theStorytellers®

THE MISSING CHAPTER:

WHY EMOTIONAL BUY-IN IS CRITICAL FOR SUCCESSFUL M&A

Methodology

In the summer of 2013, The Storytellers and Mergermarket surveyed 100 senior executives with experience of the M&A process using a mixture of quantitative and qualitative questions. These questions focused on the challenges associated with M&A integration, the importance of getting people to buy into a deal and the role that emotion plays in successful dealmaking. All interviews were conducted by telephone and all responses are anonymised and presented in aggregate.

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THE MISSING CHAPTER:

Foreword

It's not surprising that cultural integration is regularly ranked as the greatest business challenge during a post-merger integration. All the rational reasons for bringing two businesses together may stack up, but failing to engage people emotionally in the purpose of the merger or acquisition and what success could look like can be a major barrier to the rational factors playing out. If the goal is to create long-term, sustainable value, then business leaders need to plan – early on – how they will land this message with their employees and create a culture that supports these ambitions.

We have commissioned this study to explore the importance of emotional buy-in during post-merger integration. A number of business leaders have come to us for help over the years having recognised the need to embed their strategy, vision and a common culture into the heart of the organisation. It's been an essential part of their early planning, in order to expedite a smooth and rapid transition and to minimise any negative impact on customer relationships, the exit of talent and the development of an unproductive and resistant workforce which is unable to make sense of the inevitable changes, and feeling a lack of control over what is happening to them.

The Storytellers' role has been to help these leaders articulate the journey ahead as a simple, clear and compelling narrative and align the entire organisation behind it. Our post-merger integration programme focuses on helping leaders become inspiring, authentic storytellers, equipped to engage their teams and bring them with them through change. We help them capture stories of success that build people's confidence in and commitment to the new entity. And in turn create a sense of shared identity and belonging, raising levels of pride, purpose, engagement and productivity. It's a critical success factor.

Alison Esse,
Joint Managing Director, The Storytellers

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Why do people and culture matter in M&A?

"Integration is not as simple as it sounds and is the most time-consuming aspect of the entire M&A process. Some companies go through cultural integration for many years and still do not succeed. If not handled with enough resources from the beginning then cultural and people integration will become a never ending process."

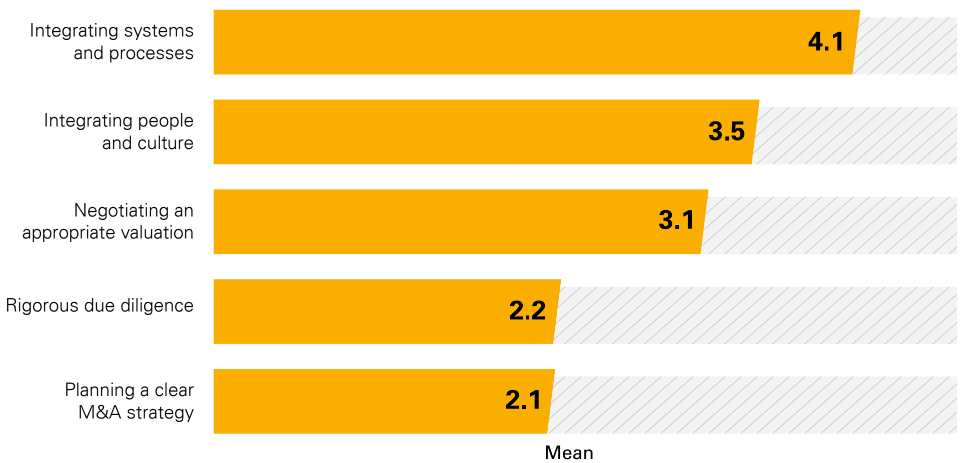
Director of Human Resources,
Spanish construction company

The successful integration of people and culture is seen as one of the most important factors in making an M&A transaction a success. However, it can be hard work, with respondents seeing it as a step that requires very significant resources. Taken together, these results make it unsurprising that the poorly-managed integration of people is seen as one of the most common reasons why M&A deals fail.

