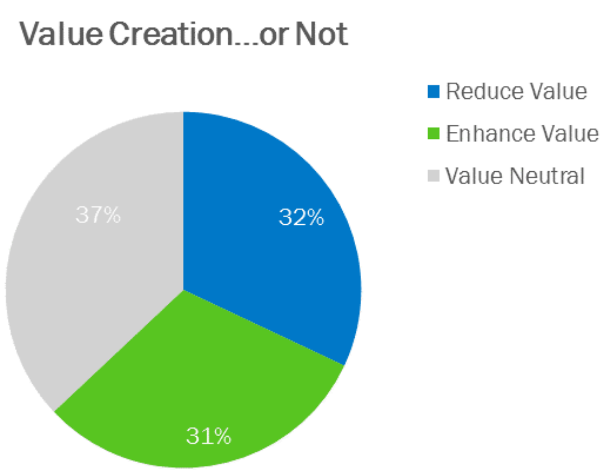
Solving the Value Creation Dilemma - How to become an "Extraordinary Acquirer"

A recent McKinsey article crossed my desk this week. The article highlighted value creation inherent in organic growth versus growth by acquisition. The author noted that over a 15-year period, companies with more organic growth generated higher shareholder returns than those relying heavily on growth by acquisition. Curious about these findings, I delved in to find an explanation, and to determine whether there was an argument in support of growth by acquisition.

Given my perspective (Valitas Capital is, after all, an M&A advisory firm), you may not be surprised to learn that I did find a persuasive argument. Shareholder value creation through an acquisition strategy can be achieved, particularly where an acquirer focuses effectively on post-acquisition integration. In fact, a 2014 academic paper published in the Journal of Financial Economics identifies a category of "Extraordinary Acquirers", companies that consistently create shareholder value through their acquisitions.

In examining a sample of more than 12,000 transactions over 4,128 firms, the authors concluded that extraordinary acquirer returns could not be explained by target or deal characteristics, and were not CEO or industry specific. They suggested, rather, that this persistent shareholder value creation might reflect "acquisition skill… [such as] expertise residing in internal M&A/corporate development teams, or particular practices in terms of post-merger integration" (PMI).

A recent KPMG report provides further support for this thesis. The report, aptly titled "Why Most Acquisitions Fail", suggests that more than 60% of M&A deals don't deliver on their expected value, with 32% of deals actually eroding shareholder value, and attributes this failure primarily to poor post-deal execution (or PMI).



Source: KPMG Global Research

The KPMG authors point to “common integration errors” including:

1. Inadequate integration planning
2. Lack of post-merger “program” leadership
3. Lack of formal and fast decision making process
4. Loss of focus on everyday operations
5. Major synergies not driven through
6. Customers get forgotten

We would add to this list:

7. Lack of awareness of organizational/culture differences

8. Lack of accountability across departments for integration success

Value enhancing deals (31% in the KPMG sample), on the other hand, consistent with the “Extraordinary Acquirer” thesis, can attribute their success in large part to effective PMI, with a management team that creates an integration plan to address the issues listed above.

Being an “Extraordinary Acquirer” isn’t the result of a particular CEO or senior leadership team’s abilities but rather, is tied to their ongoing commitment to effective deal integration. PMI is a key part of the deal that is sometimes just the subject of lip service, and often overlooked outright.

A key step to becoming an "Extraordinary Acquirer" is to create a measurable PMI strategy tailored to deal imperatives, cultural requirements, and organizational capabilities. In effectively building and executing on such a strategy, companies reduce complexity, mitigate risks, speed integration and enable shareholder value creation.

So where does this leave us? Certainly, given the rate of failure to deliver shareholder value through acquisition, organic growth is, on its surface, an attractive option, albeit a tough one to pursue in the current low organic growth environment. However, firms that invest in building M&A skill, including a framework for PMI, can successfully create shareholder value through acquisition. They might even become “Extraordinary Acquirers”.

Thanks to Tim Morton, Valitas Advisor, for lending his expertise to this article. Tim is the Managing Partner and founder of Prompta Inc., a leading consultancy, and has 20 years of experience successfully leading transformational change for over 20 organizations across 12 industries. He is a post-merger integration (PMI) specialist

having enabled mergers, acquisitions and divestitures of valued at $32 billion in aggregate.