BTD
BEYOND THE DEAL

Handle with Care

Some traditional M&A best practices can cause more harm than good.

In less experienced acquirers, we see a different challenge: Those who follow what they believe to be M&A and integration best practices – but do so in a way that destroys business value.

Over the last decade, my team and I have seen real progress in the evolution of best practices for acquisition and integration. Across most areas, corporate organisations – and the advisers who support them – appear at last to be converging on what *really* makes M&A work: The right combination of connected, well-governed process; people with real experience applied to the task; and behaviours that support accountability, focus, and objectivity. That's encouraging, but application remains patchy: While between 80% and 95% of senior executives believe the use of a number of specific M&A and integration best practices has a major impact on long-term deal success, fewer than 45% consistently follow them.[1]

In less experienced acquirers, we see a different challenge: Those who *follow* what they believe to be generic M&A and integration best practices – but do so in a way that reduces the likelihood of deal success. We find ourselves regularly engaging in conversations that start with, "But everyone knows we should…", to which we reply, "Yes, perhaps in principle, but…" As with so much else in this field, context and experience count more than standard process and conventional wisdom.

My team and I came together to identify, unravel, and explore a number of these so-called best practices: when they work, when they don't, and how they can be applied more thoughtfully to support, rather than damage, an acquisition or integration. We've seen each and every one of these practices backfire when misapplied, and continue working with our clients to find better ways to handle them. Sometimes the best option is to ignore them entirely. Like any hazardous tool or activity around the house, the key is to think first about their purpose, application, and unintended consequences; and ensure you understand how to apply them safely before a trip to the emergency room becomes necessary:

1. **"Our shareholders want accelerated growth, but M&A is risky. We minimise this risk by choosing organic routes to the same goals whenever we can."**
   Agreed – M&A is a risky path to growth, but that doesn't mean that organic growth is always easier or less risky. In many cases M&A represents the *only* realistic way to achieve specific

[1] *Inconvenient Truths: Leadership behaviours that stop M&A from working*; Beyond the Deal, 2014

objectives, for example when looking to enter into a new, unfamiliar market or build a different capability within the business. Investment Cases should certainly compare any potential deal with alternative uses of the capital, but only if those alternatives are realistically assessed in terms of their ability to achieve your *strategic* goals.

Alternatives for JV or strategic partnership should also be evaluated as these can sometimes achieve the same as M&A at reduced risk, albeit usually more slowly. The ‘do nothing’ option should also be considered and quantified alongside your investment alternatives – in declining, disruptive or highly-competitive markets, this approach can highlight that ‘slow but steady’ organic growth is indeed the riskiest option of them all!

Every acquisition must ultimately be judged on three criteria: Does it support our strategic goals? Will it provide a sufficient return on the investment? Will we be able to make it achieve both post-close?

We continue to be surprised at how often one or more of these is not genuinely considered in deal-making.

2. **“We need to keep our pre-deal process quick and small to ensure agility and confidentiality.”**
Which is ultimately more important: keeping the deal secret, or ensuring you do the right deal? Both of course! Clearly agility and confidentiality are critical, but so is objectivity, rigour and *breadth* of assessment to ensure that the acquisition is a good strategic fit, and that the deal objectives can be realised post-close. This can only be done if senior people – especially those accountable for delivering benefits post-close – are involved in almost every step of the pre-close journey. Assign a project manager to co-ordinate the pre-deal process, manage the flow of information between teams, control the pace, and connect the thinking between acquisition rationale, target assessment and integration planning.

3. **“We’re not going to get distracted by qualitative or soft benefits; we’re staying firmly focussed on the numbers.”**
Regardless of the sophistication of synergy and valuation models, all of them are based on a foundation of assumptions: assumptions driven by historical data, market projections, and a hefty dose of gut feel. Dressing them up in twelve-tabbed spreadsheets only makes things more dangerous as executives confuse sophistication and data granularity with accuracy – we often find an inverse relationship between the two.

