



M&A Strategies for the 21st Century

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M&A blog: <http://strategyscape.typepad.com/and/>

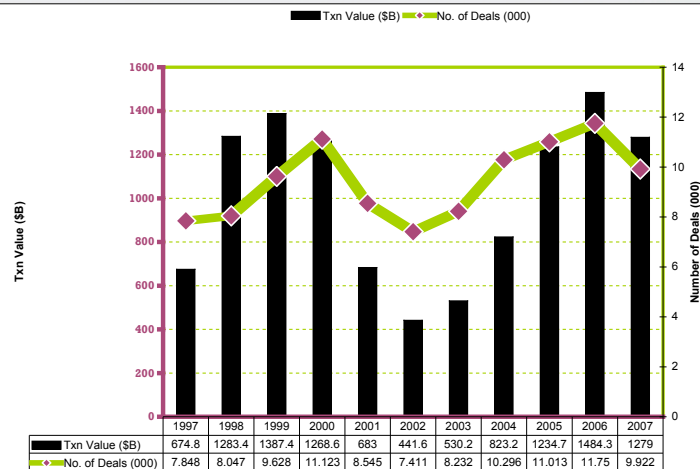


Outline

- Introduction
- The 21st Century M&A environment
- M&A: The challenges
- 7 principles for successful M&A
- An M&A process model
- Illustrative best practices
- Conclusion

The 21st Century M&A environment

M&A: A Historical Look (US)



Understanding M&A cycles

- 1895-1904
- 1922-1929
- 1940-1947
- 1960's
- 1980's
- 1990's
- 2004-2007

8% of overall stock market value per annum, on average.

M&A volume historically 10-42% of annual investment in Plant, Property & Equipment.

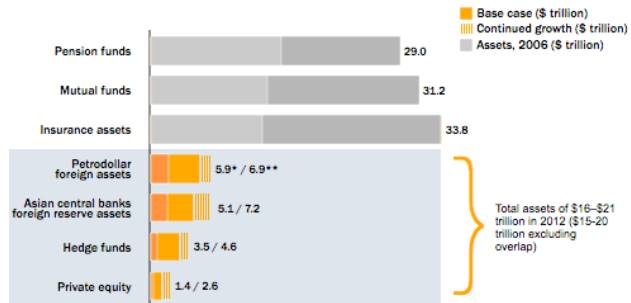
The Future of Global M&A...

- Financial Depth
 - Global financial stock now 316% annual world GDP
- New players: Petrodollar investors (SWF), Asian Central Banks, hedge funds and private equity
 - BRIC acquirers in Triad
- Commodity industries' renaissance
 - Need for super-scale to keep pace with globalizing markets
- Demographic factors

The Future of Global M&A

NEW POWER BROKERS COULD HAVE UP TO \$21 TRILLION BY 2012

Assets under management, 2012E



*At oil price of \$50 per barrel. If oil prices fell to \$30 per barrel, petrodollar foreign assets would grow to \$4.8 trillion in 2012.

**At oil price of \$70 per barrel.

Source: Hedge Fund Research; Venture Economics; PE Analyst; IFSL estimates; Hennessee Group data; MGI Cross-Border Claims Database; McKinsey Global Institute analysis

Graphics Source: McKinsey Global Institute

M&A: The challenge



Compaq Stumbles (1999)

- “Compaq is having difficulty integrating DEC, which it bought last year, with its other operations. Costs seem to have got out of control, partly because the DEC deal was about buying people more than about buying technology. Lots of sackings in the early days of integration would have had the talent packing its bags...The DEC deal also dramatizes Compaq’s dilemma about what exactly it is.” *The Economist*, 4/17/99
- “Other near-term problems [include] the difficulty of integrating Digital Equipment into Compaq.” *The New York Times*, 4/19/99



Compaq Stumbles (1999) ...

- Many observers believe that Compaq’s subsequent acquisition by HP stemmed from Compaq’s difficulties in integrating Digital.
- “Compaq is like a snake that swallowed a rabbit,” says Nick Earle, chief marketing officer for HP’s enterprise computing unit. “You go to sleep for a long time when you do that.” (1999)
- M&A Integration as key challenge



The M&A Failure Syndrome

- 50-75% of M&A never provide the benefits they promised, or take too long to produce them [Various sources]
 - Only 37% of M&A considered successful by management
- Past failures traceable to
 - Lack of homework
 - Unrelated diversification
- Proposition:
 - Current failures largely due to poor M&A integration



After the Deal is Done

- Companies are paying more attention to M&A integration as a strategic priority
 - More than just deal-making
- Managing integration
 - Strategic: Does the deal fit with your strategy?
 - Organizational: Can the two organizations work well together?
 - “Plug and play” versus “Plug and pray”