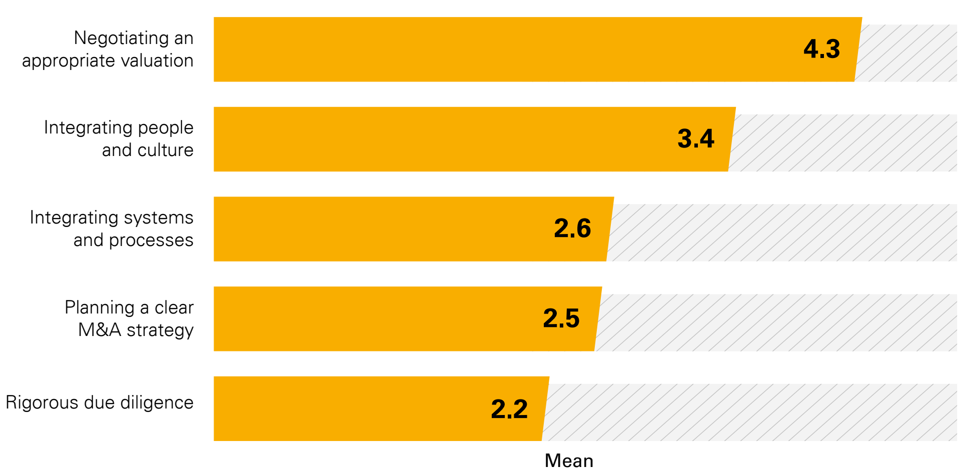
Fiona Ware, Human Resources Director at construction company Costain, elaborates: "The main focus during due diligence is often on financials and governance, which is hugely important. After all, if you can't make money then don't do it. However, more attention needs to be paid to the differing cultures of the organisations and whether these can successfully be brought together without destroying the inherent value of the company being acquired. Understanding the cultural differences is crucial to being able to create a culture and identity for the combined business that can drive the engagement of the whole workforce."

- Integrating people and culture is seen as the second most important factor in making an M&A deal a success, behind integrating systems and processes.
- It was the factor rated as requiring the second largest quantity of resources, behind negotiating an appropriate valuation.
- Scrimping on this aspect of a deal is therefore always likely to be a false economy, with firms that fail to assign sufficient resources less likely to conduct successful acquisitions.

What are the most important factors in making an M&A transaction a success?
(Please rank from 1 to 5, where 5 = most important)



Which steps require the most resources?
(Please rank from 1 to 5, where 5 = most important)

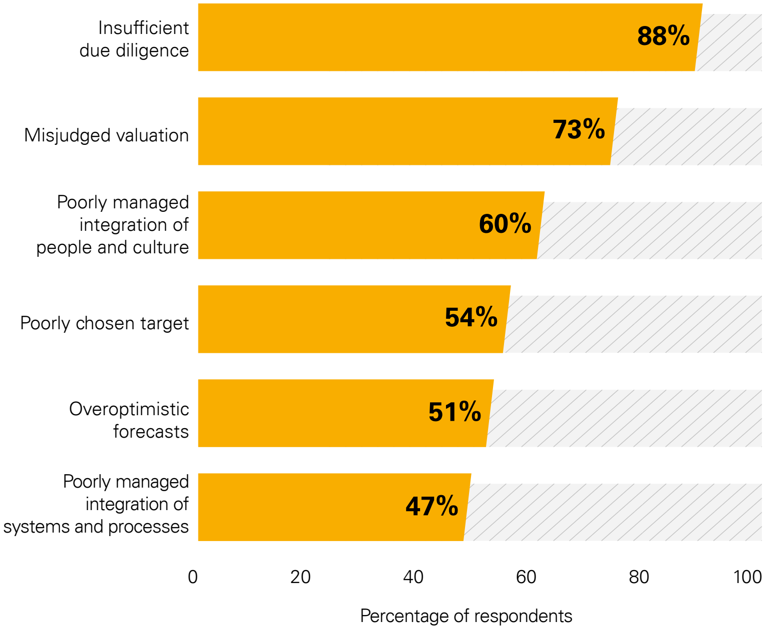


> “New co-workers are naturally wary of each other. There are no bonds between them and there is certainly little or no trust. These factors hinder information flows, so quickly establishing the company’s vision and values is the most important factor for making an M&A transaction a success.”

Vice President of Human Resources,
French industrial minerals company

- 60% of respondents list integrating people and culture as one of the most common reasons that M&A deals are unsuccessful.
- This factor was placed behind only insufficient due diligence (88%) and a misjudged valuation (73%).

What are the most common reasons that M&A deals are unsuccessful?