Of course data is important, but every acquisition must ultimately be judged (not just calculated) on three criteria: *Does it support our strategic goals? Will it provide a sufficient return* *on the investment? Will we be able to make it achieve both post-close?* We continue to be surprised at how often one or more of these is not genuinely considered in deal-making. An equal consideration of all three will encourage a proper look at those elusive 'deal killers' such as cultural alignment, leadership engagement, and readiness for change, all of which should be assessed as part of any deal.

How much you spend on integration and improvement is not a directly related to deal size; in many cases the lower the deal price, the more will need to be invested post-close.

Instead, it should be based on three factors: How much added value you expect to achieve as a result of the investment, when this value needs to be delivered, and at what risk.

4. **"We make people personally accountable for getting the deal done."**
Good thinking, excellent practice. But as the saying goes, "bad measures promote bad behaviour". Is your M&A team being motivated to do the deal, or make the deal work for the long-term? In our 2013 research, 36% of executives and board members surveyed believed that their M&A teams usually viewed getting the deal done as more important than what happens afterwards.[1] Even where this isn't formally the case, there can be an unspoken expectation that the M&A team is 'there to do deals'. Make sure the objectives and incentives driving your M&A team – formal and informal – *personally* motivate them to say 'no' as well as 'yes' (and ideally 'no' far more frequently), and that they keep everyone focused on long-term value. Manage executive and Board expectations also so that deal success is defined by long-term performance, not deal completion.

5. **"We play to our strengths within our organisation: Corporate M&A does the deal, then it's handed to the BU to integrate it."**
One of the most common organisational arrangements across corporate groups is also in our view one of the most dangerous. Unless proactively addressed, this division of responsibilities usually results in an 'accountability disconnect' in which corporate M&A groups – despite the best of conscious intentions – come to see doing deals as the primary objective, leaving value generation post-close to become 'someone else's problem'. On the other side of the artificial divide that emerges, business unit leaders accountable for the entity post-close can find themselves unable to influence the deal decision up-front, unaware of deal objectives or other vital information revealed during due diligence, and conveniently disengaged from ultimate success or failure; "They should never have done this deal, now I'm stuck with it – not my fault if it fails!". Regardless of how responsibilities are split between corporate and divisions, give

personal accountability to both groups for ultimate delivery of deal benefits; involve both sides in the end-to-end process; and reward both for long-term success.

While every deal differs, experience suggests that a poorly-executed integration typically erodes about 25% of the benefits promised in a three-year acquisition investment case, and creates unnecessary disruption to the business.

How much is it worth investing to protect, if not enhance, this return?

6. **"It's a small deal; we shouldn't be spending lots of money on integration."**
   Constraining your integration investment to reflect a (typically depressed) deal price is the same as refusing to spend what's needed to maintain or improve a second-hand car: The cheaper the car, the more you're likely to need to spend to fix and maintain it, unless of course you're happy for it to sit idle in your drive. Like any other capital investment, how much you spend on post-close needs instead to be based on three factors only: *How much added value* you expect to achieve as a result of the investment, *when* this value needs to be delivered, and at *what risk*.

   The second mistake stems from an inherent under-appreciation of the impact a successful (or struggling) integration can have on projected deal benefits and ongoing operations. In a typical acquisition, even a three-month delay in achieving typical synergies equates to a 10% - 15% reduction in business case benefits. While data is scarce and every deal differs, our experience across over 50 deals suggests that a poorly-executed integration typically erodes about 25% of the benefits promised in a three-year acquisition investment case, and creates unnecessary disruption to the business. How much is it worth investing to protect, if not enhance, this return?

7. **"Quality and consistency of the M&A process is critical, so we insist on a standard set of processes and templates for every deal."**
   Tempting as it may be, successful acquisition and integration is not achieved solely through the use of standard processes, tools and templates. Success ultimately comes to those who remain focused on *what* needs to be achieved (acquisition objectives), while retaining a flexible approach to *how* it's to be achieved. Each deal is usually different, and things change during integration: business conditions, leadership engagement, new learnings about the acquired entity and more, so insisting on an inflexible methodology and enforcing too much structure can make people lose sight of the real challenges and opportunities at hand – a successful operation in which the patient dies

anyway. Keep the use of specific tools and templates optional, and instead focus on consistent application of a rigorous approach and core guiding principles.

