THE MERGER & ACQUISITION LEADER'S PLAYBOOK

A PRACTICAL GUIDE TO **INTEGRATING ORGANIZATIONS**, **EXECUTING STRATEGY**, AND **DRIVING NEW GROWTH** AFTER M&A OR PRIVATE EQUITY DEALS

GEORGE B. BRADT
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EXECUTIVE SUMMARY

Those leading through a merger, acquisition, or the like do so to create more value faster. They look for revenues to double or more on the way to returning many times their initial investments. Maybe you're driving or leading the investment. Maybe you're leading the business itself or playing a supporting role. In any case, you need a leadership playbook for the merger or acquisition.

This is that playbook, the one we've used as investors, leaders, and supporters. It gives you the frameworks, tools, and sub-playbooks you need to create that value faster. Our overarching approach is to work through customers, capabilities, and costs—in that order. First, figure out how you're going to win with customers. Then build the leadership, team, and capabilities required for that. Fund those efforts by cutting less valuable efforts and their associated costs.

This is how we've created value faster against a backdrop of others failing to deliver the desired results 83 percent of the time. In a *Harvard Business Review* article, Kenny Graham noted that "between 70 and 90 percent of acquisitions fail."[1] A KPMG M&A study found that 17 percent of deals added value, whereas 30 percent produced no discernible difference and 53 percent destroyed value.[2]

This book lays out the seven sub-playbooks and a prototypical order that comprise the M&A leader's complete playbook. We also include summaries of tools to help along the way, each of which has an editable download available at www.primegenesis.com/tools.

The seven sub-playbooks are:

1. The Strategic Playbook
2. The Commercial Playbook
3. The Operational Playbook

[1]Graham, Kenny, 2020, "Don't Make This Common M&A Mistake." *Harvard Business Review* (March 16).
[2]KPMG Mergers and Acquisitions: Global Research Report 1999.

4. The Financial Playbook
5. The Governance Playbook
6. The Organizational Playbook
7. The Change Management Playbook

As this is inherently a non-linear process, parts of each of these playbooks need to be deployed at different times in different mergers or acquisitions. With that in mind, adapt this prototypical order for your particular situation.

Concept => Research => Investment Case => Negotiation => Deal/ Due Diligence => Contract => Close => Integration => Acceleration => The Next Normal => The Next Chapter

	The Strategic Playbook	The Commercial Playbook	The Operational Playbook	The Financial Playbook	The Governance Playbook	The Organizational Playbook	The Change Management Playbook
Concept	The Investment Case					Culture	Integration Leader
Research		Organic Revenue Growth	Cost Optimization	Deal/ Due Diligence			
Investment Case					Regulatory	Incentives	Change Management
Negotiation			Operational Excellence: Supply Chain, Distribution, Continual Improvement				
Deal/Due Diligence	Focus			Financing	Financial	Leadership	Communication
Contract		Customers					
Close	Plans			M&A	Board	People	Announcement
Integration		Marketing & Sales					
Acceleration	Innovation		Technology			Politics	Adjustments
Next Normal							

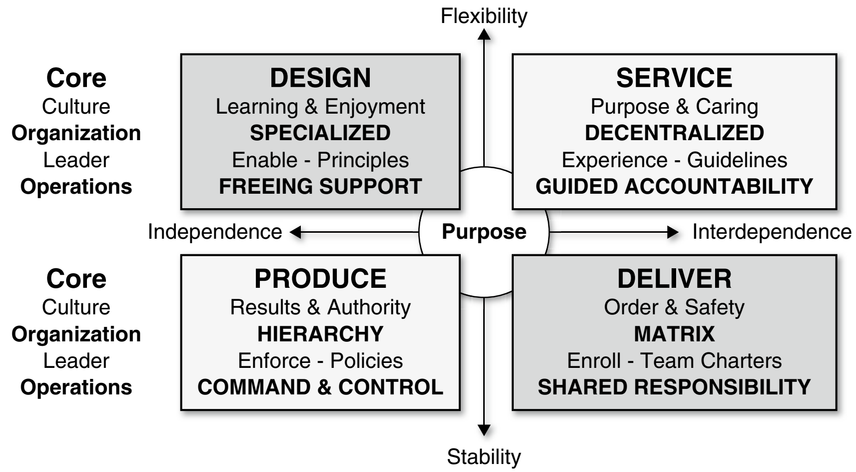
The Strategic Playbook

Be clear on what you want out of an acquisition or merger, how it would fit with what you've already got, and what you're willing to give up to get it. Then broaden your perspective to look at different possibilities before narrowing on the few best candidates and putting together investment cases for them.