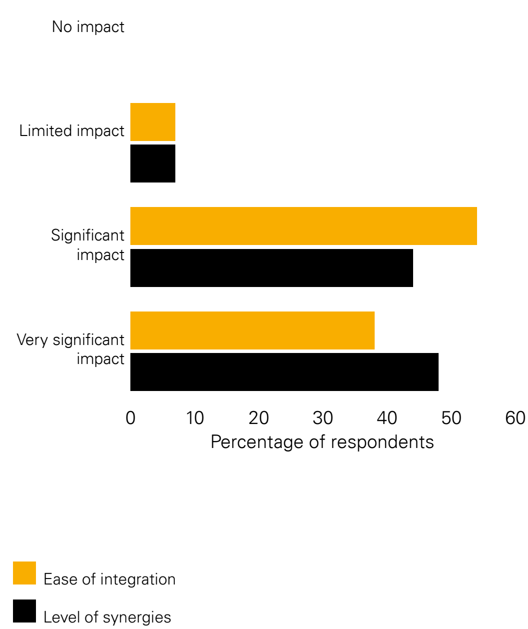
Getting emotional buy-in is key

If employees feel hostile towards the new company then all other aspects of the integration will be much more challenging. It is therefore crucial to get new employees on board, with the process of creating an emotional connection an often-overlooked aspect of ensuring the integration can proceed smoothly and efficiently.

Bill Payne, Vice President of CRM and Industries at IBM elaborates: "You have to approach the process with a mindset that will have two halves that add up to more than one, with people who can collaborate, contribute, communicate, complete tasks and are culturally savvy. To make this happen you need to get them on board as soon as possible with what the organisation is trying to achieve – emotionally engaged in its ambition and understanding the personal role they can play."

- Respondents reveal that making employees feel emotionally attached to the acquiring company is a key factor for an easy integration and high level of synergies.
- 93% of respondents say that the time taken for an employee to feel proud of their new organisation has a significant or very significant impact on the ease of integration and level of synergies.

Does the time taken for employees to state that they are proud to work for the acquiring company have an impact on how easily the integration proceeds and the size of synergies achieved?



The average number of days that respondents report it takes for an employee to say that they are proud to work for the company following an acquisition.

How to build an emotional connection

When asked what should be done to help build an emotional connection, respondents suggested that early and continuous communication was the most important factor. This was followed by a need to rapidly bring teams from the two organisations together, with delays likely to fuel resentment and distrust.

Linda Kennedy, former HR Director at Everything Everywhere, explains: "During integration, strong leadership from the front is critical – defining the strategy and getting people aligned behind it along with consistent two-way communication will help you to engage employees. Delivering some quick wins and sharing success stories will really help to bond employees together and ensure progress is made – but it won't happen overnight."

- Making sure all levels of management feel responsible for the deal was also seen as important, with enthusiasm likely to filter down and aid getting the rest of the organisation on board.

- Getting people excited about the deal and creating a compelling vision were also seen as key ways of ensuring employees become emotionally engaged with the new organisation.

> "The penny really drops when teams can see a shared vision of what the new company looks like. It shows that the leaders mean business, and creates a sense of excitement about the ambition of the new organisation."
>
> Martin Clarkson, Chairman, The Storytellers

During an M&A transaction, what steps should be taken to encourage employees to connect emotionally to the new entity?

1


Early and continuous communication

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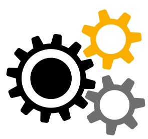

Rapidly bringing teams from two organisations together

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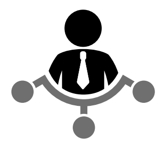

Ensuring managers at all levels feel responsible for making the deal a success

4


Creation of a compelling vision for the combined company

5


Getting people excited about the opportunities that the deal affords

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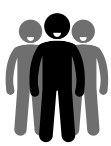

Behavioural modelling by senior leadership (leading by example)

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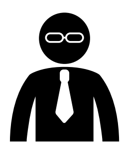


Strongly connecting the CEO with the deal

8


Training sessions and workshops

> "During M&A, change can be especially difficult and lead to stress, which can have a negative impact on morale if not handled effectively. Communication is critical during these times and organisations should strive to share as much information about what is happening and, most importantly, how the changes will affect individual employees."

Group Director of Finance, UK software company

What are the barriers to emotional buy-in?

In some deals the process of encouraging employees to build an emotional bond can be particularly challenging, with the attributes of the organisation being acquired having an impact on how difficult this process is. Respondents judge the most important factor to be a strong emotional attachment to the company being acquired. In these instances it can be important to take this attachment into consideration, with a message that stresses combining the best of the old with the best of the new.

