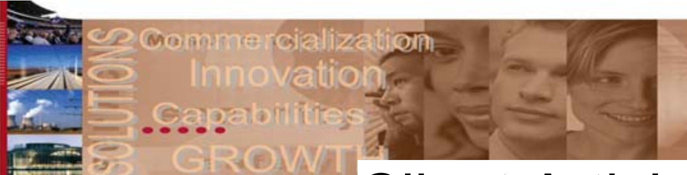

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Client Article

Mergers and acquisitions are becoming more critical — and more perilous — than ever. You can build your capabilities, even in the midst of turmoil.

The credit collapse and economic crisis of 2008–09 may have reduced the number of merger and acquisition deals in the short run, but it has increased the importance of M&A capabilities going forward. Industries are consolidating and restructuring with increasing speed — sometimes by choice, and sometimes by government fiat. Companies with available cash are pursuing an increasing array of acquisition opportunities presented to them as the crisis unfolds. Just in the pharmaceutical industry, in the first three months of 2009 alone, Roche bid US$40 billion for Genentech, Pfizer agreed to buy Wyeth for $68 billion, and Merck said it would acquire Schering-Plough for $41 billion.

At the same time, the pressure to avoid failure, in deal making and execution, has never been so high. Years ago, a company might have had more time to fine-tune the details, or a chance to recover if its M&A initiatives went sour. Today, the margin for error is much reduced. Capital is more expensive, the time granted by investors to produce results is shorter, and there is less slack in the balance sheet to recover from missteps. If the post-merger integration falters, then analysts grow sceptical, shareholders look for the exits, employees become restless, regulators and prosecutors get curious, and competitors pounce.

The stages of M&A should be pursued parallel (with substantial overlap and continuous referencing back and forth), managed by a single large team whose members communicate easily and regularly with one another and with the rest of the organization. This type of process places great demands on resources, time, and staff. But the results are worth the added effort. This is a good time to bring in experienced interim people.

To understand this approach, consider how the process works for more experienced M&A leaders during the four basic stages of any merger or acquisition.

Stage 1: An Enhanced Pre-deal Business Case

An effective M&A process begins before any deal is considered setting out a road map for future growth. This road map is not just a traditional long-term strategic plan, but rather a detailed set of proposed milestones toward the strategic goals of the company integrating mergers and acquisitions, organic growth investments, and alliances. It provides a foundation for understanding the kinds of deals that a company should pursue, and establishes a "sanity check" to make sure there is a compelling business case for all proposed deals. With that road map in hand, the M&A team can make an objective assessment of a deal's prospects and provides a thorough analysis of the prospects a combined company can realize. This might mean answering questions such as:

- How accurate is our perception of the business environment? What are we assuming about regulators, customers, and competitors?
- How might those assumptions, often developed from our first impressions, differ from reality? (For instance, will the merger invite new competitors?)
- What makes us believe that the combined company can succeed any better than the parts would on their own? Is an acquisition the only way to capture these synergies?
- What capabilities does the acquired company bring, and where are there gaps that could threaten the new company's success?
- Can we successfully integrate the operations? What will the talent attrition rate be? Do we have the financial resources that the combined company will need?

If a transaction aligns with the broader growth road map, it may be worth more than its stand-alone value. If it doesn't fit, or if the warning signals are too daunting, an experienced acquisitions team should be prepared to pull out of the deal.

Stage 2: Strategic Due Diligence

A traditional due diligence exercise, defined narrowly, is intended to validate, verify, and “stress test” the financial and legal aspects of the business case. But as business cases become more robust, due diligence should become more comprehensive. *Strategic* due diligence seeks to answer two questions: First, is it reasonable to conclude that the deal will produce an enduring, attractive economic return? Second, can we validate that the participating companies have the skills necessary to deliver on that promise?

To answer those questions, the team must assess such issues as the combined leadership talent, the likely responses of potential competitors, and the risk of technological or cultural incompatibilities between the two companies.

Stage 3: Plotting the Post-merger Integration

In a well-designed planning process, the integration team articulates what each function, business, and geography should look like after the merger, and what each team should do to bring the plan to life:

Translating the strategic intent into integration guidance. In the new, post-merger company, the important functions, geographies, and lines of business will have questions.

Building external stakeholder enthusiasm. Often the ability to succeed in the long term is shaped by the response from outside. Important constituents include customers, franchisees, supply chain partners, regulators, schools and other talent markets, local communities, municipal governments, and alliance partners.

Energizing the teams. The best M&A practitioners build detailed programs for organizational and cultural change that are tied to specific integration initiatives.

Stabilizing operations. During the first crucial weeks of a merger, planners need to detect problems before they grow intractable.

Designing “one company.” A good plan for a positive “one company” outcome describes the necessary changes in organizational structures, systems, and processes. It sets forth specific milestones and identifies who will be responsible for each element of the plan.

Capturing near-term value and positioning for upsides. There is enormous pressure to demonstrate clear progress during the first year or two of a merger. The key to managing that pressure is to enable a balanced pace of short-term synergy: fast and fierce enough to keep the faith of stakeholders by demonstrating tangible results, but not so aggressive as to sap the new organization of morale, talent, and energy.

Stage 4: Executing Successful Integrations

By the time a company reaches this point; it has considered a wide range of scenarios and has created alternative plans to manage them. However, for the promises of the deal to bear fruit, the company must convert plans into reality. This is the work of the final stage: staying the course after the excitement of the deal has subsided.

The most significant risk to a well-designed implementation plan is drift. In a business world that increasingly values decentralization and the empowerment of line managers, keeping a complex, interdependent implementation on course can be a challenge. It requires adherence to the outline of the plan, yet also requires that managers be granted the flexibility needed to adapt to changing circumstances.

Post-merger governance demands a team with the authority to manage and enforce plan execution and to oversee plan variations. That team may be the executive or management committee, or it may be a separate, dedicated integration oversight team. In either case, the team needs to have had some continuity through all four stages, so that it now has an innate sense of the newly merged company's needs. Avoid the common error of handing off governance responsibility to managers who were not substantively involved in planning — or if you must make them responsible, then at least provide an oversight safety net.

Clarity in strategic intent, especially in the beginning, provides a touchstone that carries all the way into this final stage.

Capabilities and Momentum

The companies that master the capabilities of successful M&A and build their teams accordingly are the most likely to succeed in the uncertain, hyperactive M&A environment of the coming years. When an M&A team is skilled and capable, a certain momentum takes hold. The systems and processes, management, and lines of business start acting in alignment. Physical locations shut down as planned; some people are reassigned, others are promoted; business partners are chosen; IT systems are linked or eliminated; incentive structures are combined; and cultures are harmonized.

In the end, the two companies become one. The process of the acquisition is completed, and the new company turns its attention, once again, to the prospects of growth.

Deshel can help provide the interim support that a company requires at all stages of the merger or acquisition.

Many suggestions detailed above can be used during Alliances and Joint Ventures.

Contact Alan Latham +61 415 296 960