7 principles for successful M&A

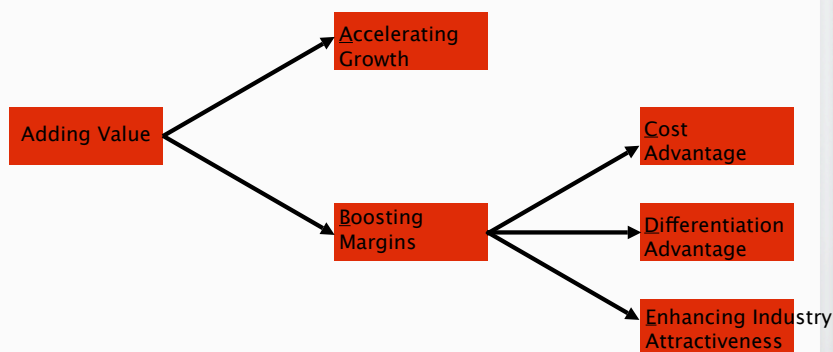
Principles for M&A Success

- M&A can only be successful if the deal is founded on the bedrock of a sound corporate strategy
- Consider all options thoroughly before committing to the deal; once committed, implement rapidly and in a disciplined manner.
- Due diligence needs to be about more than financial issues
- Organizational integration needs to reflect the strategy drivers behind the deal
- M&A managers need to manage seven sets of stakeholder expectations well
- The integration needs to be tightly executed, using the best resources available
- Managers need to think carefully about whether, and what, they are learning from each deal

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Why do M&A?



- + Forestalling Risks
- + Generating knowledge/ innovation

Adapted from Pankaj Ghemawat (2002), "Mergers: A prescriptive perspective," presentation made at the FTC Roundtable on M&A, December 9, 2002.



What Capabilities are Required?

- Required M&A capabilities vary with type of M&A
 - Reduce overcapacity (e.g., Chemical Bank merges with Chase)
 - Roll up a fragmented industry (e.g., BancOne in the 1980s)
 - Product or market extension (e.g., Quaker buys Snapple)
 - Use M&A as R&D (e.g., Microsoft buys Vermeer)
 - Build a new industry (e.g., AOL buys Time Warner)
 - Investor buyout (e.g., investor group buys Aladdin Resort & Casino)

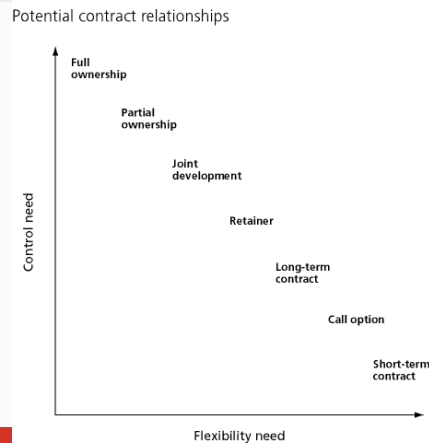
Adapted from Joseph L. Bower (2002), "A managerial perspective on M&A," presentation made at the FTC Roundtable on M&A, December 9, 2002.



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M&A as Part of a Menu of Corporate Strategy Choices



Source: James Brian Quinn (1995), "Make versus buy: Strategic outsourcing," *McKinsey Quarterly* 1995(1): 48-70.
Graphic source: http://premium.mckinseyquarterly.com/article_page.aspx?ar=74&L2=1&L3=24, accessed March 2002.

Principles for M&A Success

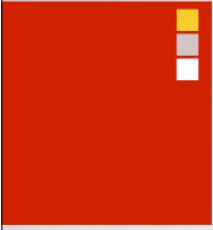
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Why Due Diligence?

- “Caveat Emptor”
 - Know what you are buying
- Validate ability to realize sources of value
- Identify “unacceptable risks” or “showstoppers” early
- Establish positive relationship with target
- Acquire early warning of sustaining resources that may be needed later in the integration effort

Adapted from Martin Todd Dorris (2001), “EHS due diligence overview for mergers & acquisitions,” presentation at Semiconductor Safety Association 2001 Annual Symposium, April 11, 2001; and Laurie A. Lehmberg (2001), “ESH due diligence in mergers & acquisitions,” presentation at Semiconductor Safety Association 2001 Annual Symposium, April 11, 2001.



