Capturing deal value

Successful deals are made, not born*

*connectedthinking

M&A has a huge impact on employees in both the organisations involved. It is all too easy to overlook the human element when there is so much else to be done.

Introduction

Asset prices have soared over the past few years and, with the re-pricing of risk, financing costs are rising rapidly. Maximising the value that can be captured from mergers and acquisitions (M&A) is thus becoming more important than ever. Yet it is well known that seven out of every 10 deals fail to generate the shareholder value they were expected to provide – and this is true in ‘up’ as well as in ‘down’ markets. It is not the marketplace, but management, that determines the success of M&A.

In fact, most business leaders understand what is required to make a deal succeed. However, practising what the text books preach is much more difficult – just as it is far harder to ski down a mountain than it is to read about how to execute the perfect descent. In our *CEO Survey 2007* cultural issues topped the list of obstacles the M&A encountered or anticipated by CEOs. And it was more experienced acquirers who were most likely (47%) to cite cultural issues and conflicts as a major obstacle.

Four features help to explain the gulf between theory and practice. First, M&A massively increase management’s normal workload. In addition to doing their ‘day jobs’, senior executives must spend time planning, negotiating and closing the deal, and supervising the post-acquisition integration. This is the equivalent of holding down several full-time posts.

Second, the timeframe in which it is possible to make positive changes is very short. The 100 days after closing a deal are particularly significant, because it is then that people are most open to new ways of thinking and working. So it is essential to set the right course within the first three months; otherwise, attitudes will harden like concrete that sets before it has been poured.

Third, M&A has a huge impact on employees in both the organisations involved; and politicking and uncertainty can erode much of the value on which a particular deal was based. But it is all too easy to overlook the human element when there is so much else to be done.

Lastly, one of the main attributes for attaining seniority is experience, but many managers have no prior experience of doing deals. Few companies engage in M&A more than once in every five or six years, and even those which regularly perform such transactions rarely maintain centres of excellence or have local expertise. So the know-how on which managers can usually call is frequently lacking at the very point at which they are under most pressure.

- Acquisitions/mergers require successful post-deal integration to capture the value of the deal.
- Deals put enormous pressure on managers who are often inexperienced in the particular environment.
- The people factors are just as critical as the project management challenge.
- Acquirers often look for help too late, after much of the value has disappeared.

Faced with challenges they have never previously had to address, many business leaders understandably focus on getting things done rather than managing the emotional undercurrents. Yet ‘soft’ factors are as important as ‘hard’ factors in determining the outcome of M&A. We have carried out research to identify the attitudes and kinds of behaviour that are typical during each stage of a deal. We have also assessed the impact of such attitudes and behaviour on the execution of the strategy (see sidebar, **Research methodology**).

Our research shows that:

- The most successful deals are those in which the leaders identify with the outcome on a personal and organisational level. Their personal goals – be these money, career progression, status or anything else – are consistent with the corporate rationale for the deal. They also identify with the new entity rather than with their original organisations.
- Three personal attributes are critical in managing deals: the ability to empathise with others; the ability to balance attention to the task at hand with attention to people; and consistently ‘fair’ decision-making.
- Cultural issues can have a major bearing on the outcome of a deal – and these vary from one country to another. Communal relationships dominate in South America and Asia, for example, while exchange or transactional relationships are more common in North America and Europe. This has implications for cross-border M&As.

This paper examines at how these ideas manifest themselves at each stage of the deal. We shall cover the key traits required to lead each phase successfully, the danger signs that may indicate an executive is behaving subversively and the sort of actions that can be taken to change such behaviour.

Research methodology

Our research was carried out between June and October 2007. It was based on 20 interviews with senior decision-makers who had participated in both successful and unsuccessful deals (measured by changes in shareholder value), over the past 10 years. Respondents represented companies based in North and South America, Western and Eastern Europe, and Australasia.

‘Soft’ factors are as important as ‘hard’ factors in determining the outcome of M&A.

EXPERTS
ONLY

Planning the deal

At the outset, strategic considerations are paramount. The would-be purchaser must identify suitable acquisition targets, review the deal potential and assemble a leadership team. At this stage, focus is typically concentrated on ‘hard’ factors like the strategic rationale, financial value, potential synergies, the initial integration plan and initial views on organisational design for the combined business and top-level management. The softer, people issues can easily be ignored or postponed, however unwisely, to a later stage in the process.