Before you attempt to acquire and integrate another entity, it's best to know your own entity first. When leaders have in-depth knowledge of their own core focus and strategic, organizational, and operational processes as well as their culture, they are far better positioned to leverage and blend the combined strengths of their own and other entities.

Align on the core focus of the new organization: design, production, delivery, or service (see Figure I.1). That choice dictates the nature of your culture, organization, and ways of working.

FIGURE I.1 The Core Focus



Similarly, understand the business context in which you're operating. Your strategy revolves around a set of choices about the markets, segments, and customers you'll serve. Know and understand them better than anyone else.

The fundamental U-shaped profit curve for almost every industry is that the vast majority of profits accrue to the most innovative who sell fewer "units" at higher prices and margins at the top and to the low-cost producers who make higher than average margins at the "market" price.

Choose whether your innovation will drive higher prices—most likely in design or service-focused organizations—or drive down your production or delivery costs.

If you can't define the value you are seeking to create, it doesn't exist. Get clear on the desired outcomes for your markets, segments, customers, organization, shareholders, and people—as well as *how* new value is going to be created with choices around where you will:

- **Win** by being predominant/top 1 percent, superior/top 10 percent, strong/top 25 percent

- **Not lose** by being above average/competitive, good enough/scaled, or
- **Not do** by outsourcing or not doing at all

Play this out through the investment case fundamentals:

1. Pay fair value for what company is currently worth.
2. Grow top-line (organically and inorganically) innovating with customers through people.
3. Make operational–operational engineering improvements, cutting costs.
4. Invest in top-line and bottom-line enablers including technology to accelerate progress.
5. Improve cash flows and pay down debt.
6. Exit or recapitalize when this round of value creation is done.

We look at this in the four chapters of the strategic playbook:

Chapter 1: **The Investment Case:** The Heart of the M&A Leader's Playbook
Chapter 2: **Focus:** It Drives Everything Else
Chapter 3: **Plans:** Strategy Precedes Execution
Chapter 4: **Innovation:** A Fundamental Strategic Choice

The Commercial Playbook

One private equity firm looked at its 25 years of deals across its eight separate funds. They calculated that 30 percent of their portfolio companies' revenue growth over time had been organically fueled by their own innovation, marketing, and sales while 70 percent came from further acquisitions. In most cases you'll need both. Organic revenue growth is harder and riskier, but you keep all of it.

There's an important difference between value creation and value capture. Value is created when a customer pays someone for a product or service that costs the supplier less than the price paid. This is why you have to think customer-back to create value by innovating to provide more valuable products and services than your competitors do.

Don't read this wrong. There's nothing wrong with capturing value from competitors—generally by undercutting their price to take market share. This is why the price of everything gets competed down to its marginal cost over time. You don't want to be the ultimate winner of the race to the bottom. But you can make a lot of money winning some of the stages along the way.

We didn't include marketing and sales in the core focus chart shown in Figure I.1. That chart is derived from Michael Porter's value chain work in which he suggests every company designs, produces, sells, delivers, and services.[3] It turns out the most successful companies focus on one of design, production, delivery, or service in addition to marketing and selling.

We look at this in the three chapters of the commercial playbook:

Chapter 5: **Organic Revenue Growth**: So Valuable

Chapter 6: **Customers**: From Which All New Value Flows

Chapter 7: **Marketing and Sales**: Which Every Organization Must Do

The Operational Playbook

The operational processes that worked before your merger or acquisition may not be adequate to deliver your future ambitions. Maintain and evolve the best of your current processes while leveraging innovation and technology to layer in the new processes required to deliver the needed cost reductions and fuel revenue growth.