8. **"Day 1 sets expectations, so it's important for us to begin by reassuring everyone that nothing will change. This helps people stay focussed on business as usual."**
…except that things almost certainly will change, and everyone is expecting it to! Unless you really mean it (in which case why did you buy the business?), painting picture that everything will remain stable is probably the best way to lose credibility. Much better to be up-front and candid that things will change, even if not immediately. Speaking plainly about your intention to learn and plan first before confirming any changes builds confidence and demonstrates your intention to think before acting; but give everyone a clear date for when planning will move to action.

View the post-deal integration phase as an opportunity for transformation, and look for opportunities to 'disintegrate' as well as integrate to generate value.

9. **"A primary source of synergies always exists through combining shared services across the merged entities – we'll target them first."**
'Synergies' come in all shapes and sizes. Many acquirers begin with an assumption that *benefits = integration*. This is not always the case, for example in situations where the acquired entity is already highly-performing as a stand-alone and perhaps needs nothing more than additional investment to increase capacity and market share. Another common scenario is one in which a small, agile and low-cost organisation suffers an *increase* in operating costs as it becomes burdened with the more sophisticated systems and processes of the parent, leading to reduced flexibility and increased headcount.

   Instead, view the post-deal integration phase as an opportunity for transformation, and look for ways to 'disintegrate' as well as integrate to generate value. Adjusting back-office service levels, and therefore cost-to-serve metrics, is an equally valid, and possibly easier to achieve, source of value for the deal.

10. **“We must be very careful when restructuring the acquired organisation. Measure twice (or three times), cut once. Remember, we’re dealing with people’s lives!”**
Integration is an activity in which the perfect is the enemy of the good, and where ‘fit for today’s purpose’ should be the paradigm. You will make mistakes when restructuring. Some good performers will be let go; some mediocre performers will remain. Learnings along the way will mean some early decisions may need to be adjusted or unwound later. The secret is to act in accordance with your guiding principles: speed, decisiveness, and respect for the individual. Adhere to your principles and provide people with clarity as soon as possible, being open to temporary solutions that can get the business back up and running within weeks or months rather than years. ‘Workable now’ is usually much better than ‘perfect later’.

Pre-close these leaders were very possibly part of the problem, so expecting them to become a key part of the solution is unrealistic.

Our experience tells us that in most cases where significant change is intended, the best option is to move the acquired leader up, sideways or out within days or weeks of closing.

11. **“We need to put in place attractive, aggressive retention plans to keep our best performing employees on Day 1.”**
The majority of good performers will be excited but also worried by the integration process. Money is rarely the prime motivator for high-potential individuals, so providing clarity regarding an individual’s *future role and career prospects* is the secret to resolving the uncertainty, engaging good performers, and letting them get back to delivering value for the new combined entity. Where retention bonuses are used, link them to delivery of integration goals, otherwise you’re incentivising someone to stick around, not to perform!

12. **“The acquired leader holds the keys to employee performance, customer relationships and inside knowledge. We’ll do everything we can to keep her in the business, at least for the first year.”**
Another extremely common situation: good intentions, but with plenty of unintended consequences. While acquired managers often do possess the advantages mentioned, they are also – especially if they are also previous owners – often the most resistant to change, slowing the very improvements needed to add value post-close. Even if formally relieved of their management responsibilities and given a ‘consulting’ role, acquired employees will habitually look to them to ratify decisions made by the new owners, and only act once they see their old leader react. Coffee-break rumours, speculation and misinterpretation will increase dramatically. And keep in mind: If

the acquired business was struggling or stalled pre-close, these leaders may very well have been part of the problem, so expecting them to become a key part of the solution is unrealistic. While perhaps counter-intuitive, our experience tells us that in most cases where significant change is intended, the best option is to move the acquired leader up, sideways or out, and in any case out of the building, *within days or weeks of closing*, giving some breathing space to his or her direct reports and allowing the rest of the team to move forward.

