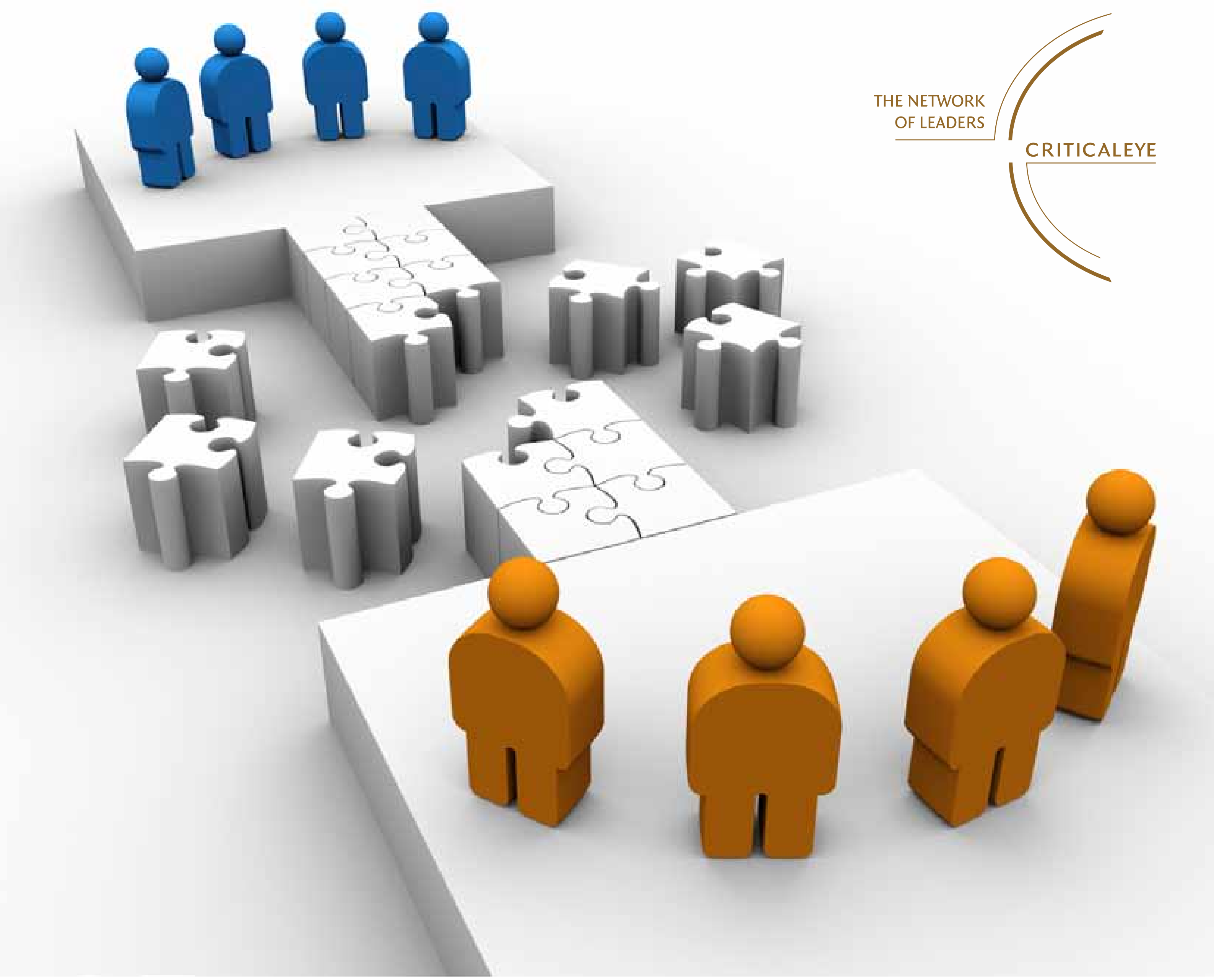

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A TIME TO BUY

Acquisitions may be the best way to expand in an environment of low economic growth. **Criticaleye** *speaks to business leaders to find out how to ensure that value is delivered when buying another company*

Caution reigns supreme in boardrooms when it comes to giving the green light to an acquisition. Once the good times do return, that 'go-slow' mentality will in all likelihood be replaced by aggressive strategies which are supposed to land with a bang but invariably end with an embarrassed whimper.

