

Take the long view

The number of mergers and acquisitions taking place has fallen sharply as the economic downturn sets in, but there are signs that companies with cash are starting to hunt for bargains. M&A expert **Danny A Davis** tells Jim Banks how negotiating a good price is only the first step. Without planning ahead for integration, an acquisition could turn out to be a white elephant.

The severe pressure on the global economy has put the dampeners on mergers and acquisitions as companies find it hard to access the credit to fund their purchases. Nevertheless, the downturn creates tempting opportunities for growth through acquisition if a company has the cash to spend. More businesses are available at bargain prices, and now could be the time to consolidate ahead in preparation for the upturn in the world's economic fortunes.

As a result M&A is still happening, but there is a need to ensure not only that due diligence is thorough, but also that the purchaser knows as early as possible about potential problems with integrating a new business. Identifying good value in M&A is not straightforward, and it is not solely about price.

'M&A is still going on, but a lot of people are sitting on their hands. They don't want to be the one that bought a company at the wrong price, so some are holding back and

not acting yet. At the same time, however, some companies are being forced to sell off parts of their enterprise to raise cash,' says Danny A Davis, partner at DD Consulting.

'There are lots of opportunities and a lot of companies have money, though from the outside we don't know which companies they are. Valuation is tough in normal times, but is especially so when companies are out there looking for bargains. There may be problems inside a company that

due diligence will miss. You might find more problems than you had hoped for,' he adds.

Davis runs a consultancy, teaching companies about the processes and tools needed for the integration of merged businesses. The workshops help companies bring all business departments, IT and systems into a coherent, combined structure, and helps with strategic reviews of integration planning.

Although his company is relatively small, Davis has provided change programmes for some of the largest mergers in recent years, including a \$6 billion global deal. He also handled the European merger of BP and Castrol with 180 projects in 30 countries across the IT, HR, finance, sales and marketing, distribution, manufacturing, property and legal functions.

This experience gives him a ringside seat on the M&A market, and he has seen the benefits of considering integration at an early stage. Failure to do so paves the way for unpleasant shocks, of which there have been many.

'Some companies have said they will not do any more M&A, either because they do not have the cash or their strategy is influenced by greater caution. But, in some cases, that caution masks a desire to grow,' he adds.

Considering integration before the deal goes through helps to take out much of the uncertainty from any acquisition.

Make or break

Integration is Davis' specialist area, and he urges companies to bring this kind of expertise to bear on the planning before a deal is struck.

'Integration is generally a 100-day planning process followed by delivery. You need to plan as always, but you should do it as early pre-deal as possible. That way you get the integration and the synergies now rather than later. The quicker the better for all concerned, because if you are prepared for the integration process then you will create a stable business sooner,' he remarks.

Adding an extra element to pre-deal planning is not without cost, but it could save both time and money in the long run.

Planning costs money, the earlier you begin the planning process the less information you have, but the faster you can deliver your synergies, you can't start too soon. You certainly cannot leave it until too long after the deal. You must think about integration

before you buy a company. CFOs want to keep costs down and maximise the synergies of an acquisition, but they must find a balance,' Davis warns.

Examples of both success and failure abound in the history of M&A, and Davis believes that there is as much to learn from those enterprises that got it wrong as from those that got it right. He recounts the tale of one business that had formulated a 10-point integration plan that had still not been implemented six months after its had completed its acquisition, its inexperience in M&A causing it to be caught out by unanticipated problems that only surfaced post-merger.

'In the current environment, where companies are taking an opportunistic approach to acquisitions, there is a greater risk that they may not plan adequately, which can lead some deals to fail. Integration must be part of the pre-deal thinking, and it may sometimes lead companies to find that a deal is not viable. You need integration people involved in the due diligence process,' says Davis.

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'A good deal is one in which you get the right price, where a sound level of integration is possible and there is nothing toxic that will come as a surprise post-merger. Transparency, however, is difficult if only limited information is available at the pre-deal stage,' he adds. When it is impossible to get the full picture up front, then any purchasing company owes it to itself to be prepared for the unexpected, and its preparation for integration will be vital to this preparation.