Key leadership factors

The planning stage focuses on creating the circumstances for a successful deal. So the key leadership factors include:

- **Leadership recruitment:** In addition to leaders known for ‘getting the job done’, successful deal teams include people-oriented leaders who are sensitive to issues of morale and uncertainty, can effectively communicate with employees in both organisations, are fair in their dealings and are personally committed to making the transaction succeed. The deal team should also include people who can provide continuity during the post-deal integration process.

- **Culture and leadership research:** The assessment of acquisition targets should go beyond quantifiable value drivers to include ways in which the organisations might complement each other in other areas, particularly leadership style and culture – both corporate and geographic. Evaluating the potential benefits of a target’s cultural differences might well require an entirely different set of measures of value.

- **Trust building:** Reaching out to a target company is like the first steps in a courtship, laying the groundwork for productive negotiations and enduring success. It is crucial that a ‘people person’ makes these overtures.

Danger signs

Even at this early stage, however, some leaders may behave in a way that is not consistent with securing the best outcome. They may, for example, talk about the ‘chances’ of the deal working – a sign that they have not personally invested in making it succeed. Alternatively, they may dismiss or disregard issues of corporate culture and values.

Example:

The leader of an investment company saw it as his role to make deals. He did not identify personally with the progress of the deal and relied on luck rather than planning or anticipating issues that might arise. While the deal was deemed a financial success, he acknowledges that the positive financial markets at the time played a significant role.

Changing behaviour

Intervening at this early stage of the deal can have a lasting effect. But a simple word of advice to a leader whose short-term focus is undermining the longer-term stability of the deal will rarely be enough, particularly if he has a record of bringing deals to the table. It is usually necessary to intervene more actively:

- **Coaching:** Deals require a different mindset and a different orientation from those required for day-to-day activities. Training may help executives who are not dedicated deal leaders to adjust. Sometimes, a few sessions with an executive coach, focusing on communication techniques and inter-personal sensitivity, may be all that is needed.

- **Sequestering and/or partnering:** Sometimes, a more significant intervention may be called for. It goes without saying that a leader with weak people skills should not be lead negotiator on implementation issues. He or she can be assigned tasks requiring less contact with others, or teamed with a leader who relates well to others, creating synergies from their respective strengths.

- **Extending the appointment:** Assigning people exclusively to pre-deal activities tends to foster a short-term focus. Leaders whose responsibilities extend to the post-deal integration process are generally less myopic.
- **Adjusting the remuneration package:** Aligning the remuneration of leaders with long-term objectives like increasing shareholder value rather than short-term goals like getting the papers signed will help to ensure that they maintain the right focus – although financial incentives alone are no guarantee that they will personally identify with the outcome of the deal.

Knowing what interventions to make to address behavioural issues is not the same as actually making them, though. So it is also important to ensure that the deal team includes someone whose responsibility is to make sure that the attitudes and behaviour of the leaders are completely aligned with the imperatives for achieving a successful deal. A third-party advisor can be invaluable in viewing behavioural dynamics objectively and intervening to put things right.

Even at this early stage, however, some leaders may behave in a way that is not consistent with securing the best outcome.

Doing the deal

Once the deal is actually underway, three activities dominate: the structuring of the transaction, completion of due diligence and closure of the deal. As the negotiations intensify, strong 'people' skills and the personal commitment of those at the top also become increasingly important.

Tax, accounting and financing considerations play a major role in determining the best structure for a deal. Due diligence covers a broad spectrum of business issues, such as operations, IT and human resources, as well as financial performance. It also includes a reassessment of the basic strategic arguments for the deal – the key business drivers and potential synergies – and a review of management's projections. During the close, activity centres around reviewing and finalising the purchase price, contract and transaction structure and finally, signing the papers.

At this point, the leaders have to conduct a careful balancing act. They have to juggle strategic and tactical challenges, maintain the stability of the business while planning the integration process and combine confrontation with collaboration.

Key leadership factors

The key factors here include:

- **Establishing a strategic vision:** Once the target has been identified and evaluated, the leaders have to envisage what the combined organisation will look like. This is not just a matter of integrating 'us' and 'them', but of creating an entirely new entity. The process of formulating a vision is also a catalyst for leaders to identify personally with the deal.