So what are the principles that the executive and non-executive members of a board need to stick by if corporate acquisitions are to deliver real advantages and returns for shareholders? **Don Elgie**, Founder and Chief Executive of PR and communications business, Creston plc, states: "There must be a strategic rationale, balanced with an accretive profit rationale. These must be laid down well in advance."

Roger Buckley, a Corporate Finance Partner at professional services firm BDO, agrees, noting that "you need a clear strategy for acquisitive growth and a clear view as to the criteria of the type of business you want to acquire".

In theory, that's straightforward enough. But the fact is that plenty of acquisitions that appeared like matches made in heaven have failed, and the days of gathering a war-chest to engage in ambitious buy-and-build strategies no longer creates excitement among investor and financial institutions. They want clarity and assurance, not entrepreneurial exuberance and bullishness.

REALITY BITES

John Allbrook, Executive Chairman of IT finance provider Syscap Ltd, comments: "You've got to have a strong, compelling strategic story supported by the shareholders,

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whether they are private or public. Certainly in this market, people are looking for a little bit more than just cost synergies; they're after a clean, clear strategy and one that makes sure people are not overpaying for the transaction."

In fact, the notion of proposed 'synergies' takes on a chimerical aspect in the dark art that is M&A. **Colin Mayer**, a Criticaleye Thought Leader and Professor of Management Studies at Said Business School, Oxford University, says: "There are systematic biases that people introduce when they value potential acquisitions. They look at a possible target and the synergies that can be made when acquiring a company without thinking about what might happen if those synergies fail to materialise."

Positive as opposed to wishful thinking needs to be carefully weighed-up, especially where the remuneration of the executive team is pegged to the overall market cap of the acquiring company. "Non-executives should be casting a very critical eye over any proposed acquisitions, particularly large ones. It's one of the most important roles they have to play," says Colin, adding that there is an interesting issue about why so many value decreasing acquisitions have gone through. "To what extent could it have been possible for non-executive directors to have provided a more [disciplined appraisal] of what the executive team were doing?"

VALUE FOR MONEY

Even if the strategy is sound, there is a strong suspicion at the moment that prices are too high. **Aleen Gulvanessian**, a Partner at law firm Eversheds, says: "Corporates are being a lot more thorough. They aren't prepared to take risks as much and are not as entrepreneurial as they once were – that's partly led by the fact that frequently they aren't being financed as well. Banks aren't lending without ensuring that thorough due diligence has been done. They want to understand that the assets being bought are valued appropriately."

Properly crossing the t's and dotting i's for the financial and legal due diligence may be a formality nowadays, but perhaps a tougher problem is to assess some of the more intangible qualities. John says that, for him, "it's as much about cultural due diligence and whether the two businesses will be able to exist side-by-side".

Don says: "We really go to town to learn the truth of the aspirations of the directors. You need to spend time with them and really dig down. I spend a lot of one-to-one time with directors understanding their motivation and ambitions and make my judgments based on the sincerity of their comments as to what their aspirations actually are."

If a transaction is to make the grade, then the first year after the target company has been taken over is key. **Siva Shankar**, Corporate Finance Director at SEGRO plc, a commercial property investment and development company, says that "most M&A failures happen in the 'integration' phase, generally due to unrealistic expectations being set up front".

In a competitive market, particularly during an auction for a business in a hot sector, the resolve of management teams and NEDs will be sorely tested. Colin says: "The first movers might make reasonable profits before the others realise there is an important area to make acquisitions. But the 'me too' companies that come in later are the ones who are really operating in a highly competitive environment where there is frenzied bidding going on."

Don takes the view that it's better to keep away from the crowd when eyeing-up a potential deal. "We've always tried to avoid the auction process as it can destroy shareholder value as there's a tendency to overpay. We don't do deals that aren't earnings enhancing immediately."

On one level, the principles for M&A are obvious. But it is pride and an element of greed in the deal-making process that can make seemingly sensible strategies veer off course, along with a lack of focus when it comes to actually executing those proposed 'synergies'.

Kevin Appleton, the former Chief Executive of aerial equipment business Lavendon Group, says: "Having a clear, common idea of where a fair price for the business might sit avoids either party being drawn, even sub-consciously, into favouring self-interest."

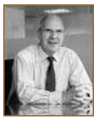
It remains to be seen whether boards and financial institutions will adhere to a genuinely results-based approach to M&A once the markets are in full flow again.

Featuring commentary from:

John Allbrook
Executive Chairman
Syscap Ltd

Kevin Appleton
Ex-Chief Executive
Lavendon Group

Roger Buckley
Corporate Finance Partner
BDO



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