- Another important factor is the size of the company being acquired in relation to the acquirer, which can raise questions over the balance of power and make it harder for employees to get on board with the deal.
- The time between the announcement and the integration is also seen as important, with delays likely to increase anxiety and resentment.
- Acquiring a foreign firm can also be more challenging, due to the increased likelihood of a cultural clash and resentment related to being managed by a firm with limited experience of the local operating environment.

> “Emotional attachment to the previous firm can be a big challenge as it is difficult to engage an individual who has served a firm for a long time and has good memories of achieving success. A change in policies and strategies may dampen their interest and the individual becomes demotivated and more likely to exit.”

Chief Financial Officer,
German telecoms company

Which factors increase the challenges in aligning corporate cultures and getting buy-in from employees?

1. Emotional attachment to existing brand
2. Large size of acquired company (in comparison to acquirer)
3. Time between announcement and integration
4. Acquiring a foreign business
5. Strength of identity of acquired company
6. Acquiring a previous competitor

“Employees become emotionally attached when they see how they make a direct contribution to their company’s success. However, during a takeover this attachment is likely to break, which makes alignment and buy-in of employees difficult.”

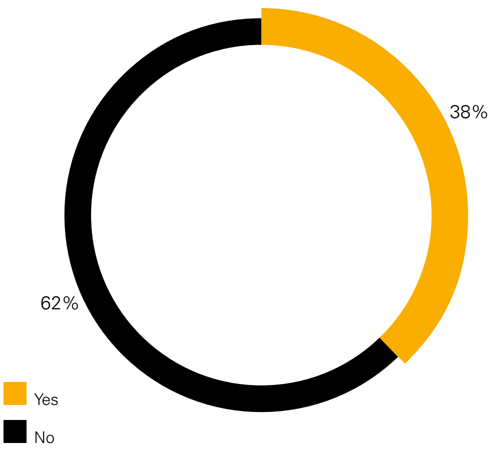
Vice President, Human Resources,
UK construction company

What happens when people and culture are neglected?

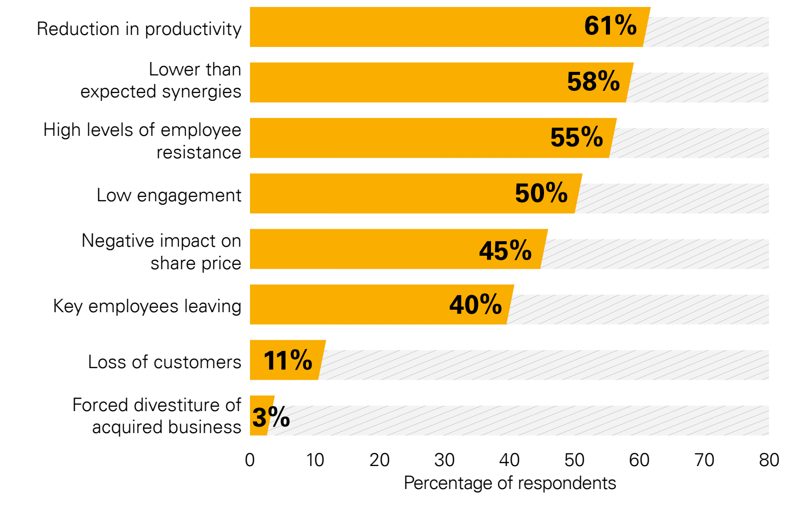
Neglecting people and culture during the M&A process can mean that a deal fails to unlock the expected value, which will ultimately have a negative impact on a company's valuation and share price. Despite high levels of awareness of its importance, a large number of respondents had been involved in a deal that was hampered by insufficient attention in this area.

- 38% of respondents have been involved in a deal that struggled because of the poorly managed integration of people and culture.
- For those respondents, the most common consequences were a reduction in productivity, lower than expected synergies and high levels of employee resistance.
- 45% of respondents said that getting the cultural integration wrong had had a negative impact on the firm's share price.

Have you been involved in a deal that struggled because of the poorly managed integration of people and culture?



What were the consequences?