Essentially, you're going to need to craft, implement, and manage four plans concurrently:

- Resource allocation and plan (requirements, sources, application): Human, financial, technical, operational
- Rules of engagement across critical business drivers
- Action plan (near-term and long-term): Actions, measures, milestones/timing, accountabilities, linkages
- Performance management plan: Operating and financial performance standards and measures

[3]Porter, Michael E., 1985, *Competitive Advantage: Creating and Sustaining Superior Performance* (New York: Simon and Schuster).

We look at these in the three chapters of the operational playbook:

Chapter 8: **Cost Optimization:** To Free Up Resources to Fuel Commercial Growth

Chapter 9: **Operational Excellence:** Supply Chain, Distribution, Continual Improvement

Chapter 10: **Technology:** Because All Companies Are Technology Companies Today

The Financial Playbook

Do the deal in a way that reduces your risk of being part of the 83 percent of mergers and acquisitions that fail to deliver the desired results. The first of the many investments you need to get a return on is the purchase price. It is better not to pay enough and lose a deal than to over pay and "win" one of the 30 percent that take a lot of work for no gain, or, even worse, one of the 53 percent that actually destroy value.

The starting point for your deal should be a fair value for what the company is currently worth based on current cash flows. This would reward the seller for what they've built and give you all future value creation. Of course, in the real world, others may be willing to give the seller a portion of the estimated future value. Couple that with some overestimation of possible future value and ego, and it's easy to see how people bid more than they should to "win" bidding contests.

Your real investment is different depending on how you finance the deal. Consider options for funding beyond cash, including equity, seller funding or earnout, and debt in the form of loans, bonds, credit lines, bridge financing, mezzanine, or subordinated debt.

Due diligence is your chance to check your assumptions. If you put a breakup fee in the deal, you did that to allow you to walk away if appropriate. Historically, 83 percent of the time others should have done that. Do due diligence in multiple phases to manage resource allocations (e.g., time, costs, opportunity). Do some before negotiating, some while negotiating, and some between contract and close to avoid wasting much time and resources on low probability or low-impact deals.

Learn as much as you can about the strategic, organizational, and operational processes and culture of the entity you're acquiring.

Don't just take third parties' opinions; be active in learning as much as you can—as soon as you can.

1. Check your assumptions about the value creators that can enhance competitive advantages, increase impact, and enable top-line growth with *customers*.
2. Check your assumptions about cultural compatibility. Because if you can't make the *people* work, nothing else matters.
3. Check your assumptions about synergistic *cost* reductions that can fuel investment in the value creators.
4. Look for other *investments* that will be new and needed for the combined company and need to be planned for and part of the strategy.
5. Then make a go or no-go *decision* being clear on the advantage of cutting your losses before they become material.

We look at this in the three chapters of the financial playbook:

Chapter 11: **The Deal/Due Diligence:** Iteratively

Chapter 12: **Financing the Deal:** The Different Options

Chapter 13: **Further M&A:** Enabling Commercial and Operational Success

The Governance Playbook

You need a license to drive a car. And you need licenses to do mergers and acquisitions. Those licenses come from government regulators, banks, and other investors and get translated and managed by your board.

We look at this across the three chapters of the governance playbook:

Chapter 14: **Regulatory:** And the License to Play

Chapter 15: **Financial Governance:** Always Necessary

Chapter 16: **The Board:** And Its Multiple Roles

The Organizational Playbook

The root cause of many mergers' success or failure is culture. Choose the behaviors, relationships, attitudes, values, and environment (BRAVE) that will make up your new culture. Make sure you are encouraging helpful things and discouraging unhelpful things with your incentives and other tools. Also, as you're choosing key leaders and the broader team, keep in mind that you are inviting people into the new culture, noting who really accepts your invitation in what they say, do, and are.

Take a hard look at the combined organization's skills and capabilities through the lens of the new core focus and strategy to determine if any critical capability sets are missing or misaligned. Not only look at the people, plans, and practices, but also pay particular attention to how well you are performing in the markets, segments, and customers you've decided to pursue. Quickly move to bridge any gaps that exist.