'There are always surprises after an acquisition and they need to be dealt with quickly. They must be contained,' stresses Davis.

The fundamental question in any M&A activity is whether you are paying the right price for a company. This may not always be clear, but consolidation in sectors such as banking and retail is happening nonetheless.

'There may be bargains, but in the banking market there is a lot of uncertainty about

what unpleasant surprises might lay in wait. So, do you wait until the share price rises, suggesting greater certainty about the integrity of the business, or do you gamble? It's like buying a house. Do you buy it without a survey, or do you wait for the surveyor's report and risk a price increase?' asks Davis.

The integration equation

There is, of course, no cookie-cutter approach to integrating a new business.

'The process will depend on the nature of a business, but in general it seems that companies don't have a list of the issues they need to look at. The first thing they should do is look at the financial perspective. Then they should take control of the money in the business; get hold of the signatories so that no one can run off with the cash,' says Davis. 'Fiscal control must happen immediately.'

Successful integration means careful examination of the people, systems, data and processes that make up the finance

function, but this must also happen within the context of a review of the people and systems across the whole business. Finance is a priority, but cannot be approached in isolation.

'Finance needs to integrate itself and the rest of the company. Financial integration of HR, for instance, must happen early. You need to get the resources to integrate finance across the company and achieve the necessary change in process and culture,' Davis remarks.

The cultural element is a high priority, and a mismatch of corporate cultures can manifest in the most unexpected areas, with damaging results. Davis notes that even details as small as the design of expenses forms can cause rifts in a business, and he has seen such factors cause key people to leave a merged entity, particularly when a service company and a product company are brought together.

From the cultural differences at the top of the chain to down to the format of expenses forms, there are myriad issues a purchaser should try hard to foresee.

'There are always differences in culture and structure, and an acquisition is often a financial decision that ignores the issue of culture. But it affects every aspect of a business, from its systems and processes to how it deals with customers,' Davis remarks.

Even if the initial integration has been successful, Davis warns that the process should not necessarily stop there. A second wave of integration of the merged entity may offer further opportunities to better integration and, therefore, greater efficiency.

Davis recalls a huge global merger where he handled the integration of functions such as finance and HR, which revealed many synergies, but the merged entity continued the process, leading it to create a global finance function, replacing the country-by-country structures previously in place.

'That company didn't make the double-jump to a global finance infrastructure straight away. The second wave of cost cutting was made successful after the initial merger had settled down. At this stage, specific improvements can be split into shorter elements of planning,' he comments.

Further questions arise if the process of growth through acquisition is ongoing. The

complexity of multiple acquisitions has led some large companies to limit the number of acquisitions, but this fixes the possible rate of M&A growth and, therefore, overall growth. Davis believes that the right approach to integration can overcome this problem.

'Where a company is making a series of acquisitions, the pre-deal and post-deal elements must be brought together. If a company is doing integration after integration there may be blurring around the edges of each deal as different strategies compete, so a firm must be clear about whether it is making a one-off acquisition or a series,' he says.

'Linking pre- and post-deal phases and delivering them well can release growth opportunities and allow a company to be a more opportunistic buyer, which is very useful in the current market. You don't want your competitors to snaffle all the bargains.'

Different strategies for integration have emerged, and they differ greatly. GE, for example, needs relatively little integration – setting financial targets for its acquired companies to drive them in the right direction.

'CFOs are sometimes too busy to see all potential problems or are focused on short term targets and so they don't need look at the long-term consequences. CFOs – and the rest of the business – must see the full implications of any deal,' believes Davis.

Without a thorough and considered approach to integration even acquisitions with good potential can fail. Companies must not only look at how to get a deal through, but must also envisage what the merged business will be like post-deal. Never has this lesson been more relevant than now. ■

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Danny Davis

Danny A Davis is the youngest ever trustee director on the board of the Chartered Management Institute, also chairing the Marketing and Policy Committee. He is a guest speaker at a number of the world's top business schools on the strategy and M&A courses, and soon to publish his first book, *M&A Integration Success*.

