Valitas Insights: Abandoned Acquisitions – Why Do M&A Deals Fail?

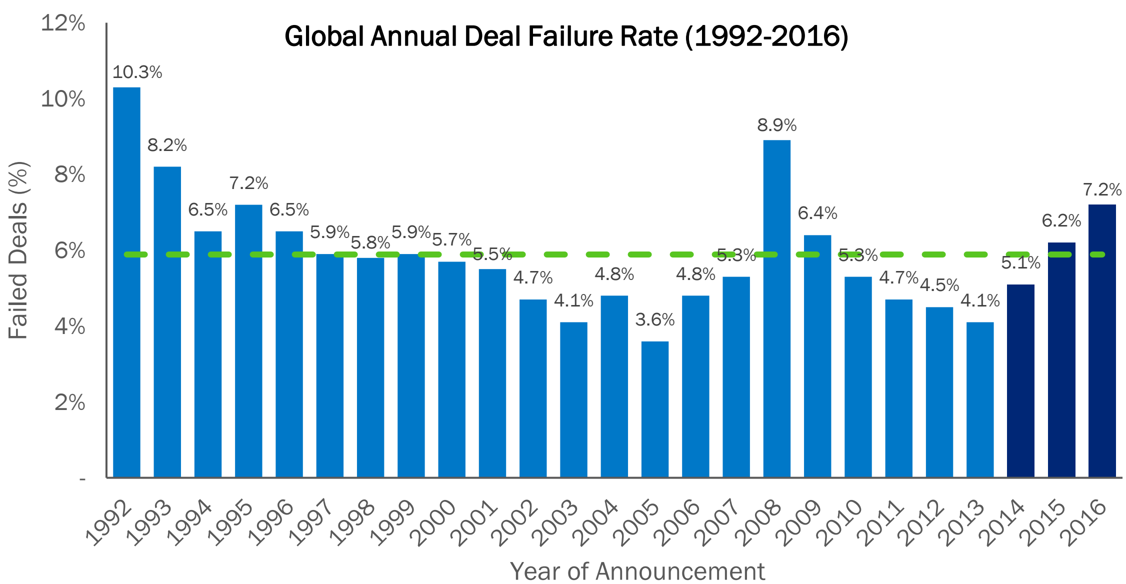
Part 1: Pre-Acquisition Deal Failure

This article is part 1 of a 2-part series about why M&A deals fail to succeed in today's bull market. Part 1 considers M&A deals that fall apart during the pre-acquisition phase, comparing failure rates across different geographies and industries, as well as in private versus public companies.

In today's hot market, business owners are jumping on the bandwagon to sell their companies, looking to take advantage of the large multiples being paid by buyers. With baby boomers aging and retirement on the horizon for many, more businesses are for sale now than ever before.[1] However, wanting to sell your business and actually selling your business are two different things. Some sources estimate that 80% of small and middle market business owners who put their companies up for sale never close a transaction, either having the deal fall apart after engaging with a potential buyer or never finding a potential buyer altogether.[2] IntraLinks teamed up with Cass Business School to explore the former scenario, digging deeper into why M&A deals fall apart after a potential buyer has been engaged. Drawing on over 78,500 M&A deals spanning the last 25 years, as well as on the insights of 40 global M&A professionals, the study identifies trends and contributing factors underlying pre-acquisition deal failure.

M&A Deal Cycles

The percentage of M&A deals that fail to close has increased annually since 2013, reaching 7.6% in 2016, the highest rate since the 2008 financial crisis.[3] Historically, the rate of deal failure has hovered between 4 and 10%.