Start by defining the right structure and roles to execute on your mission. Be specific about talent, knowledge, skill, experience, and craft requirements for success in each key role, and then match them with the right people.

- *Innate talent*: Either born with or not
- *Learned knowledge*: From books, classes, or training
- *Practiced skills*: From deliberate repetition
- *Hard-won experience*: Digested from real-world mistakes
- *Apprenticed craft*: Absorbed over time from masters with artistic care and sensibilities

We look at this across the five chapters of the organization playbook:

Chapter 17: **Culture:** The Underlying Root Cause of Nearly Every Merger's Success or Failure

Chapter 18: **Incentives:** Show Me How They're Paid and I'll Tell You What They Do

Chapter 19: **Leadership:** Starting with the Core Leadership Team

The Change Management Playbook

We've all seen organizations acquire other organizations and then run them as wholly owned, separate entities. You can't possibly realize synergies out of separate organizations. Synergies must be created together by teams looking beyond themselves to new problems they can solve for others. This is why a deliberate and detailed integration plan that spans across organizational, operational, strategic, and cultural issues is essential.

All lasting change is cultural change in attitudes, relationships, and behaviors following a point of inflection change in environment or situation and ambition and objectives. Manage that cultural transformation purposefully, deliberately, actively, and in detail. Have a cultural transformation plan in place. When you merge cultures well, value is created. When you don't, value is destroyed.

Implement systems to track, assess, and adjust daily, weekly, monthly, quarterly, and annually: Don't confuse communication with operating cadences. Avoid the public company sprint to do things just ahead of quarterly earnings calls, instead staying ahead of the curve at all times.

- Balanced scorecard (e.g., financial, customer, internal business processes, learning and growth)
- Finance (e.g., revenue, cash flow and cash conversion cycle, earnings before interest, taxes, depreciation, and amortization [EBITDA], return on investment)
- Customer (e.g., sales from new products, on-time delivery, share, customer concentration)
- Internal business processes (e.g., cycle time, unit cost, yield, new product development)
- Learning and growth (e.g., time to market, product life cycle)

We look at this across the five chapters of the change management playbook:

Chapter 22: **Integration Leadership:** Start Here

Chapter 23: **Change Management:** Leading Through the Point of Inflection

Chapter 24: **Communication:** Everything Communicates

Chapter 25: **Announcement Cascade:** Emotional, Direct, Indirect

Chapter 26: **Adjustments:** Because You'll Need Them

Prototypical Order

Chapter 27, "Prototypical Order," covers the last step: preparing for further growth and transformation like the next exit or other "event" as a platform company or bait for strategic buyer. When preparing for an exit, get the story right:

- Strategically: Organic revenue growth; Other M&A
- Organizationally: Buyable management team; Capabilities valuable to others
- Operationally: Buyable infrastructure (Assets, data, IT systems, financial reporting;) Processes; New product development capabilities
- Personally: Making yourself invaluable to the next owners

What really matters is how you influence others and the impact you all make together. Do start with the context and industry landscape. Do align people, plans, and practices around a shared purpose to create commercial and other value. Do the cost-cutting required to free up the resources you need to strengthen the combined entity's culture and strategic, organizational, and operational processes. Do that, thinking customers, then capabilities, then cash, and the merger and acquisitions you lead will go well.

PART I

The Strategic Playbook

CHAPTER I

The Investment Case: The Heart of the Merger and Acquisition Leader's Playbook

	The Strategic Playbook	The Commercial Playbook	The Operational Playbook	The Financial Playbook	The Governance Playbook	The Organizational Playbook	The Change Management Playbook
Concept **Research** **Investment Case**	The Investment Case	Organic Revenue Growth	Cost Optimization	Deal/ Due Diligence	Regulatory	Culture Incentives	Integration Leader Change Management
Negotiation **Deal/Due Diligence**	Focus		Operational Excellence: Supply Chain, Distribution, Continual Improvement	Financing	Financial	Leadership	Communication
Contract **Close**	Plans	Customers		M&A	Board	People	Announcement
Integration **Acceleration** **Next Normal**	Innovation	Marketing & Sales	Technology			Politics	Adjustments

The first component of the strategic playbook is the investment case. It guides every other part of the investment playbook and every other playbook. The first, fundamental questions go to what you want out of an acquisition or merger, how it would fit with what you've already got, and what you're willing to give up to get it.