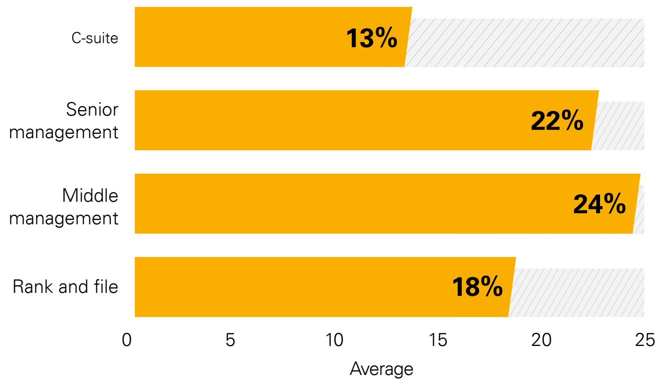


A direct financial and operational cost

One of the most visible results of poor cultural and employee integration is high employee turnover, which has a direct financial cost. Our survey suggests that disaffected middle and senior managers are the employees most likely to leave, resulting in a shortage of expertise and leadership exactly when it is needed the most.

- Respondents report that uncertainty and change resulting from the M&A process leads to a high number of employees leaving that the organisation would have liked to retain.
- The biggest losses are seen in senior and middle management, meaning that companies will often be left with an experience and expertise gap while these employees are replaced.

During the M&A process, what percentage of acquired employees (that the buyer would like to retain) end up leaving the organisation?



"Bringing companies together in an M&A results in core competencies that must be actively harvested to enrich the new overall organisation. If this process is not given the care and attention it needs the resulting company may fail to flourish."

Chief Financial Officer,
UK electronics manufacturer

Using the results of the survey and figures for the average cost of employee turnover from CIPD we can calculate the representative cost of unwanted employee churn as a result of M&A. For an organisation of 1,000 employees a takeover is likely to result in a cost of £1.3mn from unwanted employee turnover, with this cost rising to £6.5mn for an organisation with 5,000 employees.

Organisation size (employees)	Cost resulting from unwanted employee turnover as a result of M&A
500	£650,000
1,000	£1.3mn
5,000	£6.5mn
20,000	£25.8mn
100,000	£129mn

“During a merger major changes often happen in the senior management team as there will be a lot of strategic changes which may not suit the senior management’s attitude and behaviour – and this can result in them quitting the organisation.”

Director of Human Resources,
Luxembourg-based industrial company

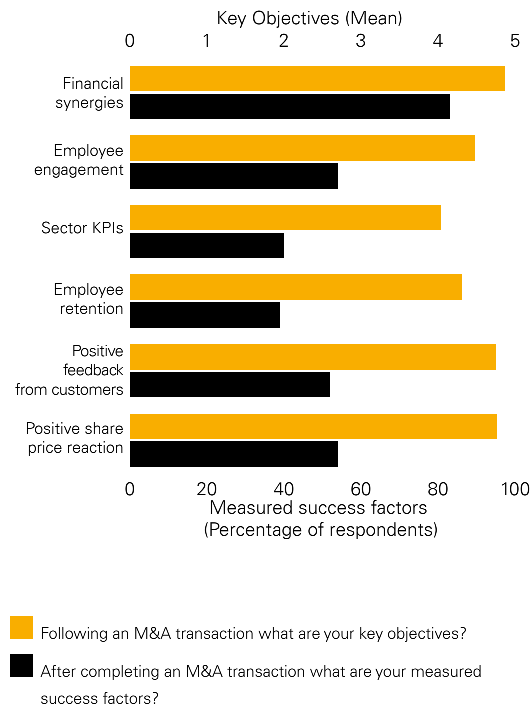
Why are people and culture neglected?

Even though the majority of executives now recognise the importance of getting the cultural aspects of a deal right, the high number of deals that fail for this reason suggests that this aspect still does not receive enough attention.

One reason for this is that factors such as employee engagement and retention are not used as key success measures by which the deal is judged and therefore do not get the focus that they deserve.

- Employee engagement and employee retention are less likely to be rated as key objectives in comparison to financial synergies and share price reaction.
- They are also much less likely to be used as a measure of success – only 50% of respondents use employee engagement as a measure of success, while less than 40% measure employee retention.
- In comparison, more than 80% of respondents use financial synergy measures to judge whether a deal has been successful.

Paul Staples, Head of Corporate Finance at BNP Paribas elaborates: "During the heat of battle, it is important for boards to recognise that M&A is an exercise in risk management as well as value creation. This highlights the significance of effective, trusted communication between divisional management and the executive team. Efficient integration should be viewed as a journey rather than as a stated objective."



