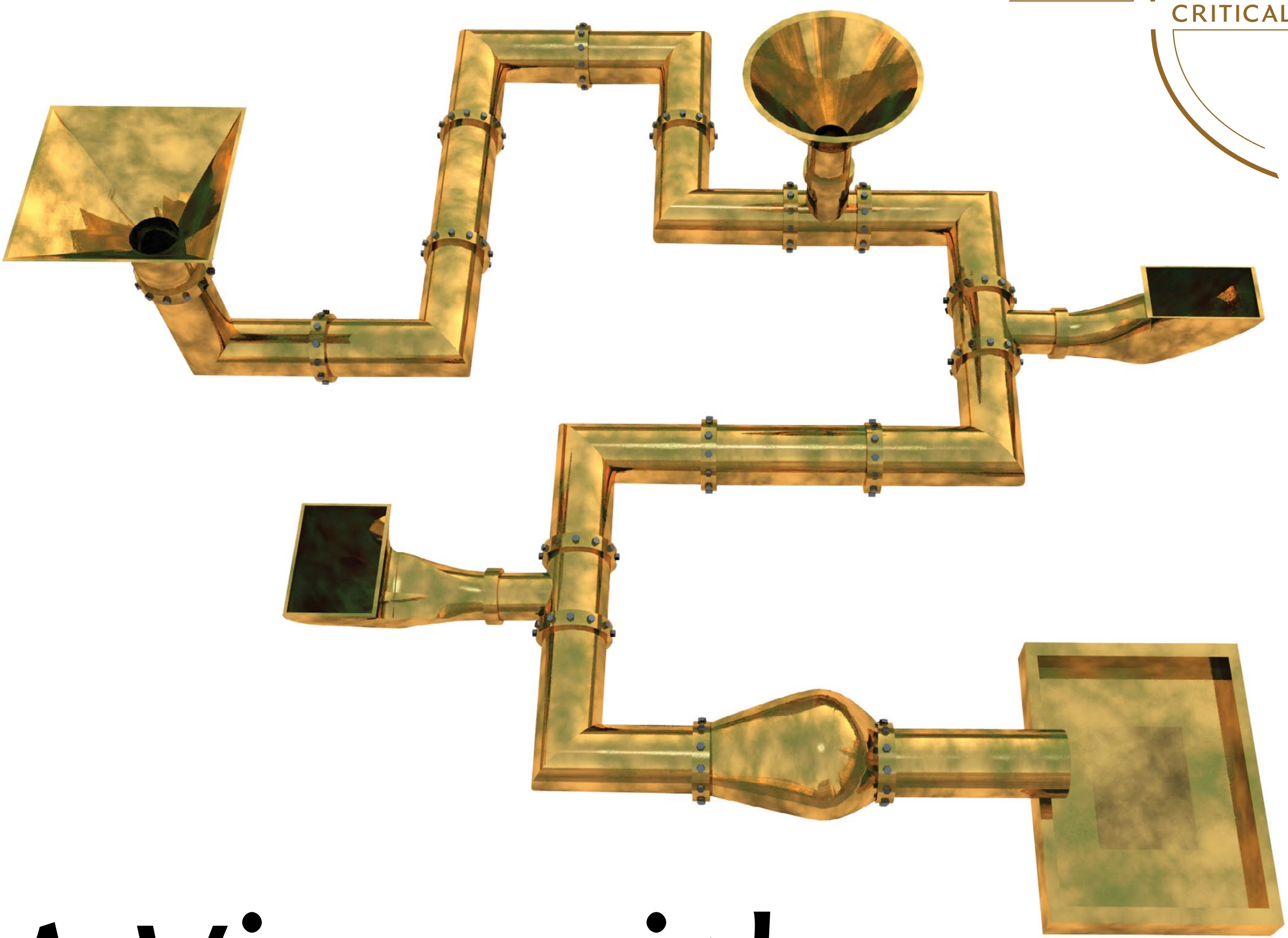

A View with Multiple Lenses

Developing & managing your acquisition pipeline

Like it or not, it is a fact that many acquisitions fail well before the deal even closes. Overestimated deal benefits, incomplete due diligence, insufficient scenario planning around future market conditions, or the planned departure of acquired management as part of handover are just a few of many examples in which the game is lost in the opening moves.

