The Impact of Management on M&A Success:

Is the Right Team in Place to Maximize Your Company's Pre-Sale Value?

Articles designed to help CEOs identify and close performance gaps in their organizations.

There may be no bigger transition in the evolution of your company than that of a merger or acquisition.

Perhaps this pending change has been part of your exit strategy all-along, formulated along a well-thought out path as part of your strategic planning process. Maybe it is in response to some other change. Regardless, it is not just the end result that will be dramatic, but the process itself.

Perhaps you know all of this, and at Cerius, we do not want to temper any CEO's enthusiasm for planning or executing an M&A strategy! We do, however, want to offer a functional and realistic menu of questions to help you prepare. Why? For starters, research indicates that the majority of M&A transactions or other strategic alliances fail, whether the objectives are financial or strategic. Not only that, the same research indicates that regardless of the nature of the merger – friendly, hostile, or well-managed – the individuals involved undergo stress. A well-placed team can help you execute a transaction successfully with maximum value for your company – and mitigate the seemingly inherent stress involved. To this end, we solicited advice from some of our seasoned executives, to help you set the management stage for the opening act of a successful M&A: your company's pre-sale value.

Reasons for M&A Failure: Why Do They Fail?

In a research paper published in 2011 in the European Journal of Business and Management, the authors pointed out that about 80 percent of "corporate combinations" fail in terms of achieving "their desired financial or strategic objectives" (Rajeev, Jyoti, 2011). This has been supported by other noted researchers, with a few key reasons for failure:

1) the wrong company

2) the wrong price

3) the wrong time

But at the root of most failures?

"the process through which the deal is conceived and executed" (Marks, Mirvis 2001). At the top of the CEO's checklist needs to be having the necessary expertise on your team to navigate your company through a proven arduous process that has left many corporate carcasses in its wake. Successful M&A outcomes occur, but you need the weapons to predict and then defeat the impediments to that success. "I believe the failure to achieve the desired results is impacted tremendously by the quality and efficacy of the pre-merger integration planning, and the post-merger integration execution," says one of Cerius's interim executives with extensive M&A experience.

Questions for All Companies

Do you have a written strategic plan currently in place that has been followed?

This question specifically incorporates "that has been followed" because too many times, the process of the plan creation gains the emphasis, rather than the *ongoing execution and monitoring.* Remember this plan includes a SWOT analysis – your strengths, weaknesses, opportunities and threats – so that you can capitalize on your strengths, and shore up your weaknesses. One of our interim executives advises that any company preparing for an M&A process that does not have a strategic plan, should develop one. "You'll get credit for having one during due diligence," he notes.

Why it's important for your management team and the M&A process: In addition to keeping you on your path for growth, your strategic plan – done correctly – contains the processes you need to evaluate the strength of your team. Are they meeting their performance indicators? You will have fewer unanswered questions if these measurements have been taken on an ongoing basis.

Do you know what the buyer is looking for?

"Initially, buyers target a business for acquisition based on the uniqueness of its product or service, and revenue growth opportunity," explains one interim executive. "Once a buyer is interested in the company, the next highest item of importance is typically the management team." There may be some variations on this depending on the type of transaction, but "the best value proposition possible needs to be presented to the transaction partner," says another executive.

Why it's important for your management team and the M&A process: Buyers go to great lengths making certain the team that will run the acquired company is very strong and has the necessary skills and experience for success. As a CEO or business owner looking to sell a company, it is very important that the qualities and abilities of the team are as strong as, or stronger than, the product or service the business provides. One interim executive suggests CEOs think of it as shoring up the foundation of a house they are selling, complete with a thorough understanding of what your value proposition is for each potential buyer to maximize valuation – as this will vary based on the capabilities and strategic objectives of the acquiring company.

Is this a strategic sale, or a financial sale?

