# How to build value into a merger

By Walter E. Shill and David W. Mackenzie

In the M&A marketplace, leading practitioners have shifted their focus from the mechanics of the deal to the value-creating potential of integration. And no aspect of the process is more critical than post-merger organization design.

Since two large consumer products companies merged in a $6 billion transaction in 1999, nearly three-fourths of their top 100 employee positions have turned over, and the company's stock still has not recovered to pre-deal levels. Though many variables can have an impact on share price, the huge executive turnover seems to be symptomatic of a post-merger organization design gone wrong.

Through Accenture's work on 400 merger engagements, we have found something that is surprisingly clear: The end is in the beginning, and vice versa. The ultimate value potential of a post-merger organization is determined largely during the merger's creation, through a set of managerial actions—implicit and explicit, conscious and unconscious—we call post-merger organization design. The actual value created is determined by the execution of that design.

During the past decade, post-merger organization design has moved from the periphery of M&A concern to center stage. Leading M&A practitioners now fully appreciate the complexity of forging two organizations and their distinct cultures into a single successor company that can outperform competitors over the long term. Furthermore, these organizations more readily appreciate how critical a discipline of traditionally "soft" factors has become in the "hard" short-term make-or-break of successful transactions. Finally, technology that can accurately measure some of these soft factors is now readily available. Companies can therefore measure many aspects of the organization before the deal to assess the merger's potential and then, once the deal is complete, measure its progress.

From our perspective—having witnessed more than 20 years of pre-deal M&A strategic discussions at close hand—effective post-merger organization design is defined by five principles.

## Value creation is the informing objective

Organization design is never an end in itself but rather a means to value creation, as defined by widely accepted performance and financial metrics. Simply put, the goal must be to exceed the premium paid for the merger, with minimal value destruction.

Even in companies with serial acquisition experience, management can lose track of the original

financial goals; in these cases, post-merger organization design becomes de-coupled in the details and, over time, from pre-merger strategy.

In practical application, value-centric post-merger organization design certainly has a key financial component, but it's not the only one. Cisco Systems, for example, has pursued a well-articulated strategy of expanding its product range through the acquisition of small, niche companies. Because Cisco's value proposition includes the capacity for future product development as well as for developing products it can sell immediately, its template for post-merger organization design also stresses the preservation of the acquired company's distinct culture. Centralization efforts are focused mainly on leveraging Cisco's enormous sales, distribution and support capacities.

The sources of value creation can vary widely from merger to merger. One merger may be based on proposed cost reductions, while another may be based on cross selling or geographic growth. The optimal organization design for each objective will vary.

## Organization design is more than filling boxes

In Accenture's experience, effective post-merger organization design is dynamic rather than static. Yes, from the beginning, executives must be matched to the appropriate roles, but that is not enough. These roles must be defined in great detail, including clearly established responsibilities and reporting lines. In fact, this seldom happens because in the rush to close the deal, much critical work is left undone.

In one Accenture engagement, a major challenge was merging a top-down, command-and-control organization with one that emphasized decentralized, autonomous decision making. The model had to be sufficiently structured to drive a common understanding of policies, procedures and governance issues through the new entity, but simultaneously supple enough to accommodate nuances of personality.

The decisions made prior to a deal closing have organizational implications that extend for years beyond formal post-merger integration periods. Effective post-merger organization design calls for the flexibility to adjust not only to predictable factors but to unanticipated side effects as well.

One company is so committed to acquisition-driven growth that it has established a dedicated post-merger integration team. Executives of the company acknowledged a mistake they had made repeatedly: To minimize post-merger disruption and demoralization, they had habitually made quick, aggressive staff cuts, only to find themselves understaffed as organic growth resumed. Eventually, the company learned its lesson and shifted to a post-merger organization design template that features rapidly scalable staffing arrangements, such as using the acquired company's management to help integrate the two companies.

## The most underappreciated issue in mergers is managing culture clash

More than any other factor we have seen, cultural differences are responsible for undermining prospects for value creation and, in some cases, compelling buyers to unwind deals that once held so much promise. At the same time,

these cultural differences are systematically underweighted in pre-deal analysis. In one well-known merger between two high-tech manufacturers, senior executives claimed that the post-merger financial picture was not as strong as expected because they had underestimated the "junior" merger partner's highly esteemed culture.

There is no orthodox approach that fits all post-merger circumstances. Again, as long as culture is appropriately acknowledged as a factor on both the customer-facing front and in the back offices, any number of approaches are possible.

