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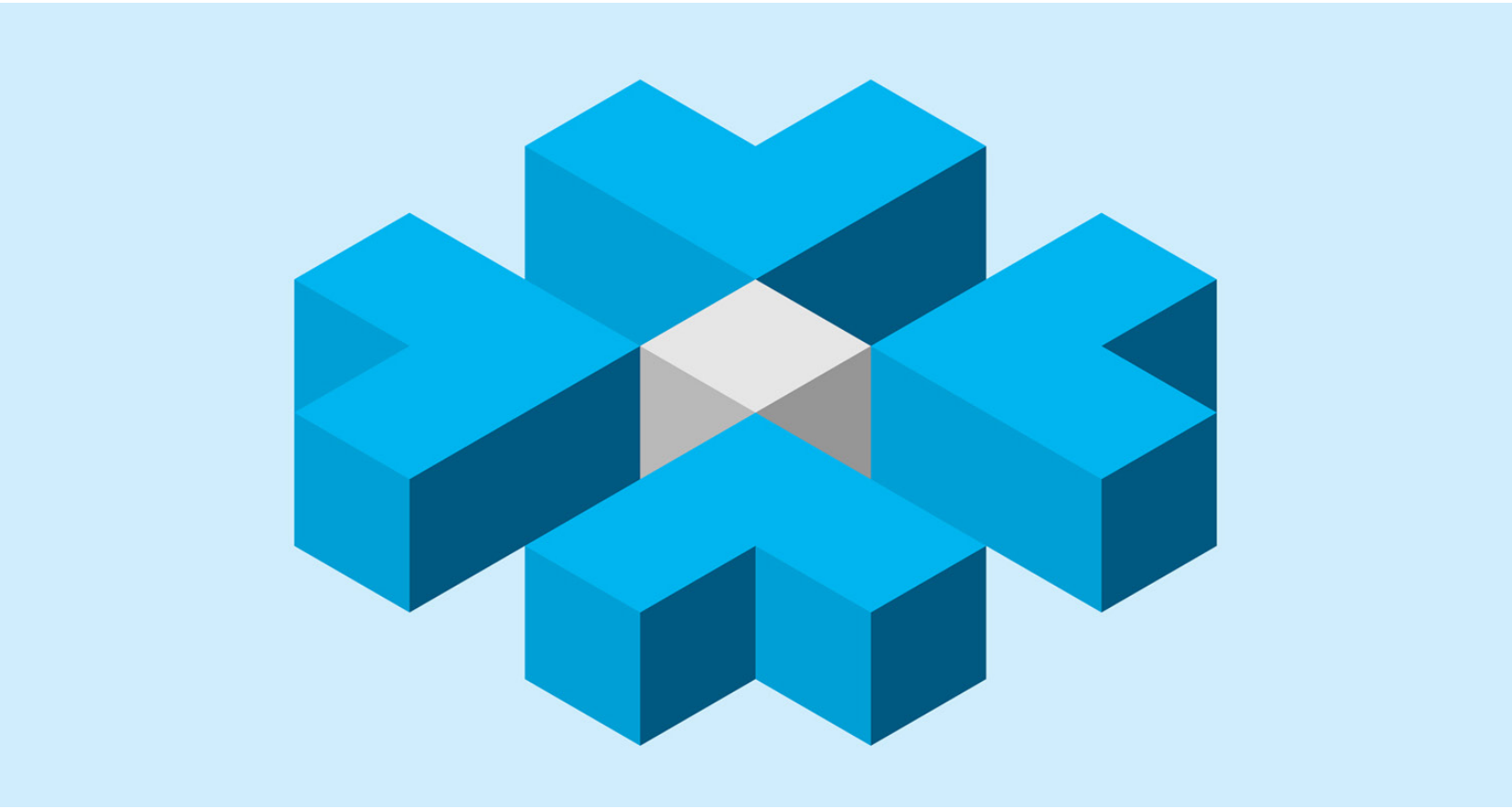
In conversation: Four keys to merger integration success

M&A experts share the integration practices that set the most successful large deals apart.