Drawing from an executive Discussion Group held in late 2010, this article by **Carlos Keener**, *provides experienced guidance on how effectively to manage the early stages of M&A from the development of an acquisition strategy to target identification and early-stage assessment.*

Managing an acquisition pipeline is about balancing speed and confidentiality with a need for information, analysis and strategic thinking. Challenges often include:

- How can we avoid delusionary synergy business cases, especially around revenue?
- How can you separate quality businesses heading for distress from those that are already damaged goods?
- What degree of proactive process is useful in identifying acquisition targets?
- How can you prevent competitors beating you to the deal?
- How can we minimise 'deal fever' as we approach the finishing line?
- What is the best role and value of external advisors in the process?

DEVELOPING A STRATEGY FOR ACQUISITION: KNOW WHAT YOU WANT AND HOW IT WILL SERVE THE BUSINESS

The acquisition process does not begin with the development of target criteria, but starts a few steps further back with the creation (or at least the confirmation and clarity) of your business' growth objectives, and the degree to which acquisition may play a part alongside other options (organic, joint venture, collaboration, etc). This growth strategy should directly support your overall plans for the business, typically addressing some of the 'later' horizons related to the creation of new or more competitive business propositions. Acquisition benefits are rarely delivered quickly, so are generally best when designed to address your longer-term objectives for growth and diversification. Make sure your acquisition strategy asks the following questions:

- What business targets should your acquisitions help you achieve, and by when?
- What would the combined business post-deal(s) need to look like to enable and support these goals? Are there multiple landing points envisaged? How far a stretch will this be from what you already do well?
- What specific pressures on your current business model would future acquisitions pose? What will need to change within your own business (people, processes, structures) to prepare for or address these challenges?
- Are there other ways to deliver your strategic goals outside of acquisition? How far could you get without doing a deal?
- How would this strategy change if market conditions shifted over the coming years? Under what conditions would acquisitions no longer make sense?

Your answers will provide a solid base from which to begin identifying and assessing targets, without the need at this stage for overly-detailed analysis. Without them, you risk a situation in which target assessment criteria (and associated filtering processes) are unclear or biased, disconnected to the wider business strategy, and more easily subject to deal pressure (in either direction) as momentum builds.

FINDING THE RIGHT ACQUISITION TARGETS: INSIGHT OR SERENDIPITY?

There is unfortunately no best practice method for finding the right acquisition targets, and the range of ways to source and approach potential vendors continues to include everything from informal discussions at trade shows to an exhaustive search and analysis of every firm in your target market. Despite this, common good practices do exist:

- Publicise key aspects of your acquisition strategy across the market, allowing targets to self-select and approach you, so reducing the search effort required from your side;
- Manage a number of identification and approach strategies in parallel – you never know which one will deliver the right deal, or when;
- Take the time to build relationships with potential target owners and managers, allowing each side to learn more from the other and signal intent early;
- Use newer technologies such as internet-published business auctions (increasingly common in China) to identify targets;
- Continue the search in good times and in bad – good deals can be found in both.

ACQUISITION TARGET ASSESSMENT: GOING BEYOND THE NUMBERS

One of the paradoxes of target assessment is that the amount of time, effort and management distraction involved is often the same regardless of deal size. Another is that – despite (or indeed because of) the intense focus put on financial assessment, business cases and valuation – the real factors that see acquisitions fail rarely have much to do with any business case. When in doubt, too many managers seek reassurance in deeper market or financial analyses, failing to understand that increasingly-detailed spreadsheets will never insure against (and often further obscure) key assumptions that underpin deal success; namely, those that relate to management, culture, strategy and other leadership issues. Those attending our Discussion Group were unanimous in their view that effective deal assessment requires more:

- Ensure a good strategic fit: Can you explain the deal rationale simply and concisely?
- Understand the true capability synergy the deal could bring: What do they do that's clever, or that can be combined with your own strengths to bring something new to your business and/or the market?
- Consider the best Operating Model for the combined business post-close: What changes will be necessary in both organisations, and how easy will it be to make them?
- Get serious about cultural alignment: Make this one of the first areas of assessment, not the last; and regardless of your process, keep it objective and comprehensive; As any experienced acquirer will tell you, "I can tell with people, and we get on really well" is not sufficient!
- Review leadership on both sides of the deal, and the new context in which they may operate: Post-close, will they have the capabilities and desire to engage

One of the paradoxes of target assessment is that the amount of time, effort and management distraction involved is often the same regardless of deal size with, and deliver, the new business? How compatible will they be with managers from the other side? Will their motivations and aspirations change as a result of the deal and the new Operating Model?