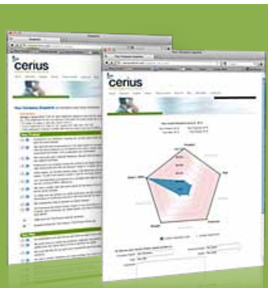
All of our interims agree that "there are distinct differences between financial and strategic buyers when it comes to the management team of the company being acquired," as one put it. The financial buyer, perhaps a private equity group or hedge fund, will not be in your business "space," while the strategic buyer is, and likely to be in it for the long haul. These differences will affect not only their examination efforts, but should be reflected in the strengths of your management team.

Why it's important for your management team and the M&A process: A financial buyer is more likely to keep the company's management team in place following the transaction, but that team will be subjected to exhaustive interviews and evaluations to gain a high level of comfort it can carry the business forward to the next level of projected results. This buyer will want to leave the day-to-day business operations to this team. The strategic buyer will either integrate your company into existing operations, or keep it as a stand-alone entity. You may need an outside expert to facilitate some integration initiatives.

Given the nature of the sale, are you confident that you have the management strengths that are most needed?

This relates directly to the previous question: Is the purchase strategic or financial? "The financial buyer will generally provide board level oversight and financial resources along with key customer, technology, and supply contacts," notes one interim executive. "The seller needs a strong management team that is positioned to take the company forward, and demonstrate that to the buyer." A strong player in a strategic sale may be one with a distinctive capability that can greatly enhance overall capabilities and performance – perhaps a CIO or VP of Sales.

Why it's important for your management team and the M&A process: Since financial buyers generally want a comfort level in the



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Interim executives are sometimes referred to as contract managers, temporary managers, even super temps.

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management team to continue running day-to-day operations, they demand a very strong CFO to manage the company's capital and produce detailed financial reports and models. This needs to be proven prior to the sale. The strategic sale needs strengths for a transition, or integration, depending on the buyer's long-term goals.

Have you given yourself enough time prior to the transaction to have the best management team in place so its impact on business performance is clearly evident?

A buyer will typically conduct a very thorough due diligence, which can take several weeks, or even months, to complete. This process will identify and confirm the strengths of the company, as well as any issues. You want the strengths to outweigh the potentially problematic issues. "In general, if the management team needs to be upgraded or expanded, it would be wise to have them onboard at least six to nine months prior to any acquisitions so that their effectiveness can be demonstrated," notes one interim executive. Another cautions that to have a new management team in place without giving it enough time to demonstrate performance can actually increase the perceived risk – thereby lowering the value and the ultimate purchase price.

Why it's important for your management team and the M&A process: In order for the seller to maximize company value, it is important to start well in advance of the desired sale date. Inevitably, something will come up during due diligence that should have been addressed prior to negotiating its sale. Interim executives with significant M&A experience can address key operating, sales, and financial issues well in advance of any negotiations.

Are you paying the right amount of attention to your human resources?

"People are one of the highest considerations in any M&A transaction," says one interim executive. "This is particularly true for middle-market privately owned companies that are usually tightly staffed. " He also points out that most CEOs and business owners will sell only one business in their lifetime, so calling in expert help is paramount to a successful outcome. "Your company must be 'hitting on all cylinders' prior to a sale, so the weakest areas need the most attention, while no areas can be ignored," cautions another executive.

Why it's important for your management team and the M&A process: While you and other key members of your team are juggling the demands of ongoing business operations and preparing the company for sale, the human element is easy to overlook. If this is your first such transaction, it is even more challenging. This risks employees disengaging from their jobs, which can lead to a drop in productivity and thus, profitability – not what you want prior to your sale. While anxiety and resulting productivity decline is common in transactions for buyers and sellers alike, a proactive communications plan can diminish many people problems and stifle the rumor mill that will operate in the absence of well-communicated facts.

Do you know how to handle gaps, or weaknesses, in your management team?

If you know there is a weak link in your management team, you may be concerned that replacing him or her would signal instability. Our executives' advice? "Shed that feeling," says one. "Ask yourself if you should be supplementing a deficiency, particularly when you are concerned about pre-sale value." In both this instance or to fill an existing gap, do not assume that a permanent personnel hire is the best approach prior to M&A activity. Depending on the type of transaction, an interim executive could offer attractive flexibility to a buyer who will be bringing in his own team. "There may be intermediaries or financial advisors involved in the sale of the company, and you may be tempted to feel as though that's enough," says one executive. "However, realize that these advisors have a vested interest in the fees they will receive for the sale of the company which may cause them to press a CEO to 'get the deal done.' An interim has no such agenda and can provide completely objective advice."