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The period after a large transaction closes determines whether the deal delivers the promised value, but integration is also the phase that business leaders struggle with the most. In this conversation, authors of the recent article "Post-close excellence in large-deal M&A"—McKinsey's Brian Dinneen, Christine Johnson, and Alex Liu, along with Becky Kaetzler—discuss their research into the practices that helped shape the past decade's most successful deals with communications director Sean Brown. An edited version of their conversation follows.

Sean Brown: How did you approach the research and why did you focus specifically on large deals?

Brian Dinneen: Much has been written about large-deal M&A. Some people have the perspective that such deals are disruptive to business momentum, rife with culture conflicts, and tend to destroy value. Others view them as opportunities to accelerate the strategy, reinvent their business models, or enter new markets and quickly gain scale. We weren't interested in whether generally large deals are good or bad but in finding out what makes them successful or unsuccessful.

We started with a decade's worth of large deals made by 2,000 global companies. We looked at the financial metrics, including growth and excess total shareholder returns [TSR] to see how the companies performed post-merger against their peers. We also looked at 29 of the largest deals within this data set and followed them from announcement through three years after they closed, studying investor transcripts, press coverage, and analyst reports to get a sense of the deal arc. Next came a survey of executives at 500 companies to understand the capabilities within those organizations. We then interviewed the leaders of the most successful and transformational deals to get the inside story: What were the pivotal points in the transaction? What practices did they employ and what lessons did they learn along the way? Finally, we tested the ideas with our advisory board of M&A executives.

Sean Brown: Why did you decide to focus specifically on the integration stage?

Brian Dinneen: Our survey showed that executives find integrating acquired companies to be the hardest stage in a deal. The pain points are felt most acutely during that post-close period because that's when you start to see integration milestones slipping and cultural conflicts emerging, such as misalignment among the top team.

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We also found that the first 12 to 18 months after close had a significant impact on the merger's ultimate success or failure. By the time a deal closes, the leaders have communicated their integration plans to investors and made promises about synergies, but we found little correlation between the excess TSR at close and company performance three years later. However, in the first 12 months to 18 months investors can see whether companies can make real organizational changes, deliver on the synergy targets, and maintain revenue growth. All these data points help investors get a better sense of whether the deal is likely to succeed or fail. This is so much the case that if we look at all the deal makers that outperformed their peers 18 months after close, 79 percent continue to outperform three years later. Conversely, of the deals that were underperforming peers 18 months after close, only 17 percent were able to turn the performance around.

Sean Brown: You ended up finding four core elements that deal leaders need to get right. Can you take us through them?

Brian Dinneen: The first element is protecting business momentum. We looked at the organic growth of the two companies in the first year after the merger. Are they able to maintain the growth or is there slippage? In successful mergers, 72 percent maintained organic growth but only 33 percent of ultimately unsuccessful deals managed to maintain growth momentum. The second element is the ability to accelerate synergies and integration. Leaders of successful deals deliver milestones on time, which reassures their organizations and investors. Those companies met 50 percent or more of their public synergy targets within the first year and in many cases exceeded those targets.

The third element is institutionalizing new ways of working. This means using the integration to rewrite the accountability system within the organization to ensure it aligns with the strategy, which often requires changing incentives. You also need to identify the processes that drive the deal's value, such as the go-to-market approach. It's important to be very clear about which processes need to change and dedicate resources to managing the necessary organizational and behavioral shifts. When we talked to M&A practitioners, 60 percent told us that they wished they had spent more resources on culture and change. In successful deals, companies put significant investment into that.

The fourth element is catalyzing the transformation, which means using the merger not just to gain economies of scale but to reposition yourself in the market, accelerate your strategy, and create a new cost structure. Among the companies we studied, those that went beyond integration to transformation delivered 10 percent or more excess TSR, significantly outperforming their peers over the life of the deal.

Sean Brown: Do some of these elements have higher importance than others?