What You Want

Synergy happens when two or more people or businesses work together to create new value, capture existing value, or prevent or slow the destruction of value. That leads to some of the different types of mergers and acquisitions and the different reasons to do them:

- Merging organizations with complementary capabilities and strengths to create something that no one else can do, like Stanley merging its hand tool and construction strengths with BLACK+DECKER's power tool strengths.
- Adding innovation or technology capabilities, like Disney buying Pixar to leverage its technology across all animation.
- Gaining access to a new market with a new business model or new Internet protocol, like Google buying Android to give it an operating system.
- Expanding product and service offerings, like executive search firm, Korn Ferry's string of acquisitions to add other human capital consulting offerings.
- Shoring up a weakness to stop destroying value, like Philip Morris buying Kraft foods and merging it with General Foods so the Kraft management team could provide needed leadership to General Foods or the second reason Disney bought Pixar, which was to acquire new leadership for Disney Animation.
- Repositioning a company in a new category (with higher multiples) like Delux's move from being a printing company focused on printing paper checks to merging into payment technology companies.
- Leveraging costs across the platform, like Coca-Cola's master bottlers swallowing up smaller bottlers to further increase their economies of scale.
- Creating critical mass for a platform company to enable future value creation, like regional companies merging to create a national or international footprint so they can expand geographically and serve national or international customers.
- Scaling the platform, where there are economies of scale, perhaps in an industry consolidation like Disney buying Marvel and then Lucas Films/Star Wars and then Fox after buying Pixar.

What You Are Willing to Give Up

You have to give up something to make any merger or acquisition work, whether it's cash or just a dilution of your control. You'd never do this if you didn't believe there would be a positive return on your investment (ROI) in an appropriate time frame.

If you're a public company, you'll need to manage that ROI in your quarterly and annual earnings announcements. Many public company investors will want to see accretion to earnings per share (EPS) every quarter. You will need to think about this aspect and ensure messaging and expectations are clear on when the merger will add to EPS. If you're a private equity firm, you'll need to manage that ROI within the time frame of the appropriate fund. If you're a family or family office, the ROI may be associated with generational wealth creation. Your ROI can be positive if you pay or contribute less or receive more for an asset than it's actually worth. In that case, there's a transfer of value between past and future owners with no need to chase synergies.

This book and this chapter focus on mergers and acquisitions (M&A) in which the combined parts are worth more together than they were separately—creating top-line and bottom-line growth through synergies.

Which Opportunities to Pursue

Knowing what you want and what you're willing to give up to get it points you in the right direction to consider all the alternatives, taking into account overall risks at a high level and how you might mitigate those risks.

British philosopher Carveth Read taught us "it is better to be vaguely right than precisely wrong."[1] Others encourage divergent thinking before converging on a solution. When it comes to looking at merger or acquisition targets, they are the same idea: Expand your thinking to look at vaguely right possibilities before narrowing in, getting more precise at each step.

In any case, make sure the opportunities tie directly into your strategic plan, building strategically important capabilities. Mergers and acquisitions are tactics, not strategies. Not thinking this way is one of the main reasons so many mergers fail.

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[1]Read, Carveth, 1989, "Logic: Deductive and Inductive," Grant Richards, London, June.

There are four basic things private equity investors do to earn money:[2]

- *Raise money* from limited partners (LPs) like pension and retirement funds, endowments, insurance companies, sovereign wealth funds, and wealthy individuals as well as the private equity (PE) firms and their partners' contributions to the deal(s)
- *Source, due diligence, and close* deals to acquire companies
- *Improve* commercial, innovation, and technology strengths and operations, cut costs, manage risks, and tighten management in their portfolio companies
- *Sell or recapitalize* portfolio companies (i.e., exit them) at a profit

When PE firms analyze companies for potential acquisition, they will consider things like what the company does (their product or service and their strategy for it), the senior management team of the company, the industry the company is in, the company's financial performance in recent years, emerging technologies, industry trends, risks, opportunities, the regulatory environment, reputation, potential competitive response, products and services, customers, and the valuation and likely exit scenarios of the company.

