

# The Challenges of M&A Execution

A Report of Findings from The Keystone Group's  
2007 Survey of M&A Execution Performance



THE KEYSTONE GROUP

MERGERS & ACQUISITIONS SERVICES ■  
STRATEGY AND OPERATIONS CONSULTING  
■ TURNAROUND CONSULTING

# The Challenges of M&A Execution

A Report of Findings from The Keystone Group's  
2007 Survey of M&A Execution Performance

January 2008

The 2007 Survey of M&A Execution Performance is just one of the many ways The Keystone Group helps companies track and improve their deal performance. In addition to the current research, our Quarterly M&A Executive Forum takes an in-depth look at specific issues related to diligence, integration and, ultimately, deal success, as well as providing an opportunity for M&A executives to share their experiences with and learn from their peers. Previous sessions have examined the challenges, risks and opportunities of doing deals in China, and the most pragmatic, effective ways to mitigate post-merger culture integration risk. Please let us know if you would like to be included on the invitation list for upcoming Forum sessions.

The Keystone Group was founded in 1991 to bring an execution focus to management consulting. The founders were dissatisfied with the typical consulting engagement that was long on analysis and ideas, but short on execution and delivering results. Working in small teams, we quickly define a range of solutions, build a plan of attack and get on with delivering results. Visit [www.TheKeystoneGroup.com](http://www.TheKeystoneGroup.com) for more about our backgrounds and experience, or contact

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## INTRODUCTION

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The Keystone Group annually surveys industry leaders active in corporate Mergers and Acquisitions. The goal is to better understand how companies view deal performance and manage the complexities of merger integration.

During the month of December 2007, we requested input from a variety of deal participants, including senior corporate and division line managers, senior corporate staff (CFOs, legal, HR, etc) and senior corporate development managers. This report presents the results and provides a unique perspective on how people who are actively doing deals address the challenges of M&A execution.

The findings are presented in four sections covering background on the deals and the market, how companies approach execution, what the outcome of their deals has been and lessons learned. Significant comments have been paraphrased to present a consensus view and preserve anonymity.

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## EXECUTIVE SUMMARY

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2007 Survey Highlights Include:

- Overall expected deal flow to be down in 2008. Less pronounced for mid-market strategic buyers, more pronounced for private equity financial buyers.
- General nature of transactions changing. Less focus on cost synergies and increasing focus on top line and incremental capability expansion.
- Execution requirements (e.g., meaningful target participation in planning) related to new deal environment are still inconsistently addressed. Results in mediocre performance in key areas like knowledge transfer and top line synergy capture.
- Culture integration and assimilation continues to represent a critical risk area relative to deal execution performance.

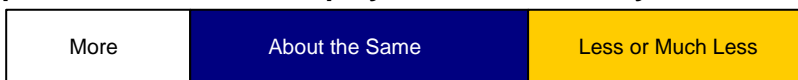
# MAJOR FINDINGS

## Deal Background, Market and Drivers

While deal volume held steady during 2006 and 2007, participants expect to complete fewer transactions in 2008, even though both valuations and competition from Private Equity firms are seen as unchanged or somewhat lower over the last 12 months.

As in 2006, Top Line Growth was the primary reason companies pursued acquisitions. While Cost Synergies were important, they were rarely the number one deal driver for survey participants. Perhaps not surprisingly, cost synergies were more frequently associated with larger transaction sizes.

### Competition from Private Equity firms versus last year



### Valuations versus last year



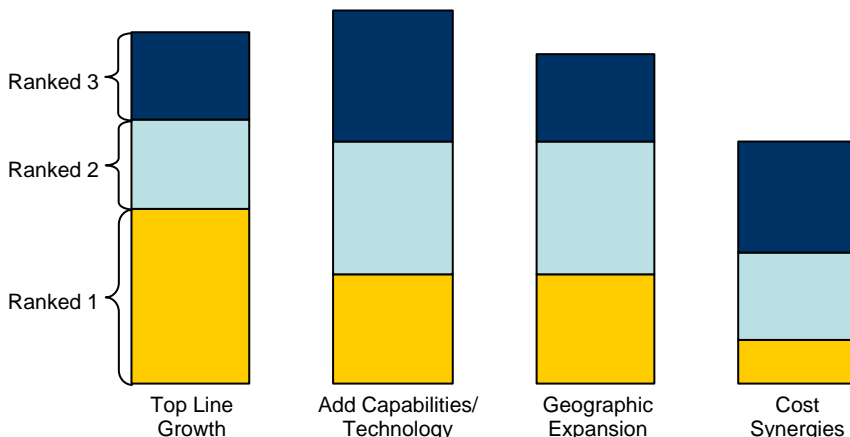
75% said competition from Private Equity was about the same or lower, while 80% saw valuations about the same or lower.