Brian Dinneen: The first three are essential—you have to get them right. The last one is optional. If you want to deliver significant outperformance and capture the deal's full potential, you need to catalyze a transformation.

Alex Liu: I would add that within the first three, protecting base business momentum stands above the other two. No amount of synergies will make up for a disruption to the top line. Investors want to see both companies' revenues continue to grow.

Sean Brown: Your research identified specific practices that those who led successful integrations applied. Christine, how did deal makers maintain business momentum?

Christine Johnson: There is a common phenomenon in large-deal M&A that we call "the year-one dip," wherein companies witness a drop in their base revenue as they pursue merger synergies. Yet we found that more than 70 percent of the deals that were ultimately successful skipped that first-year dip. When we explored how they did that, we saw two distinct practices. The first is protecting the base at all costs, which requires relentless prioritization of current-business performance. The integration leader of a large healthcare industry merger told us that every meeting on synergies

throughout the integration process would start with an update on the core business.

The other practice is shifting out of the functional mindset in integration planning and putting yourself into the shoes of your customers, employees, and other key stakeholders. Functions often manage their swim lanes efficiently, but great performance requires intersecting those functional plans with the stakeholder lens and understanding how the integration will affect customers, suppliers, and others critical to business performance. Let me give you an example of an integration where cross-sell synergies were paramount. When the company looked at the planned functional changes, it realized that the sales force would experience a lot of disruption in the first 100 days. Consequently, they decided to delay a site consolidation and the rollout of a new CRM system, which were important to achieving cost synergies, so the sales team could focus on cross-selling. They adapted the sequence of changes to minimize disruption to core business momentum and improve the experience of core employees.

Sean Brown: The next element is about acceleration. How should companies go about this?

Christine Johnson: So while you keep the two companies going, the integration team has to focus on capturing the deal value. The first practice we found among companies that do this well is to make sure that line leaders are accountable for the synergies. At a philosophical level, they have to believe in the plans for creating value and own their targets. From a practical standpoint, those goals have to be hardwired into leaders' annual operating plans or budgets. You own the numbers, and you own the plan.

Now, handing responsibility to business unit leaders does not mean the integration team can disappear. In fact, having a strong integration team for the life of the deal, which could be a two-year window, is critical to post-close excellence. Which brings us to a second practice among successful larger mergers, which is implementing value-based governance to track synergies. That means taking departments through a structured process to prove the business case and align the resources to achieve it, then tracking that through the P&L.

This is painstaking work and we often see companies pivot this responsibility to their selling, general, and administrative [SG&A] expense groups soon after close: "It's in the budget, we're good. The leaders have their targets." To be among the companies that achieve post-close excellence, you need to continue resourcing this value-capture team. Companies that get this right talk about the powerful role that the value-capture leader or team within finance plays throughout the life of the deal. These colleagues keep the foot on the gas pedal. They are relentless and rigorous about ensuring that the value promised in the deal rationale finds its way into the statement.

Sean Brown: This process probably leads to the next one, which is institutionalizing new ways of working. Becky, can you take us through that?

Becky Kaetzler: Early in integration planning, we often see clients design an organizational structure that they hope will enable the deal's strategic goals. As time goes by, however, the impetus to bring all the colleagues into the new structure diminishes. It's not just about reporting lines and what function sits where but how the work gets done on a day-to-day basis, from both process and behavioral perspectives. It's important to introduce two initiatives as early as possible: building the new business processes and ensuring that behaviors critical to capturing the value in the merger are nonnegotiable.

Let me give you an example on the behaviors point. In one merger where the focus was on cross-selling, the client needed to get sales reps, who before were competitors, to collaborate, share leads with one another, and sometimes go jointly to customers with a broader array of products. We started bringing those teams together as soon as possible so they could get to know each other and learn each other's products. We incorporated some levers into their compensation programs to drive cross-selling and then spent a lot of time with

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the sales managers to ensure they were role-modeling the behaviors for the sales force. But it’s not enough to tell your colleagues to start doing things differently—you need to give them resources, training, and processes or metrics that will help them measure their performance.

