staffan engström limited

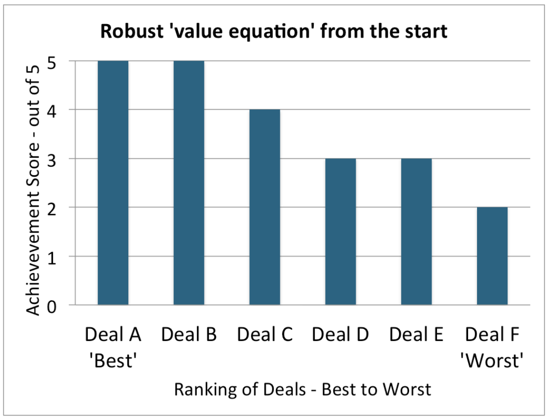
Making Successful Acquisitions

Having led many acquisitions over the years, I have put together my main lessons on what makes a successful acquisition. I have taken a look at half a dozen of the deals that stand out as amongst the most interesting that I have done, and ranked them from A-F in terms of their overall success (A as the best, F as the 'worst'). I have then drawn out my main lessons learned and estimated how each performed by these lessons, on a scale of 1 to 5.

1. Develop a robust 'value equation'

My first lesson is the need for a robust 'value equation' when you do a deal. You need to understand precisely how you expect value to be created through it, splitting the problem into its component parts: sales growth delivery by business and market; cost savings; cross-selling etc. This is so that the plan can be tested, individual leaders and managers can take ownership and accountability for delivering the results, and you know how you are doing on its delivery. Surprisingly many purchasers rely on broad business plan growth and margin numbers without a concrete underpinning assumptions framework, in effect betting success on hope and promises.

The question that I always ask is: How does 2+2=7? The usual equation of 2+2=5 to justify a deal is NOT enough. The benefit potential needs to be substantial enough to support a good deal of error, because there will be surprises.



When I looked at my half-dozen 'best-to-worst' deals I found a direct correlation between the robustness of the valuation equation and the success of the deals. See the graph, above.

2. Only consider targets already identified in the strategy

Do you have those times when an investment bank or sales agent gets in touch to find out if you are interested in acquiring a certain business? Often nobody knows, so the idea either flops around while no-one takes accountability, or it starts moving too quickly, costing money and distraction because it has a champion but no-one strong or clear enough to stop it.

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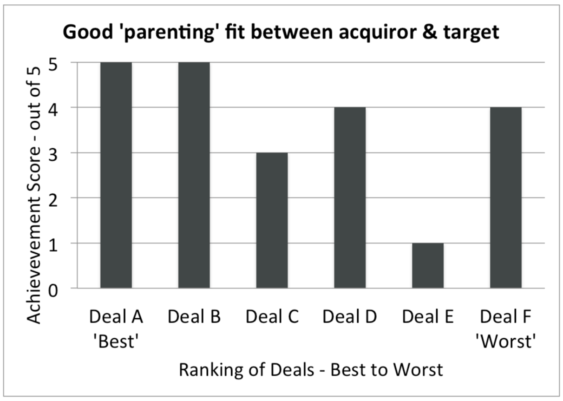
My firm advice is that you will save a lot of wasted time, effort, post-rationalisation and distraction if you employ the rule never to go after anything unless it fits the pre-set criteria that you agreed *before* you heard about the deal. It doesn't have to specify individual targets, but you should know in advance what kinds of opportunity you are looking for and why. Again, my six Best to Worst deals show a strong correlation between target identification and deal effectiveness.

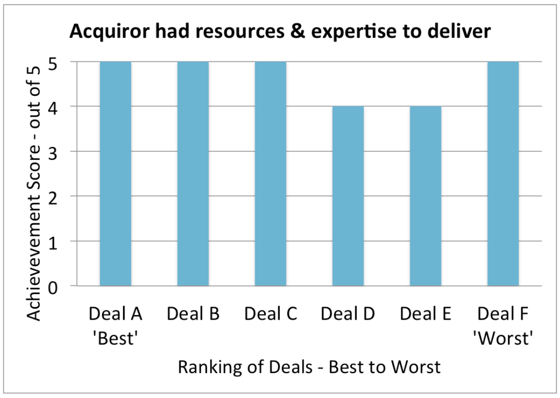
3. Buy only what you understand well enough to manage



When you make an acquisition, it is essential that the people at the top of the company understand how to manage what they have bought. If they don't you will find that the wrong senior-level 'levers' are pulled at the wrong times, which are mistakes that destroy value.

For example, when blue-collar delivery companies try to manage professional services businesses they frequently fail to understand the importance of acknowledging and managing the professional self-image of the 'workforce', with a consequent adverse impacts on key staff retention.

4. Make sure that you have the appropriate resources to deliver



I know that this one sounds obvious, but it really matters. I have too often seen managers, who do not understand M&A, try to save money by hiring advisors that are cheap. Beware of using cheap advice – it is cheap for a reason! You have to have the resource and expertise both to do the deal and to integrate efficiently and effectively.

5. Undertake due diligence on what *really* matters

Of course, doing proper due diligence is a must for any deal, but the surprising aspect from my analysis shows that great due diligence will not create the best deals. The reason for this is that whilst good due diligence might prevent you doing a bad deal; it is not in itself the creator of value. Value comes from the implementation of the ideas, strategy and inspiration put into action through the acquisition. It is this value creation that needs to

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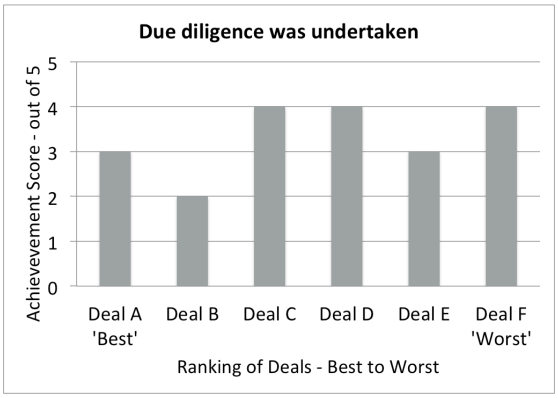
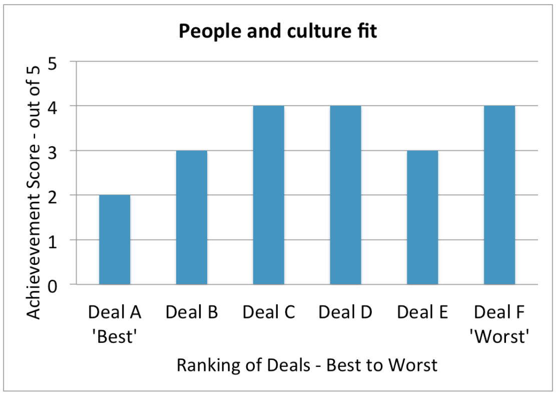
be clearly elucidated and validated as part of the deal… without ignoring the more normal due diligence work!



My advice is to insource your operational due diligence. If you haven't got the skills for this, then beware. Is this really a business that you know how to manage? See 3, above.

6. Make sure that the people fit works

Making sure that the people fit works is one of my key lessons, yet which acquirers seem to spend so little time on. Why do they do this? It is because it is really hard to do well!



It is vital to take the time to form a clear view over whether your respective organisations will understand each other and how management effectiveness will be reinforced. Very few bankers, lawyers, or accountants will advise you on it. *You* have to make the judgment.

Saying that, you will notice that if anything, my experience of the deals above shows the opposite trend, with the best deal having scored lowest in people and culture fit.

I can think of only one thing to put forward in my defence: *"The exception proves the rule."*

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