Key Action Outcomes from Due Diligence

- Properly value (or revalue) transaction
- Shift or insure against risks by contract or other mechanism
- Restructure (or abandon) transaction

Adapted from Lehmberg (2001), *ibid.*



“Nontraditional Components” in Due Diligence

- Integration risks
 - Can we blend the companies as needed?
 - Level of integration required for synergies?
 - Our capability to get it done? Their capability to get it done?
 - Historical or other barriers to getting it done?
 - Cultural risks
 - Human capital risks

Adapted from Galpin & Herndon (2000), *ibid.*



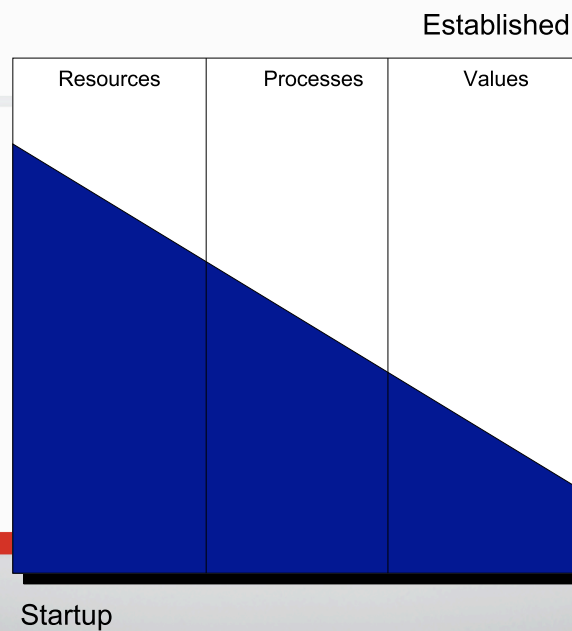
Due Diligence Challenges

- Time limitations
- Staffing limitations
- Need to maintain secrecy
- Target’s confidentiality needs
- What happens to shared information if the deal eventually falls through?
 - Competitive information
 - People involved
 - “Clean rooms” and “Neat rooms”

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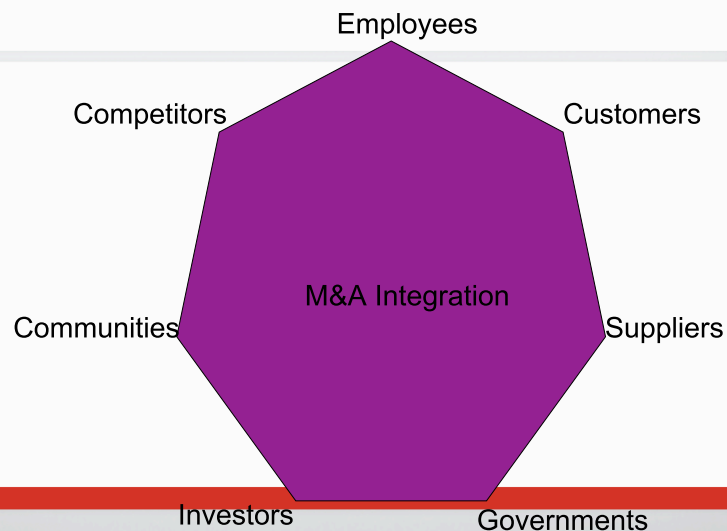
R-P-V Model in M&A



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Stakeholders in M&A Integration





Re-Recruitment

- Why re-recruit?
 - Loss of key talent
 - Increased openness to other opportunities
 - Decreased productivity
 - Decreased quality
 - Increased recruitment and training costs
 - Loss of organizational knowledge
 - Sullen survivors (poor morale)
- 4 simple steps to re-recruitment
 - Identify key people
 - Understand what motivates them
 - Develop plan to address retention
 - Personalized solutions
 - Execute plan to address retention
- Address the “me issues” quickly

Adapted from The L Group, 2003



Incentives

- Financial incentives should not be the only tool to ensure retention
- Some guidelines
 - Not just retention, but sustained value creation
 - Create high-stakes, attention-getting income opportunities
 - Simple and straight-forward plans
 - Sponsorship by the highest level management
- Some interesting findings from high-tech mergers
 - Financial incentives not significant predictor of retention
 - Key factors
 - Target firm autonomy
 - Target managers’ status
 - Acquirer’s commitment to target

Source: Spratt & Feldman, 1991

Source: Ranft & Lord, 2000



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Need to Track Integration Success

- “Until now, our executive team had a ‘don’t ask, don’t tell’ policy surrounding mergers. I don’t ask when the next deal is going to be, and they don’t ask me how this one is going.” (Vice president in charge of merger integration)

Integration Metrics

- Integration measures
- Operational measures
- Process and cultural measures
- Financial measures

Source: Galpin & Herndon, 2000, *ibid.*

Measuring Integration Performance

- Strategic
 - Market share
 - New product development
 - Product portfolio
- Operating
 - Employee retention
 - Headcount reduction
 - Employee satisfaction
 - Management selection
 - Customer retention
 - IT systems integration
- Economic
 - Share price
 - Revenue
 - Net income
 - Operating income
 - EVA
 - Sales expense ratio
 - Cost savings

Source: S. Gates & P. Very (2003), "Measuring performance during M&A integration." Long Range Planning.