The main sources of value capture at exit include market share growth, growing revenue (and therefore earnings before interest, taxes, depreciation, and amortization [EBITDA] and cash flow) substantially during the holding period, cutting costs and optimizing working capital (and therefore increasing EBITDA and cash flow), selling the company at a higher multiple than the original acquisition multiple, and paying down debt that was initially used to fund the transaction.

This leads to a framework for the investment case—simplified by design. Your actual investment case will include several layers of detail below this overarching framework.

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[2]Chen, Andrew, "What Do Private Equity Investors Actually Do?" InterviewPrivateEquity.com.

The Path to Value Creation

As McKinsey's Andy West and Jeff Rudnicki laid out in their podcast on "A Winning Formula for Deal Synergies,"[3] the highest synergy potential is found in industry consolidations, capability-led roll-ups, and geographic expansions. Small product tuck-ins, corporate transformations, corporate-led white-space acquisitions, new business models, and IP acquisitions may also be strategic fits.

Think through the core focus, overall strategy and posture, strategic priorities, enablers and capabilities, and organizational and operating priorities for the investment based on a fact-based assessment of the situation.

The 6Cs situation assessment is a framework for understanding the business environment by looking at:

1. Customers: first line, customer chain, end users, influencers
2. Collaborators: suppliers, allies, government and community leaders
3. Culture: behaviors, relationships, attitudes, values, environment
4. Capabilities: human, operational, financial, technical, key assets
5. Competitors: direct, indirect, potential
6. Conditions: social, demographic, and health; political, government, and regulatory; economic, technical, market, climate

Think:

1. What: Objective, scientific truths—facts
2. So what: Subjective, personal, cultural or political truths, opinions, assumptions, judgments, conclusions
3. Now what: Indicated actions

Customers

Customers include the people your organization sells to or serves. These comprise direct customers who actually give you money, as well

[3]West, Andy, and Rudnicki, Jeff, 2020, "A Winning Formula for Deal Synergies," Inside the Strategy Room Podcast (May 8).

as their customers, their customers' customers, and so on down the line. Eventually, there are end users or consumers of whatever the output of that chain is. Additionally, there are the people who influence your various customers' purchase decisions. Take all of these into account.

FedEx sells overnight delivery services to corporate purchasing departments that contract those services on behalf of business managers. But the real decision-makers have historically been those managers' executive assistants and office mangers. So FedEx targeted its marketing efforts not at the people who write the checks, not at the managers, but at the core influencers. It aims advertising and media at those influencers and has their drivers pick the packages up from the executive assistants personally instead of going through an impersonal mailroom. FedEx trains its frontline employees on customer service and how to interact to retain business and grow share.

Collaborators

Collaborators include your suppliers, business allies, and people delivering complementary products and services across your ecosystem. What links all these groups together is that they do better when you do better. So it's in their best interest, whether they know it or not, to help you succeed. Think Microsoft and Intel, or mustard and hot dogs, or ketchup and hamburgers—though never mustard and hamburgers, of course.

Just as these relationships are two-way, so must be your analysis. You need to understand the interdependencies and reciprocal commitments. Whenever these dependencies and commitments are out of balance, the nature of the relationships will inevitably change. Think through your customer's purchasing cycle. Who comes before you? Who comes after you? If you're in corporate real estate, a relocation expert you can vouch for and trust is an obvious ally. In the M&A advisory business, attorneys, bankers, and other professional services firms pull in complementary firms to create the best outcome for their clients. However, a printing business could be your ally as your customer will need new letterhead and business cards to reflect their new location.

Collaborators are strategic partnerships whether that's intended or not. So, think strategically. The less resources you control in-house, the more important this is.