In terms of rewiring business processes, things can become complicated. You can build a new structure, but if you don’t run water through those pipes in terms of how the work is actually done, it can cause destabilization after the deal closes. So as early in the integration as you can, we recommend getting colleagues in their respective departments to put down five things they do daily, then talk about how they will perform those tasks in the new structure. We ask them to role-play how certain decisions will be made or questions answered. That starts building the skills and critical processes to support the new ways of working. In one integration we supported, the capital allocation process was critical to the deal value. First, the leadership team role-played a set of decision meetings while applying the new capital-allocation process. “How will we make sure this process leads to timely decisions? How do we handle conflict?” Then they cascaded the process down through the organization.

Sean Brown: What do you do when the two companies are culturally incompatible and their ways of working are very different?

Becky Kaetzler: It may seem like there is nothing you can do—“We’re just not compatible.” But if you go deeper, you can build an understanding of the core elements of culture in each organization, the similarities and strengths you can build on together, and identify the differences. For example, if one organization is consultative and likes a lot of discussion and the other prefers to make quick decisions and run with them, that can create friction, but it’s something you can work on.

Sean Brown: The final element is catalyzing the transformation. Alex, can you start by explaining what that means in the context of merger integration?

Alex Liu: It’s about leveraging the deal to build new capabilities and taking value creation to the next level. The companies that do this right dedicate significant management focus to this for multiple years. Integration in and of itself is hard work; transformation requires an even greater focus, intensity, and top-team commitment. A healthcare company we worked with, for example, set a vision to be the absolute leader in healthcare solutions and

services. They not only launched a dedicated effort to exceed the publicly announced synergies but announced a multiyear transformation to drive further efficiencies and change the company's operating model. That was probably a five-year commitment, and if you were in the room with the top team, you would have heard that commitment from every leader.

The second practice is selecting, expanding, and building on the combined capabilities across the two organizations. In one recent merger, one of the organizations had a stellar revenue-management capability, with a strong sales force. Immediately upon closing, the integration team designed a program to roll that revenue management capability across both organizations. That resulted in significant growth of the top line not only during the synergy window but for years to come.

One concept to keep in mind is the need to refuel for the transformation wave. In the initial phase, it's important to appropriately staff the integration to protect the base business, pursue initial synergies, and combine the two organizations, which typically takes 12 to 18 months in large deals. After that, the organization starts to get fatigued because integrating two large companies requires a tremendous amount of work. You then need to go team by team and goal by goal to understand, "Do we have the right amount of resources for the next wave? Do we need to rotate talent to provide a new injection of energy, focus, and commitment?" We find that in successful mergers, the companies assess the resources at the 12- to 18-month mark to understand how to keep the fire burning as they move through the transformation.

Sean Brown: You have framed the research in the context of large-deal integration. Do the same elements apply to smaller deals?

Alex Liu: Maintaining business momentum is a universal principle and it's especially important in smaller deals where you may not be acquiring the company for cost synergies but for its people, technology, and intellectual property. Accelerating the integration is also universal: you want to get off to a fast start in capturing the cost and revenue synergies and establishing new capabilities to signal the new way to the organization. Institutionalizing those new ways of working is also important in

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smaller deals so the acquired company understands the new expectations and corporate processes. The last one, as Brian said earlier, is a choice.

Brian Dinneen: For programmatic acquirers, it may not be one deal but a series of deals that catalyzes a transformation. You get to a culmination point where launching a transformation is possible.

Sean Brown: How often do you find companies use large transactions to transform their businesses?

Alex Liu: If you did a literature search of the largest 100 or 150 recent deals, you would see terms like "industry leader changed the game." Many companies talk about it, but not all large deals succeed. It's a mixed track record because organizations often lack a thoughtful approach to crafting the transformation program. That is partly why we undertook this research—to help increase the batting average on large deals.

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