[1] Axial, Top 10 Ways an M&A Transaction Can Go Wrong
[2] Ibid.
[3] IntraLinks, Abandoned Acquisitions: Why Do Some M&A Deals Fail To Complete

In terms of geography, targets in the Asia Pacific region (APAC) exhibit the highest deal failure rate, while Latin American (LATAM) targets exhibit low failure rates.[4] In terms of cross-border deals, Latin American acquirers are highly unsuccessful in closing deals with APAC and North American targets.[5]

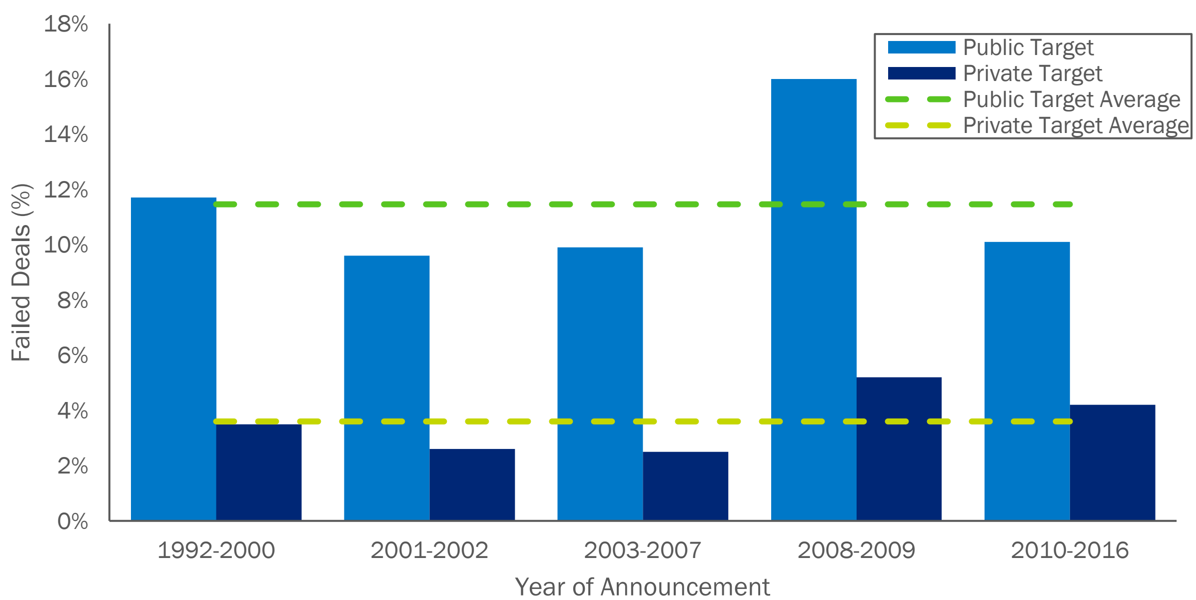
Table 1: Deal Failure Rate by Acquirer-Target Region Pairs[6]

Target Region		Acquirer Region				
		APAC	EMEA	LATAM	NA	Total
	APAC	7.3%	4.7%	18.6%	6.1%	7.1%
	EMEA	4.7%	4.2%	6.0%	4.1%	4.2%
	LATAM	3.6%	2.4%	4.3%	5.0%	4.0%
	NA	4.2%	4.6%	12.7%	6.6%	6.4%
	Total	7.1%	4.2%	5.4%	6.3%	5.7%

Public vs. Private M&A Targets

M&A deals involving public targets have a higher deal failure rate (11.1%) than those with private targets (3.7%).[7] For private business owners, this finding emphasizes the value in having access to an expansive network of potential buyers during a sale process, with the rate of deal failure sitting at just 3.7% after the engagement of a potential buyer.

Global Average Deal Failure Rate, by Public/Private Target (1992-2016



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[4] Ibid.
[5] Ibid.
[6] Ibid.
[7] Ibid.

So why do private targets have a substantially higher success rate in closing transactions? IntraLinks identified the following predictors of success for public and private targets.