- Assess targets against likely integration assumptions and dependencies: An early definition of your integration priorities and plan will allow you use target assessment and due diligence to test its feasibility, better understand risks, and be three steps ahead of the game if the deal goes through.

MANAGING THE ACQUISITION PROCESS: STAYING MEASURED, OBJECTIVE AND BALANCED

The biggest challenges cited by those around the table at this event continued to be about managing the people who manage the deal. To minimise the drain on management attention while minimising the likelihood for deal team dynamics to determine the ultimate outcome, some additional structure applied to the end-to-end process can help:

- Keep a formal cap on total 'deal capacity', something that can be measured in both management time as well as cumulative deal values – How much can you really afford to take on? Only allow a new opportunity to enter the pipeline (especially in later stages), if you are prepared to take another opportunity off the table;
- Actively prioritise the 'high likelihood' deals as well as those posing the smallest risks to integration;
- Set clear accountabilities for post-deal integration and the subsequent business, and involve line management early in the acquisition process: Like the Roman builder traditionally made to stand underneath his newly-completed arch, are post-close managers prepared to accept responsibility for the business and any new targets they may inherit? This is especially important when a business unit proposes an acquisition to a corporate centre that will fund the deal; if the deal price were coming out of their own budget, would they still proceed? Turning your lens around, the engagement and support your leadership shows towards the deal, business structure and the new targets they will inherit will speak volumes about their real engagement and confidence in making it a success.
- Take steps to slow the pace as a deal approaches the finishing line: The more any deal is seen prematurely as inevitable, the higher the ultimate price of acquisition is likely to become;
- Do everything you can to defuse deal fever: Much of this comes down to unbalanced objectives and dynamics between a deal sponsor, his or her (typically subordinate) deal team, and any outside advisors incentivised to 'get the deal done'. To combat this, include a mix of people with different agendas and experiences within the deal team to help disperse any groupthink. (See sidebar on other ways to address this problem);
- Begin post-close Operating Model design and integration planning as early as possible, and continue feeding the results of this planning into your assessment and due diligence process to validate assumptions, test risks, and ensure your ability to integrate and sustain business performance and growth in the long-term.

MANAGING YOUR ACQUISITION PIPELINE – TOP TIPS

1. There is no magic, silver bullet: Your approach should depend on the business sector, strategy & circumstances;
2. Start with a real strategy supported by the management team;
3. Managing due diligence is critical – use it to actively test acquisition, Operating Model and integration assumptions, not just 'tick the boxes';
4. Use the widest range of skills and experience within your business to support target assessment and due diligence – what does it all mean?
5. Don't be too formal – keep the process flexible and responsive to new opportunities and situations;
6. Understand why the target is for sale;
7. Outsource the deal maker; keep other external advisers focused on data provision & analysis;
8. Include a 'constructive cynic' in the deal team;
9. Strategic and cultural fit is critical – put this at the top of your assessment criteria, not the financial business case! Assuming the business case will pass, would you still do the deal?
10. Design your post-close Operating Model and integration early; inject integration costs and risks into the mix to help avoid deal fever, improve your analysis of fit and value, and prepare early for Day 1.

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USING EXTERNAL RESOURCES: GENERATING DATA AND ANALYSIS, GIVING YOU TIME TO UNDERSTAND WHAT IT MEANS

A final topic of discussion revolved around the right role for external advisers. While it was generally accepted that outside resources can be a critical asset to the process and become a natural extension to your deal team, they must not, by design or default, assume responsibility for strategic thinking and decision-making on your behalf. Keeping this principle in mind, external groups are well-placed to identify new potential targets, conduct numerical data gathering and analysis; perform management and cultural assessments; develop and assess contracts, facilitate (but not deliver) Operating Model design and integration planning, and even help you navigate and co-ordinate the transaction process itself. Conversely, they should not become directly involved in determining your acquisition strategy, conducting technical due diligence, leading deal negotiations, or delivering integration – as the group that ultimately pays the price and reaps the benefit, these must all be owned by you. Experienced advisers can also inject objectivity and balance into the process, provided their experience of acquisition and integration is broad, and their fees are not contingent on deal completion.

Carlos Keener
Founding Partner
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Carlos provides M&A integration strategy, planning and execution support to clients worldwide. He also advises businesses on corporate and acquisition strategy; operating model design; and turnaround of poorly performing acquisitions. Before establishing Beyond the Deal, Carlos was a senior consultant at PricewaterhouseCoopers, and a senior manager within Accenture's Corporate Strategy and M&A practice.

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