Example:

Recognising that the sale of the company for which he worked would give it access to new resources and knowledge, one senior executive endorsed the deal from the outset. He also welcomed the opportunity to be associated with the purchaser's major global brand. His understanding of, and identification with, the strategic objectives of the deal enabled him to support the bidder's requirements.

- **Developing the tactical plan:** The focus is on achieving the 'ideal state' of synergy while maintaining a 'steady state' for business continuity. Leaders must also balance the need to be flexible and collaborative with the need to execute quickly. It is essential to establish robust measures for assessing progress on both fronts, so that the organisation can make quick course corrections as needed. Each area of due diligence provides opportunities to address both short- and long-term objectives. The demands on the IT infrastructure during the first 100 days must, for example, be balanced with the need to integrate different IT systems and train staff.

- **Maintaining trust during negotiations:** The negotiating process reveals many facets of leadership style, from how leaders communicate to how they gain consensus. The ability to work collaboratively while engaging in the inevitable confrontations involved in reaching the right terms is fundamental to building and sustaining trust.

Example:

Two Latin American family firms led by major public figures were eager to merge as a way of ensuring their future and the financial security of the families that owned them. Both leaders also wanted to maintain their own reputations and public roles, and were transparent about these personal goals. Both were therefore keen to promote harmony and realise the full benefits of the deal. Representatives from the smaller company, for example, were given a greater level of representation on the board of the new entity than their size warranted, so that they would not feel that the other side had too much power.

Danger signs

When a leader is not fully committed to the deal, he or she will lack the confidence to map out a coherent strategic vision. If he or she is unable or unwilling to do this, it will be virtually impossible to develop a sensible tactical plan. Such behaviour may have a profound impact on negotiations with the target company. Unwillingness to negotiate, infrequent or misleading communications, and the inability to see the deal through the eyes of the other company all undermine the trust necessary both to close the deal and to set the stage for successful post-deal integration. Much can be learned about people's mindsets from the language they use; watch out for talk of 'us and them' and military analogies.

Example:

When a French company bid for a smaller American target, one of the senior U.S. executives strongly resisted the move. Rather than trying to understand the would-be buyer's perspective and values, he dismissed it as an 'old-school' firm with a bureaucratic style ill-suited to the entrepreneurial spirit that he believed characterised his own organisation. His hostile attitude alienated the people with whom he was negotiating to such an extent that the deal failed.

Changing behaviour

At this stage of the deal, the scope of activities broadens to encompass the target company. The steps required to keep the deal on course must likewise expand, since the behaviour and attitudes of the executives heading the deal are no longer the main determinant of its outcome. Everyone involved in the transaction must pull together to realise a common vision. Two elements are critical:

- **Bringing both sides to the table – early and often:** Cultural conflicts are known to be a major challenge to successful deal-making, so it is crucial to incorporate the cultural identities of both organisations. Leaders from both companies must contribute to this process, since mutual understanding and buy-in are vital to set expectations accurately and minimise the risks arising from the massive changes that take place after a deal has been signed.

Example:

When the leader of an acquiring company said, 'We are an elephant and you are a gazelle, but you will be able to stay that way', he was both acknowledging the cultural differences and creating the pre-conditions that enabled the target company to accept necessary changes.

- **Stimulating the right sort of behaviour:** It is equally important to create situations that promote the sort of attitudes and behaviour the leaders want – such as establishing a reporting structure that requires reporting to both organisations. This encourages staff to identify with the deal, and also helps to reduce uncertainty, to set appropriate expectations, and to forestall gossip and rumour. Face-to-face communications by the leaders of the acquiring company at the offices of the target company are particularly productive in building valuable relationships.

Example:

Recognising the more relationship-oriented culture of a Mexican target company, a self-confessed 'accounting nerd' at the American acquirer made a point of travelling to Mexico for face-to-face meetings that could easily have been handled by telephone. The ensuing camaraderie and trust contributed to a seamless integration process. He later encouraged his U.S. staff to learn Spanish and his Mexican staff to learn English so that communication became a vital weapon for the business rather than a cause of misunderstanding.