Table 2: Predictors of Deal Success by Private and Public Target

	Private Target Deals	Public Target Deals
Acquirer Termination Fees	✓	✗
Target Termination Fees	✗	✓
Size	✓	✓
Approach	✗	✓
Advisors	✗	✓
Consideration	✓	✓
Liquidity	✓	✗

Simply put, deals involving public targets are more successful if the deal includes negotiated termination fees, a target that is smaller than the buyer, agreed or solicited terms, multiple advisors and an all-cash consideration. Similarly, private target deals are more successful when the deal includes negotiated reverse break fees, a target that is smaller than the buyer, a liquid acquirer and an all-cash consideration.

The predictors outlined above are intuitive. It would be feasible to assume that the existence of termination fees would help to keep deal momentum driving forward. For instance, in an M&A deal, a break fee would serve to protect the buyer from losing time and resources on diligence. Contrarily, a reverse break fee would protect the seller from a buyer unable to secure the required financing. Having an all-cash consideration is logical also, as it allows shareholders to clearly measure the value of what they are being offered at the time of the transaction.

Impact of Unforeseen Events

The study also examines the impact of catastrophic events on the rate of deal failure. The analysis examines three major events in the last 10 years:

1. The Lehmnan Brothers Bankruptcy
2. The September 11th Terrorist Attacks
3. UK Brexit Referendum Results

The results indicate that while 9/11 and Brexit both resulted in political shock with long-term effects, there was no immediate impact on the rate of deal failure. However, in the wake of the Lehman Brothers bankruptcy, the rate of deal failure spiked to 19%[8]. This is because there was a sudden collapse of market confidence in the liquidity, funding and solvency of financial institutions, which led to frozen credit markets and a lack of financing options for M&A activity.[9]

[8] Ibid.
[9] Ibid.

Other Trends

Another interesting geographical trend to note is that China and Australia have the highest percentage of failed deals while Russia, Japan and France exhibit the lowest rate of deal failure.

In terms of failure rate across specific sectors, real estate, energy and power deals have the highest propensity for failure, while consumer, healthcare and industrials have the lowest.

Table 3: Deal Failure Rate by Target Region and Industry[10]

		Target Industry								
		Materials	Real Estate	Energy	Financials	TMT	Healthcare	Industrials	Consumers	Total
Target Region	APAC	10.4%	7.9%	8.6%	7.8%	6.9%	6.9%	6.1%	5.2%	7.1%
	EMEA	4.6%	5.8%	5.6%	6.4%	3.8%	3.3%	3.7%	3.0.%	4.2%
	LATAM	6.8%	2.8%	3.4%	3.5%	4.4%	0.0%	3.2%	3.9%	4.0%
	NA	8.0%	6.6%	6.1%	5.2%	6.1%	6.3%	6.6%	7.7%	6.4%
	Total	7.7%	6.8%	6.3%	6.2%	5.5%	5.5%	5.1%	4.8%	5.7%

Table 4: Deal Failure Rate by Country[11]

Target Country	Failed Deals (%)
China	12.9%
Australia	11.9%
Singapore	9.2%
Hong Kong	8.6%
Malaysia	7.7%
United States	6.4%
Canada	6.3%
United Kingdom	4.8%
Norway	4.8%
Netherlands	4.7%
South Korea	4.2%
Italy	4.1%
Sweden	3.9%
Brazil	3.8%
Spain	3.8%
India	3.5%
Germany	3.0%
France	2.5%
Japan	2.2%

While it is important to understand the trends behind pre-acquisition deal failure, it is equally important to be cognizant of its empirical nature. As much as transactions are reliant on financial models and quantitative analysis, they are equally reliant on intuition, momentum and grit. Some M&A deals fail because shareholders do not accurately price their equity consideration while others fail simply due to unrealistic value expectations from management.

This article has covered deals that fail during the pre-acquisition phase, but what about completed deals that fail in the subsequent months and years after closing? Stay tuned for part 2 of this series, which will investigate why ‘successful’ deals oftentimes lead to a destruction of value…

[10] Ibid.

[11] Ibid.