with people who were acquired two years previously.

This is not so much about preparing them beforehand, but helping them through the process. One of the biggest problems here is the sheer workload for some of these people. Ensure that they've got the physical ability to do this without burning out, and that they've got the right kind of practical training needed.

What advice would you give on preparing for cultural integration? Who has done this really well?

There are two different kinds of success in cultural integration.

There is the 'traditional' way with Phillips as an example with a fairly rigorous process for cultural assessment. They look at it not just through surveys, but through reviews of artefacts, and they walk the halls, etc. They run focus groups to ensure they know their own culture as well as that of the target and have a rigorous process that understands the differences (the bit that often gets missed), ultimately deciding on a case-by-case basis how to change the business model so that the desired culture between the two is encouraged.

Of course, that is predominantly through measures, but you can also encourage it through how you change your organisational structure, and what you do in your processes, and so on.

Then there is another (arguably even more successful) way, often applied by organisations like Google, Xstrata and IBM. They essentially stress test every individual as quickly as possible, and either they adapt fast or they leave.

These organisations are very clear in saying "this is our culture and you are coming into our business". IBM actually calls it "blue washing". It seems brutal, but it works for them - they do it by being really sharp and clear on what it is they want, and then they just let people make the choice.

The other general point is to do something pre-close. It's not an exact science, but there are ways of assessing culture well before you get to the deal itself. There is actually a great deal that you can get even just from publicly available information - even if you're in a competitive or a hostile situation.

Don't just understand the differences, aim to understand what their real impact is - both on the long-term business and on integration. If there are clear differences across the two top teams, and those are around comfort with change, with the pace of change, and with the level of risk, then you're likely to find it hard to get that top team to agree on the speed of the integration and how much of it should be perfect – perfect, but long in delivery versus quick and dirty, but risky.

So, identifying those and getting them on the table quickly is 70-80 per cent of the issue. Also, don't get lost in the survey and, before you pick any kind of assessment tool, be clear on what your intention is in terms of what you're going to do with the results.

What is M&A success and how should you measure it? How do you manage board/investor expectations up-front to ensure that 'success' is measured and achieved in the long-term?

Managers are people with the same fears as the rest of the business... they need to be treated as individuals

There is no one way that we've ever seen by which integration success ever gets measured. Measurement actually depends on how your business measures any kind of success. And this makes it especially interesting if you're doing deals in distinctly different cultures. In Tata-Corus, for example, there was a very distinct difference between one side that was looking for success in terms of EBITDA uplift, better cash positions and stronger capabilities, and the other group that was looking for success in terms of building a single culture, where all the people were performing at their best, and felt fulfilled in their roles.

So, you need to define it within your acquisition strategy and stick to it. However, it must be measured in a way that can work for the long-term - and that's where things like EBITDA become notoriously difficult.

We tend to try to help people define success, two, three, or even four levels below that, which starts to give leading indicators as to whether the integration is successful. We normally find that you end up with a mix of hard and soft measures - and that is perfectly acceptable. Just because you can't put it on a spreadsheet doesn't mean it's not true. In fact, the more I see spreadsheets, the less I believe them.

So, you often end up with a kind of three-horizon view to integration, or to acquisition metrics. Especially in the early stages, you will measure good tactical project indicators: are you meeting milestones? Are your project costs in line? And so on...

Then there is the business performance element, which is about retaining the value and ensuring your operating costs aren't going up (which they often do during the process), your customer satisfaction numbers are where they should be, etc. These operational indicators are about making sure the business keeps running.

Then, beyond that, you can start looking at deal indicators. We always recommend a mix of financial performance and a level of increased sales in particular areas, or specific reductions in operating costs, etc. I have never seen a way of categorically showing a way to link acquisition success to share price.

If you're really looking to measure acquisition success in the long-term, in my experience it depends on one thing more than anything else: the attention span of the board post close.

What are the key skills required for an Integration Director? What are the pro's and con's of having an internal v external hire?

If you can have someone do this internally you should. I think the issue is more about the role though - then you can determine where they come from. People often get tripped up thinking the Integration Director is responsible for delivering the benefits of the deal. We've never really seen that work.

It's the business' responsibility to deliver your uplift in sales, your reduction in procurement costs, or whatever it might be. If you pull that away from your new head of sales, or new head of supply chain, then you end up in trouble. The role of an integration team needs to focus around facilitating the process of integrating.

The integration team should work alongside the top team, ensuring work streams are run effectively, with the right kind of tools and the right kind of governance, that logjams are identified and resolved, and that dependencies are managed.

An illustration I use is that, if you are determining the business model for your sales department, that's for the sales director to do. An integration team can help ensure that design is done at the right time, with the right information, that the implications on other departments are understood, and different options are offered, etc, but it is not his/her role to run sales.

As to whether the role is internal or external, if you've got someone you could pull out of the business who has the right kind of (both hard and soft) skills, then why not. I am often asked where in the business such a person should come from. However, it is not so much about whether they come from IT or HR, but more about their profile and the softer skills they possess. Integration has projects within it, but it is not in and of itself just a project - there's a huge amount of ambiguity, and you need to build relationships to make it work.

So the role is for someone with the ability to generate strong relationships quickly with people they don't know. They should have broad commercial and operational awareness, be comfortable in their function, have a high EQ, and be able to engineer success through other people, as opposed to delivering it themselves.

What are the biggest pitfalls to watch out for in terms of integration?

First, you need to make sure you have a vision. You must pay attention to the people issues, and you need to make sure you are very strong in your communications, and understand culture, etc. Being a little more specific, though, we tend to see four things:

> *I have never seen an acquisition succeed where senior management, or even middle management have not been supportive*

1. **Unrealistic expectations going in.** Integrations that fail, not because the management aren't performing to the best of their ability, but because, in due diligence, or in the business case, some wrong assumptions were made about market projections, or the degree to which new cross-selling opportunities would come into place. I've seen whole management teams fired because what started out as a normal integration turned into a struggling integration, which then turned into a turnaround.

   This was not because anything was fundamentally wrong with the business or the integration, but just that the expectations were set too high upfront. These can be avoided by going back to the idea of modelling.

2. **Over complication.** This often comes when you don't build your integration plan specifically to target those acquisition benefits. This may seem obvious, but we often see well-developed acquisition business cases, which focus on three or four key objectives around specific improvements in the integrated business or in this big area of integration.

   But, when it comes to the integration programme, there is a disconnect with the pre-deal thinking. It is basically designed to crash every department together, put every IT system onto one platform, harmonise every policy and procedure across the business, and do it all within a year. In reality, 70-80 per cent of this is probably not directly going to deliver, and it's going to distract you from those 3-4 key acquisition objectives set out at the start.

3. **Sufficient structure and dedicated resources post close.** Especially with smaller businesses, they will genuinely, with the best of intentions, think they can get this job done on Tuesdays and Thursdays, in the afternoon, alongside their day job. This just can't be done.

   There are very few integration programmes of any size that won't require at least one individual dedicated to ensuring the right structure is in place, for visibility and tracking events and milestones, etc.

4. **Unsupportive leadership.** If you haven't got your leaders onboard, either with the long-term business strategy, or with the specific objectives of the integration or the deal, or their own roles in the business, it will undermine everything else. I have never seen an acquisition succeed where senior management, or even middle management have not been supportive.

Carlos Keener
Founding Partner
Beyond the Deal

Carlos provides M&A integration strategy, planning and execution support to clients worldwide. He also advises businesses on corporate and acquisition strategy; operating model design; and turnaround of poorly performing acquisitions.

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