As the deal progresses to the point at which the papers can be signed, it is also essential to ensure that those who will be responsible for integrating the two companies are fully abreast of the details. Many companies use one team to negotiate the terms of the deal, and a second to carry out the post-integration process. But if the people in the second team do not know why the strategy has been formulated as it has or what the dynamics of the negotiations have been, they cannot communicate very clearly or lead the process with a full understanding of the rationale. Continuity is essential; and post-deal leaders from both organisations should therefore be included in formulating the strategic vision and implementation plans. A simple hand-off from the boardroom negotiators to the post-deal team will not suffice.

Integrating the deal

The final phase, managing the post-acquisition process is primarily about execution. This phase focuses on creating the new normality, realising the most important synergies, like the integration of systems and operations, and reducing costs. Management must move very fast in this phase to protect the core business from internal distractions and external predators. However, the first 100 days are only the first stage in a post-acquisition period that will stretch over many months.

Key leadership factors

It is essential to maintain the strategic vision for the deal as the integration plan is implemented, so the key concerns here are:

- **Constant, comprehensive and appropriate communications:** This is not just a question of addressing uncertainties, setting accurate expectations, empathising with employees dealing with major change and providing reassuring feedback. People do not buy in to words alone; they follow leaders. So the post-deal integration leaders need to be able to mobilise the leaders in the next layer down the organisational hierarchy to give direction to people at both organisations.

- **Balancing consistency with flexibility:** They also need to stay true to the strategic vision and plans they established before closing the deal, and thus demonstrate their continuing commitment to managers and employees at both organisations. At the same time, however, they must have the agility to respond to practical considerations that arise unexpectedly and make the necessary course corrections.

Danger signs

The urgency accompanying the first 100 days can throw some leaders off track and undermine the broad perspective that is needed. They may find it difficult to set priorities, and concentrate on tasks at the expense of people and relationships. Alternatively, they may fail to identify personally with the new organisation. They may, for example, continue referring to the old entity as if the deal had never taken place or talk in terms of 'us and them'.

Example:

One respondent never saw himself as an employee of the new organisation that he was assigned to lead. He held on to his identity as part of the mother company, seeing his role simply as 'ambassador of the rules'. He did not accept that part of his role was to communicate the unique values of the new organisation to the mother company and incorporate them into the new entity.

Changing behaviour

The post-acquisition period is the time in which management must work hardest to preserve the continuity of the business while realising the synergies from the deal, and balance the need to get things done with awareness of the emotional impact on employees. The appropriate attitudes and behaviour should all be entrenched by this point, but the stresses of those first 100 days can be tremendous.

It is vital to put the right people and structures in place both to stabilise the target company and to secure its value. It is equally important to balance the effort to integrate the two entities with the maintenance of business as usual, and reward people accordingly. Given these challenges, it may be necessary to take additional steps to keep the post-deal integration on track:

- **'Integrating' the leaders:** To ensure that a leader does not fall back on his pre-deal identity once the deal closes, he should be embedded in the target company's offices. This will serve several purposes. It will ensure that communications are more direct and more interactive; enable staff at the target company to judge whether the leader's actions match his words; and enable the leader to assess whether they are responding as he wants. It will also provide the leader with more opportunities to show that he understands the target company's concerns, and allow him to assess whether a different culture is helping or hindering the integration effort.

Example:

One leader moved from the bidder to the target company in an effort to get to know the other company's culture. He made a conscious effort to be part of the target company, such that staff there saw him as one of their own. As a result, they were much more willing to work with him on implementing new processes, even though some of them knew that they would be made redundant in the new entity.

- **Monitor the metrics:** During the post-deal integration process, everyone from the top to the bottom of the new entity needs to behave consistently. It is therefore essential to establish clear, tangible objectives which balance the short- and long-term needs of the organisation and distinguish between pre-deal and post-deal goals. So, for example, a company which normally places great emphasis on product innovation may not regard innovation as its top priority during the integration process.

Similarly, it is crucial to develop key performance measures for assessing employees' progress in meeting the organisation's objectives and reward them correctly. Rigorous attention to the task at hand and attention to softer issues should both be recognised. With the right metrics, it is also possible to assess whether fatigue, frustration, alienation and other such emotions are reducing productivity.

Many deal-makers think it is the final stages of the process that make or break a deal, and it is certainly true that the opportunities for creating value are greater during the post-acquisition integration than they are at any previous point. But the attitudes, behaviour and planning that are engrained in the early stages of the process are what lay the foundation for those first 100 days – and thus, ultimately, for whether the deal itself is deemed a success. Any company that ignores the 'soft' elements at the start of the process has already doomed itself to failure. For, by the time it has summoned help, much of the value it could have captured will have vanished into thin air.