Why it's important for your management team and the M&A process: A seasoned interim executive who has guided teams through the M&A process before has the experience necessary for both performance, and tactful integration to not disrupt the company culture. This experience goes a long way for both you, and the perception of the buyer, in navigating the unknown.

Do you know where you should focus your M&A activity if your company is in trouble?

A buyer of a troubled company will want to know how much of the trouble can be attributed to management. The causative factors will dictate which areas of the company need to have stronger management in place -- whether in Finance, Operations, Marketing, Sales or Engineering.

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Meanwhile, you need to continue to meet your requirements set by banks, vendors, stakeholders, while seamlessly serving your customers. This is one scenario where an experienced interim can have an immediate impact. "Sometimes it's necessary to pull in new ideas and challenge conventional wisdom,"

Why it's important for your management team and the M&A process: In this case, an interim executive can send a strong signal to a buyer that the major issues that led to the company's trouble are being addressed. A buyer will want to see strong financial, sales, marketing, and customer service management. Communication with all stakeholders is also very important to instill confidence.

Can you be objective about whether you are the best person to lead the company through this transaction?

This can be a complex situation; not just because you have to ask – and answer – the difficult question, but because it is contingent on other factors, such as whether the buyer will be bringing in their own CEO. If you are both the CEO and the business owner, it could be in the company's best interest both pre- and post-sale to bring in a strong COO well in advance of the sale so there is a senior, non-owner leader who offers continuity, regardless of what happens. "And if you are not the business owner, the buyer will want to see that you have a vision for the company and can provide compelling leadership to engage employees and customers in being a part of that vision," one interim executive says.

Why it's important for your management team and the M&A process: If you are also the business owner, a buyer can be wary of a company's over-dependence on a CEO, and that it could make the transaction more difficult. By bringing in a strong COO, you are allowing the buyer to witness that the business can be self-sufficient without the CEO's daily involvement, which is better in terms of the sale. For CEOs who aren't the owners, the board of directors and shareholders will evaluate your capabilities to see if you are right for the next chapter of the company – regardless of how successful you have been in getting it to where it is today.

Additional Observations

1. Preparing a company for sale is an onerous process, and many steps are inadvertently neglected because the CEO is already busy, or simply may not know what needs to be done to ensure the highest possible value at time of sale. For example, one interim executive pointed out that evaluating and enhancing a company's legacy processes to become well thought-out, documented business processes that will support company growth, is something that can easily be overlooked unless you've been through the M&A process.

2. Core business still needs to be tended to – that's what makes the CEO's job so difficult! The existing management team already has its hands full running the business. Give some serious thought, well in advance of beginning the process to sell, of hiring an interim executive or even a team that can focus on refining and implementing key business improvements. These may even be done on a project basis – but should be completed prior to any negotiations.

3. Don't be guilty of a well-documented M&A sin that is worth re-emphasizing: ignoring the human element. Involve your human resources department on a very intimate level to assist you in keeping the employees updated on a regular basis. Remember that "under-communication" leads to assuming the worst, and this is not the time to deal with staff defects or productivity problems. If you can trigger enthusiasm in your employees, that will go a long way towards a successful transition; if not, at a minimum, be sensitive to their fears and concerns and make efforts to let them know they are integral to the process.

4. Related to #3 above: Buy-in from every employee may not be realistic, but do not waste your time and energy trying to stifle internal debate. Solicit criticisms and concerns; it could lead to proactive efforts that can prevent unpleasant issues from tripping you up – issues that could come up in due diligence.

Going back to our executive's metaphor of shoring up a house's foundation, remember that you, too, are staging your company for sale. Your management team is a key underpinning to a solid and secure transaction. An interim executive who has gone through the process is frequently the key to increasing your pre-sale value.

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