Miles Roberts, CEO DS Smith

Case study:

DS Smith acquisition of SCA Packaging

"It's all in the planning"

DS Smith, a UK packaging company with a strong presence in France and Poland, acquired rival SCA Packaging in 2012 as part of its strategy to become a truly pan-European corrugated supplier which could now challenge the leading player in the market. The scale and ambition of the deal was significant, given that SCA Packaging was even larger than DS Smith, and would double the size of the organisation to some 22,000 employees.

Business Development Director Gary Saunders, previously Divisional CEO, European Packaging at DS Smith, explains how careful planning months in advance was critical to the success of the integration…

"When you complete an acquisition it's like dealing with a tsunami. There's so much intensity, information, questions and uncertainty flying around, you need to be as well prepared as possible to deal with what can, at times, feel like a crisis.

For us there were three very clear priorities. The first was to establish and announce the new senior leadership team and structure immediately to create a sense of stability and ensure that clear communication could start immediately. This was absolutely critical. It was vital that employees knew from day one what was happening and why, had clear leadership and context, and knew the role they were to play within it. The second was communication to customers, making sure that our people knew the rules of engagement in dealing with their expanded customer-base – and would not try to be bigger and smarter than their counterparts, but work as a team. The third was to work out synergies as soon as possible, creating a roadmap and process to identify, deliver and track them.

The important thing was to get people settled as soon after the acquisition as possible. It's much harder to do this once time has marched on, even if painful decisions have to be made in identifying who will be staying or leaving. Mistakes will be made, but hesitation makes the process far more difficult to deal with. We spent months and months planning in advance, culminating in a major meeting for our top 200 leaders just three days after completion. For this event, our senior leadership team worked closely with The Storytellers to craft a compelling, visual narrative of our vision for the future which we confidently shared at the event, ensuring that these leaders left excited and engaged, and with the tools and confidence to share the story with their teams and explore what it meant for them in their part of the business. The ‘wow’ factor was important: you can’t manage 22,000 people on your own, so getting them on board early on was critical.

If you treat people with respect, make decisions in advance and communicate clearly and honestly, the culture should fall into place. You will always have cultural differences in a business of this size and scale, but if you get the basics right and plan well ahead you should avoid any major cultural issues. We made sure that our leaders knew that they had to work as a team; failure to do so would fall on their shoulders.

One year into the integration process, we can look back and be satisfied, although we still have many opportunities for further synergies. We didn’t lose a single customer due to any integration issues, and it was noted by one of our biggest customers that from their perspective the integration was seamless. At a recent management conference, a leader new to the business commented that it was impossible to distinguish between ‘who was ex-DS Smith and who was ex-SCA Packaging’. We started to work as a single team from day one, and the integration process has been a smooth one as a result. Without detailed and early planning though, it wouldn’t have been the success story that it’s been.”

For further information, please contact Alison Esse, The Storytellers, on +44 (0)20 7590 5440.
Or visit our website at www.thestorytellers.com

About The Storytellers

Founded 10 years ago, The Storytellers are world leaders in the use of narrative and storytelling techniques that help business leaders realise the potential of their people. We help them to execute strategy, build cultures, improve performance and make change happen.

We have worked with over 140 organisations worldwide to create cultural and behavioural change using our innovative approach. Based in a historic town house in South Kensington, London, we are a thriving team with a highly unusual mix of skills; from strategic writing and dynamic coaching/facilitation, to change management, psychology and film, graphic and multi-media design.

Our programmes often start in the boardroom, where we've helped dozens of executive teams develop a clear and inspiring narrative of the journey they are on. We're proud of how we've helped them go on to inspire and engage their people, and how teams across almost every industry sector have used our techniques to identify and implement the changes they need to make. And how they have built a rich culture of storytelling, where stories that exemplify desired behaviours reflect 'the way we do things around here'.

The results speak for themselves; time and time again we've made a tangible contribution to improved productivity and business performance.

We've seen a fundamental shift in the way that businesses embrace the use of storytelling. We're still unique. We're still learning. We're still pioneering, and we're still committed to our vision of helping everyone in business realise the power of their story.

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About Mergermarket

Mergermarket is an unparalleled, independent mergers & acquisitions (M&A) proprietary intelligence tool. Unlike any other service of its kind. Mergermarket provides a complete overview of the M&A market by offering both a forward-looking intelligence database and a historical deals database, achieving real revenues for Mergermarket clients.

For more information, please visit www.mergermarket.com

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