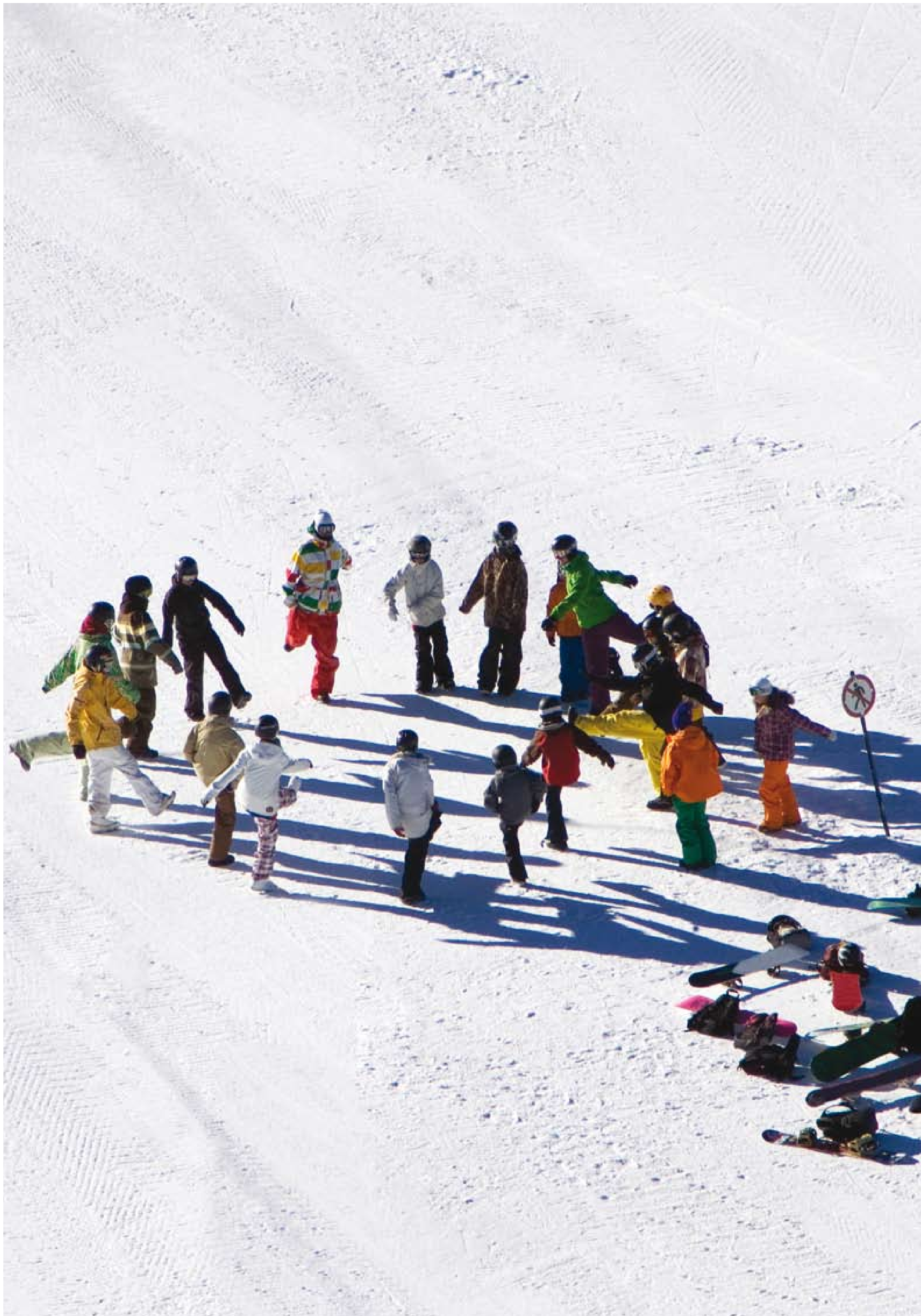
The attitudes, behaviour and planning that are engrained in the early stages of the process are what lay the foundation for those first 100 days – and thus, ultimately, for whether the deal itself is deemed a success.