### Deal volume



Half of survey participants expect to do fewer deals in 2008 than they did in 2007.

### Deal drivers



Top Line Growth was ranked first by almost one-third of respondents. Adding Capabilities/Technology and Geographic Expansion were also important deal drivers. Fewer than 10% of respondents made acquisitions last year driven primarily by Cost Synergies.

The tightening capital market environment along with (in some industries) a dwindling number of suitable target prospects appears to be slowing the blistering pace of transactions we've observed over the past two years.

However, strong corporate balance sheets, combined with lessened private equity competition seems to have created a window of opportunity for many strategic buyers.

Cost synergies were rarely the number one reason for doing deals. This may reflect a realization that consolidation synergies can be difficult (and painful) to achieve.

Moreover, we've also observed that a number of industry sectors have already undergone significant consolidation, leaving the remaining deal opportunities in areas like top line and marketshare growth, incremental capability, etc.

# MAJOR FINDINGS, CONTINUED

## Execution Approach

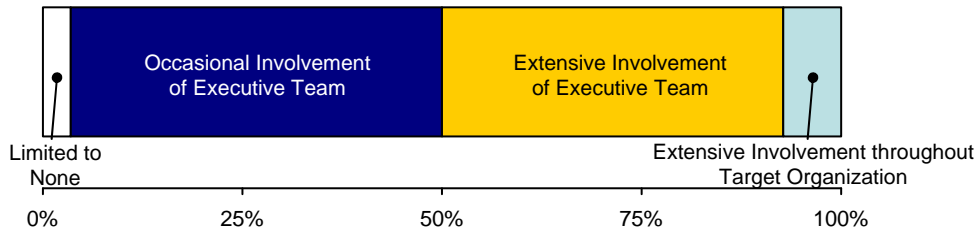
In this section of the survey we explored how companies tackle the challenges of execution, including whether they have dedicated teams that are specialists in integrating new acquisitions; when they begin planning integration and who is involved in that planning; and whether deal performance is tracked in real time by specific synergies, overall performance or after-the-fact.

We found that only a small percentage of the most acquisitive companies have a dedicated integration team. Most companies (68%) rely heavily on resources from their operating teams to complete post-merger integration. However, there is clearly growing frustration and discomfort with trying to execute time-sensitive integration with operating resources who still have their “day job” responsibilities. When asked what they would do differently, many put a dedicated integration team at the top of their lists.

Overall, 92% of surveyed companies begin integration planning during or prior to due diligence. Generally speaking, the more deals a company does, the earlier it tends to begin planning the integration.

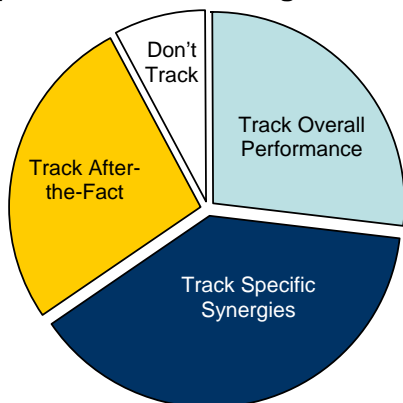
The target’s executive team has had at least occasional integration planning involvement in the vast majority of transactions. Companies were far more likely to involve the target in integration planning when cost synergies were the deal drivers than when they were looking for top-line growth or new capabilities.

### Target involvement in integration planning



The target’s executive team is extensively involved in planning in 43% of survey responses, and the entire organization in 7%.

### Deal performance tracking



Nearly all companies track deal performance in some way. Fewer than 40% track the results of specific synergy projects. A fourth of the respondents report tracking overall performance metrics like revenue and EBITDA, and an equal number say they roll acquisitions into operating results then audit deal performance later.

Deal performance tracking approaches vary widely.

Among the lessons learned (not surprisingly):

A dedicated integration team dramatically improves odds of deal success.

Early integration planning is critical to downstream execution performance.

Given competitive and/or regulatory restrictions re information sharing, early utilization of “clean room” or other pre-close planning techniques have proven to be particularly effective in getting a jump start on planning.

The tracking of deal performance—particularly in the area of synergy realization—often encompasses far more than standard accounting tools provide.

*“A commitment to early integration planning has had a definite impact on our ability to hit the ground running upon close.”*

Survey Response

# MAJOR FINDINGS, CONTINUED

## Deal Performance

In our experience, acquisitions that deliver are the result of sound deal strategy and valuation, meticulous post-close business continuity, and accelerated synergy realization. Integration planning and execution discipline are key tools to achieve these results. We asked our survey participants how they felt about their deal performance overall, and to examine the specific drivers of this performance.