M&AI as Program Management

- “Acquisition integration project management is project management at its fullest, most complex and challenging. The nature of this type of project requires that this work be done repeatedly, often by a different mix of team members at different stages of the project.”

Source: Vester (2002), p. 36



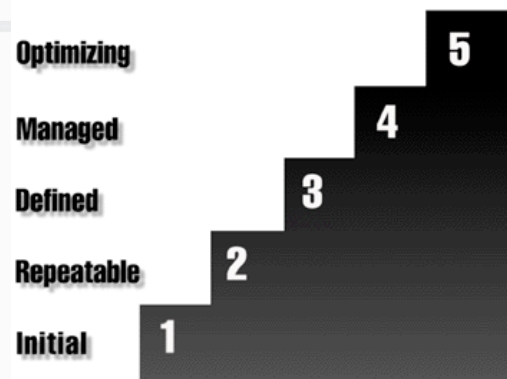
Integration Roles

- Executive team
 - Oversight, strategic direction, impasse resolution, investment decisions
- Core team
 - Daily coordination of integration
- Task forces
 - Integration design of operational and functional areas
 - 4-6 members per task force
 - Co-leaders per task force, preferably one from each company

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Capability Maturity Model



Source: <http://www.sei.cmu.edu/cmm/cmm.html>, accessed June 19, 2003



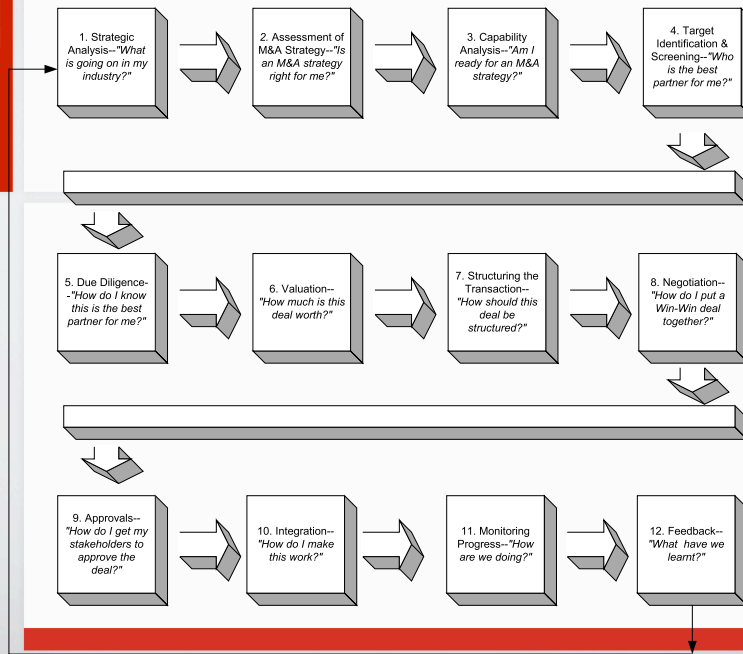
Institutionalizing Merger Success

- Full-time position
- Career track
- Permanent teams
- Process documentation
- Process monitoring
- Continuous improvement
- “Lessons Learned” process
 - Complex learning, tacit knowledge, cannot document everything



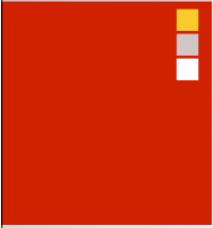
An M&A process model

The M&A Strategy Cycle



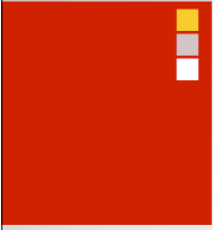
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Illustrative best practices



Successful Integration: Illustrative Guidelines

- Critical time window: 1 year
- The 100-day milestone
- Process must be swiftly executed, objective, and effectively communicated
- Use the opportunity to upgrade resources
- Tailor pace and degree of integration to strategic context
- Include integration executives in the negotiation team
- Create a permanent M&A integration team where feasible



Successful Integration: Key Process Steps

- Don't do the deal if you can't find the leader
- Offer big retention incentives to top-level executives
- Restore stability ASAP
- Assign a high-caliber, respected senior manager to manage the integration full-time
- Target a few quick wins
- Make decisions faster, not slower



Successful Integration: Mistakes to Avoid

- Too much democracy
 - Trying to please everyone
- Poor skills
 - Reinventing the wheel
- Conflicting processes
 - Allowing divergent initiatives
- Lack of facts
- Inadequate resources
 - Using-part time players



Conclusion



Key Takeaways

- We should expect to see significant M&A activity continue on a global basis
- Successful M&A has two imperatives
 - Integrate deal with firm strategy
 - Integrate target firm in an appropriate manner
- The 7 core principles of managing M&A strategically

- **Further resources**

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