Capturing deal value

70% of deals still fail to realise the value they are expected to generate, due to weak acquisition strategies or poor implementation. Our experience shows that acquisitions rarely fail due to flawed strategy, rather failure is most often a result of not executing the strategy in a timely fashion. While underlying synergies are typically the catalyst for a transaction, success in the long-term requires strategic planning and investment before, during, and after the ink is dry.

Our deals experts can help you plan, negotiate, complete and implement deals all over the world, and allow management to operate the business at peak levels while we help you integrate your systems, technologies and people.

Success in the long-term requires strategic planning and investment before, during and after the ink is dry.



Our Global Capturing deal value network

Increasingly, value is created across a connected network of partners, suppliers, customers, regulators and stakeholders and success depends on collaboration among them. This means most business issues can no longer be resolved within your own four walls. The best solutions must both capture opportunities and navigate risk across an extended business network.

PricewaterhouseCoopers' Advisory team can help you to execute your business strategy. We advise and we implement – locally and globally. We help organisations capture opportunities, navigate risk and deliver lasting change across business networks.

Our deals experts focus across the deal continuum from strategy through execution to post deal integration and operational consulting to capture the maximum value from mergers, acquisitions and divestitures. We offer a full range of consulting, tax, financial and business assurance services. We're also able to call on extensive industry expertise and knowledge of local markets anywhere and everywhere your company operates.

We help our clients to:

- Find the best targets, and analyse their strengths and weaknesses.
- Identify synergies and potential opportunities for improvement.
- Negotiate the best terms based on deep understanding of value drivers.
- Structure the deal, including the tax perspective, to recognise greater value .
- Access the capital markets and other sources of finance.
- Manage the post-deal integration process – particularly the first 100 days, when it is essential to stabilise the new acquisition and stop any 'value leakages'.
- Carve out non-core assets and sell them for as much as possible; and
- Improve long-term performance by further consolidation, reducing cost, streamlining organisational structures, and simplifying processes.

We take the time to listen and have the courage to debate different points of view – based on independent and challenging insights, supported by facts and industry benchmarks. We give you the confidence to succeed in a connected world.

For more information please visit www.pwc.com/deals

Andrew Miskin
Global Capturing
Deal Value leader
+44 (0) 20 7804 6583

UK
John Dowty
+44 (0) 20 7804 9548

US
Greg Nahass
+1 (213) 356 6245

Europe
Ralf Schlaepfer
+41 (58) 792 1620

Asia Pacific
Chao Choon Ong
+65 6236 3018

Australia
Peter Mastos
+61 (3) 8603 2194

Canada
Ajay Chadha
+1 (416) 814 5788

Steve Rimmer
Human Resources Services
Deals leader
+1 (646) 471 8860

UK
Jeffery Rowney
+44 (0) 20 7212 4453

US
Steve Rimmer
+1 (646) 471 8860

Europe
Andrew Kruseman Aretz
+31 (0) 205686251

Colin McKay
Global Deals leader
+1 (646) 471 5183

UK
John Dwyer
+44 (0) 20 7213 1133

US
Mike Burwell
+1 (313) 394 3504

Europe
Philippe Degonzague
+33 (1) 56 57 10 92

Asia Pacific
Chao Choon Ong
+65 6236 3018

Middle East
Nitin Khanna
+971 (4) 304 3200

Central and Eastern Europe
Steven Berger
+7 (495) 967 6325

South America
Jorge Bacher
+54 (11) 4850 6814

Canada
Russell Goodman
+1 (514) 205 5064

References to PricewaterhouseCoopers Corporate Finance should be read as referring to the Corporate Finance team that is part of the Advisory line of service within PricewaterhouseCoopers LLP. The corporate finance services highlighted on this website are not available to US persons other than through our registered NASD Broker Dealer within the US, PricewaterhouseCoopers Corporate Advisory and Restructuring LLC, which can be contacted directly at pwcs@us.pwc.com. This restriction does not apply to Valuation services.

PricewaterhouseCoopers provides industry-focused assurance, tax, and advisory services to build public trust and enhance value for its clients and their stakeholders. More than 155,000 people in 153 countries across our network share their thinking, experience and solutions to develop fresh perspectives and practical advice.

© 2009 PricewaterhouseCoopers. All rights reserved. “PricewaterhouseCoopers” refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

Designed by studioec4 19709 (03/09)

pwc.com/deals