Unfortunately, fully half of participants report overall deal performance is mixed or below-expectations. While this represents a slight improvement over the 55% in this range in 2006, it still points to substantial unrealized value. Companies doing deals to achieve cost synergies or capacity roll-ups were slightly more satisfied with deal performance, but even they reported results exceeded expectations in only 55% of their transactions.

Despite a growing pool of experience, and a record number of transactions, half of all survey participants report overall deal performance is mixed or poor.

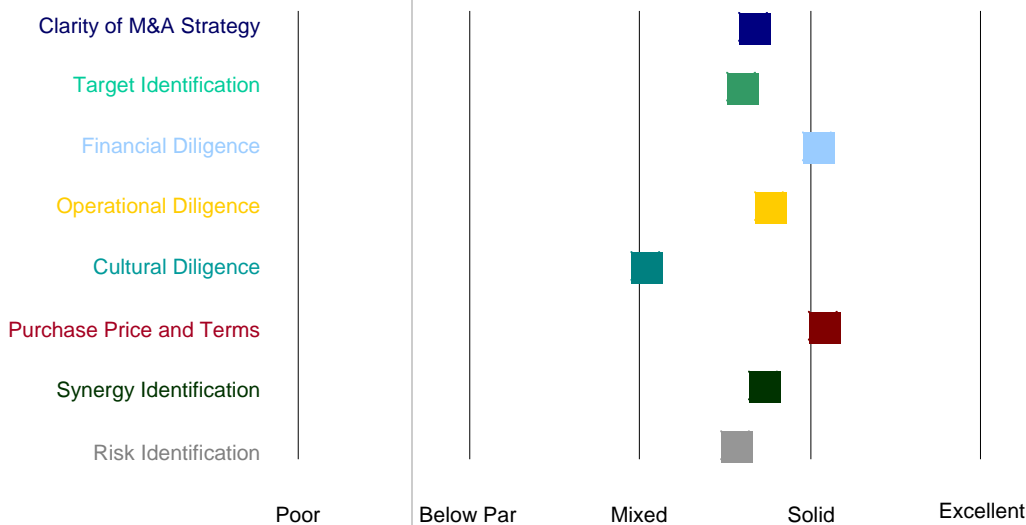
The only two areas of reported “solid performance” include: financial diligence, and purchase price and terms. All other deal areas reported “mixed” performance or worse.

The problem of M&A value capture remains a problem of *planning and execution*. The most common areas of pain are Culture Diligence and Culture Integration.

Customer retention has been a key area of post-close continuity focus.

There is growing concern, however, about the impact of the other risk areas on eventual customer retention.

### Deal strategy and valuation performance



Companies felt their performance on financial diligence and purchase price were generally solid. Most other aspects of deal strategy and valuation were mixed, with the exception of cultural diligence, where performance tended toward below par. Companies reporting solid results on operational and cultural diligence also felt better about their performance retaining key employees and identifying and quantifying risk.

### Post-close business continuity performance



Seamless operations and culture assimilation were the most challenging aspects of post-close business continuity performance. Not surprisingly, culture assimilation tended to be better when cultural diligence was better. Only in the area of customer retention did companies consistently report solid results.

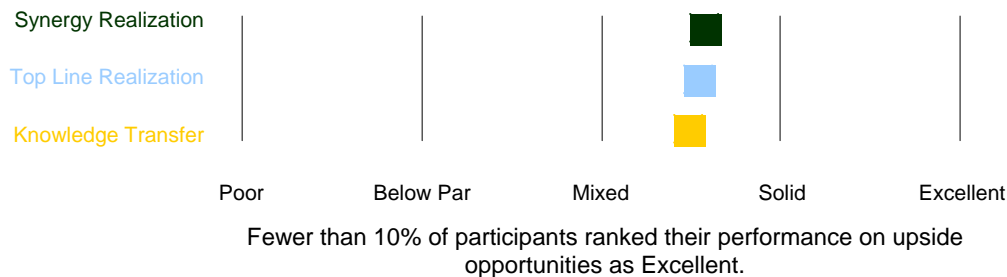
*“I’d like to see us get better at understanding the target’s best practices before we jump in and try to change them.”*

Survey Response

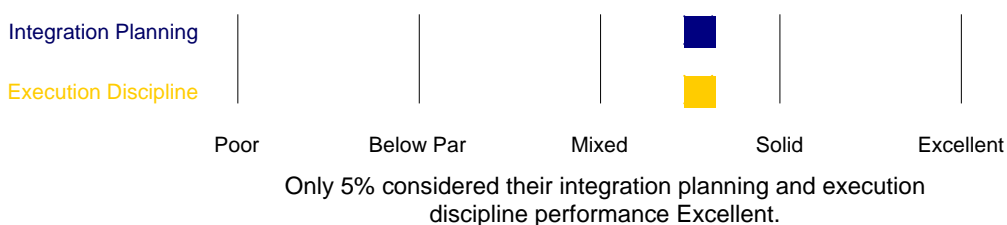
## MAJOR FINDINGS, CONTINUED

Companies reported mixed results capturing upside opportunities, particularly in the areas of best practice and knowledge transfer. Integration planning and execution discipline performance were also mixed. Taking a longer view, nearly half report that a substantial number of the deals completed 6 to 24 months ago still have not realized all their synergy potential. In our experience, these transactions are at significant risk of never fully realizing the anticipated synergies.