Look for opportunities to 'declare victory' early, and announce a return to business-as-usual.

13. **"We only communicate when we have something new and tangible to say. Otherwise, our target audience will quickly grow cynical."**
While there is no such thing as over-communication, a lack of communications only strengthens the negative rumour mill. The secret is to enable two-way dialogue through multiple channels: blogs, town hall meetings, brown-bag lunches etc. Move quickly and decisively through integration, but also keep talking and listening, and feed what you learn back into your future communication and integration plans.

14. **"We get HR to drive cultural alignment, communications and employee engagement – that's their job!"**
Your HR team may have approaches, tools and experience in these 'softer' areas, but that doesn't mean they're the right people to *lead* change. Just as during day-to-day business, line managers are there to lead, motivate and influence the behaviours of their teams, and this role is never more critical than during integration. Line managers need to be front-and-centre to deliver key communications, listen to their staff, support changes taking place through the business, and set the example in adjusting to new cultures. Other groups including HR can help ensure best practices around these areas are followed, and that key messages stay aligned, but need to do so in the background. Leaders lead, HR supports; make sure both are able and ready to do so.

15. **"Integration is a complex, challenging process, often taking 18-24 months to complete. We'll make sure to build and run an integration programme that will see it through to the very last milestone."**
Integration is indeed complex, and some streams of work (particularly large-scale IT projects) may not be completed within 12 months. That doesn't mean a formal integration programme is needed for all of it. Integration Management Offices (IMOs) are best placed to manage complexity between workstreams, providing visibility, managing dependencies, tracking benefits and risks, and supporting cross-functional aspects such as communications, change management, and cultural alignment. At some point – often earlier than people expect – the need for this 'glue' diminishes, even while individual workstreams continue to deliver significant change and benefit within their areas.

    Look for opportunities to 'declare victory' early, and announce a return to business-as-usual, building any outstanding items into functional objectives and/or other ongoing continuous improvement streams. 'Timebox' your efforts to define the combined operating model and integration/transition plan, and keep the formal integration programme as short as possible, winding down as and when the need for workstream support disappears…but ensure someone continues to measure delivery of deal goals.

UNCONVENTIONAL WISDOM: 14 BETTER PRACTICES FOR ACQUISITION & INTEGRATION

1. Shareholders want accelerated growth, but M&A is risky. Rigorously assess strategic fit, financial return and operational feasibility.
2. Keep your pre-deal process structured and inclusive to ensure speed and quality alongside agility and confidentiality. Manage it like a project.
3. M&A is ultimately about judgement and experience. Balance qualitative or soft benefits alongside the numbers. Insist on robust, high-quality assumptions.
4. Make people personally accountable for doing the right the deal, and making it work.
5. Break down the organisational barrier between pre- and post-close: *Everyone* must be responsible for long-term success.
6. Strive to minimise deal price; invest enough post-close to generate acceptable returns at acceptable risk.
7. Mandate core integration principles to ensure consistency and quality from one deal to the next.
8. Day 1 sets expectations: Being open, honest and detailed will help them stay focussed on business as usual.
9. Synergies can come from integration, disintegration, improvement or investment. Be open and flexible on how to achieve value.
10. Be respectful but quick when restructuring the acquired organisation. Accept solutions that are 'good enough for now' and be prepared to learn as you go.
11. Communicate early and often, and use quiet periods to listen, otherwise your target audience will quickly grow cynical.
12. Use career-based incentives alongside money to retain your best performing employees on Day 1. This may not include the acquired leader!
13. Get business leaders to drive cultural alignment, communications and employee engagement.
14. Integration is a complex, challenging process. Quick wins and stability are most important. Transition to business as usual as quickly as possible.

ABOUT THE AUTHORS

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