### Upside opportunities performance



### Planning and execution performance



## Lessons Learned

Given the mixed scores our survey participants gave themselves on integration planning and execution discipline, we were not surprised to see better planning at the top of the lessons learned. The need for speed, details and contingency planning were mentioned repeatedly.

- Among the things our respondents would do differently, at the top was the need for better planning. Human resource and culture issues followed closely. Comments included:
  - Need detailed plans and an aggressive timeline for integration and synergy capture
  - Set the new organization and reporting structure for every employee early in the process
  - Be thorough about assessing target culture before acquisition
- Other lessons mentioned:
  - Involve a broader group of functional teams in diligence
  - Vet the synergy plan thoroughly
  - Communicate, communicate, communicate
  - Plan for contingencies

Our experience has shown that (all things equal), the longer the synergy realization timeline drags out, the less likely a company is to ultimately realize the synergies in question. It is critical to prioritize synergy opportunities, adequately resource them, and then accelerate the realization effort and timeline. Any form of protracted (or “hockey stick”) execution thinking effectively undermines deal value.

Given the mixed deal results outlined earlier, it is perhaps not surprising that very few of our serial acquirer respondents consider their integration planning and execution performance to be “Excellent”.

*“It’s hard to transfer best practices—our organization was very resistant to adopting target company methods, even when they were clearly superior.”*

Survey Response

## SURVEY DEMOGRAPHICS

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Is your company public or private?

- 52% Public
- 48% Private

What is your company's annual revenue?

- 70% Greater than \$1 billion
- 19% Between \$500 million and \$1 billion
- 11% Less than \$500 million

What is your company's primary industry sector?

- 52% Manufacturing
- 26% Distribution
- 22% Other

What is your role in the M&A process?

- 15% Senior corporate line management - I approve deals for our company
- 33% Senior corporate staff (CFO, HR, Legal, etc.)
- 45% Senior corporate development
- 7% Other

Public and private companies were equally represented in the survey, with manufacturing and distribution most heavily represented.

The bulk of these companies have had significant M&A deal experience.

The bulk of responding executives had a “hands-on” role in the planning and execution of deal value capture.

# ABOUT THE KEYSTONE GROUP

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The Keystone Group was founded in 1991 to bring an execution focus to management consulting. The founders were dissatisfied with the typical consulting engagement that was long on analysis and ideas, but short on execution and delivering results. Working in small teams, we quickly define a range of solutions, build a plan of attack, and get on with delivering results.

## Our Services and Approach

Our M&A execution approach is simple, yet practical and proven. Most people think of M&A as only due diligence and deal-making - and that's where most people fail. Our experience has shown that M&A is not theoretical—or deal-making—problem ... it is an EXECUTION problem. Over years of hands-on experience, we have honed a proven approach to mitigating critical deal risks, accelerating synergy realization, and positioning the ongoing organization for sustained performance. Our clients, both strategic and financial buyers, engage us to support them throughout the overall process—from diligence through post-close execution.

## Delivering Execution Results

With over 75 deals worth over \$70 billion in value under our belts, we've helped companies successfully execute against deals of all shapes and sizes. Our unique, collaborative style is complemented by a proven approach, rapid decision-making model, and an easy-to-use toolset. Our experience can quickly put you on the 50-yard line, and get you to the goal line efficiently and effectively. We measure our success on how quickly our clients meet and exceed their synergy realization targets and we will put fees at risk to prove it.

*"For our next deal,  
Keystone will be  
the only firm we  
call."*

President

*"The last several  
months with  
Keystone have given  
our entire  
organization a sense  
of direction that no  
other consulting  
group has been able  
to provide us. We  
see Keystone as a  
valuable partner for  
the future...a group  
who understands our  
business and will be  
an on-going resource  
for our company."*

Executive Vice  
President & Chief  
Operating Officer

*"They are truly in a  
class by  
themselves."*

CFO

*"They brought order  
to the chaos."*

CEO

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This report is also available online at  
[www.TheKeystoneGroup.com](http://www.TheKeystoneGroup.com)

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