When Deutsche BP, a German subsidiary of BP, acquired oil concern Veba Oel—along with its retailing subsidiary Aral, Germany's largest chain of petrol stations—the strategic rationale was to gain Central European market share and recognition. While Veba Oel was the more important company by both of those Central European measures, there was no question that "the BP Group way" would inform organization design decisions. The result was a cultural-hybrid design model that called for executives from both BP and Veba Oel to support operational continuity while opening the way for gradual assimilation into the BP culture.

## A continuous campaign to win the hearts and minds of employees is essential

Just because a company is purchased, it doesn't mean employees will decide to stay. Under post-merger conditions, recruitment can never be a one-time event, particularly for strategically essential executives. In our experience, the only development worse than a mass exodus of talent is a situation in which talent does not leave—but for all intents and purposes quits anyway, in terms of real commitment, accountability or performance. This can be particularly damaging if the employees are in customer-facing roles, where poor service can drive customers away. An effective post-merger integration design must continuously re-recruit, re-staff and retain its key people by winning their hearts and minds.

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As Jeffrey Krug pointed out in his February 2003 *Harvard Business Review* analysis of post-merger executive departure, the loss of talent in the first year is often 25 percent—three times the rate of similar companies that have not gone through a merger. In the second year following the acquisition, executives leave at about double the normal rate (15 percent). What's more, the departure rate remains abnormally high for up to nine years after a merger. For those who stay, the departure of valued colleagues is profoundly demoralizing. And management is blamed for having allowed the systemic breakdown to occur, through poor or nonexistent planning.

## There is no such thing as too much communication, at any stage in a merger

In the absence of clear communications, organizational behavior is driven by rumor, anxiety and deep fatigue. The rank and file of the merged organization have none of the familiarity with the merger's strategic rationale that the circle of executives who planned it do. Nor

do they necessarily care, beyond thinking about the impact on their own careers. In these circumstances, no amount of communication is too much. In the absence of information, people really do make things up.

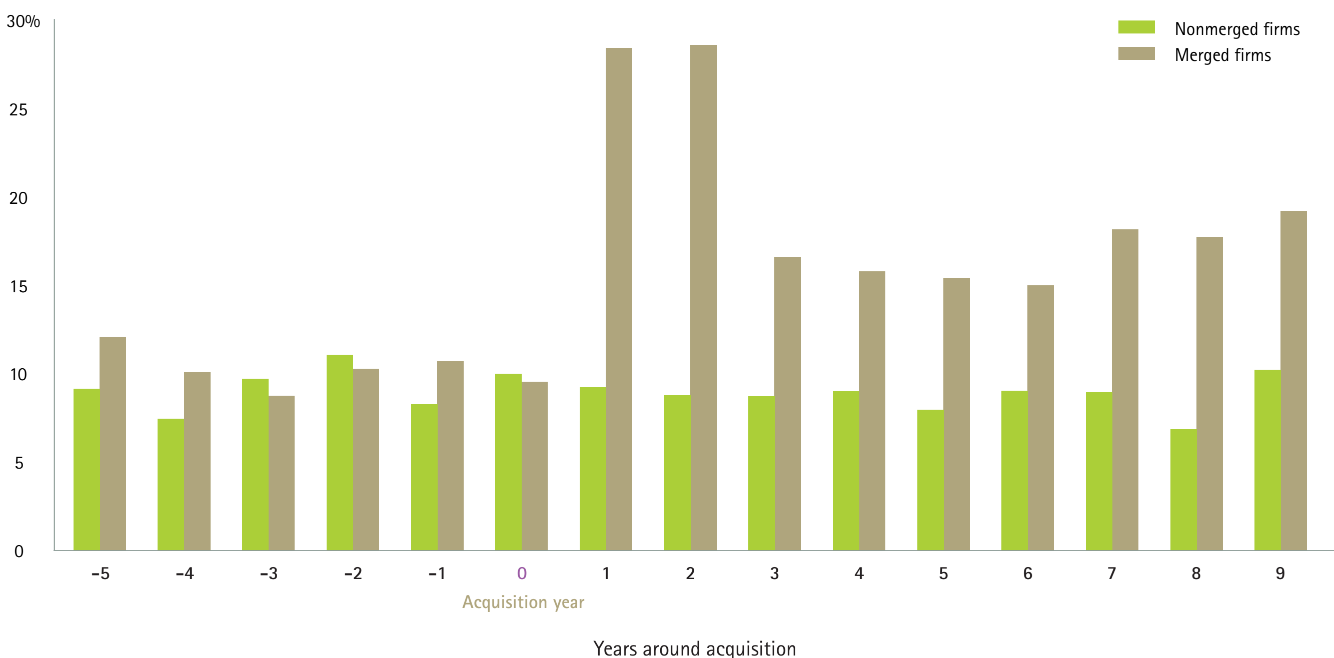
Some basic principles include the use of multiple communications channels, consistency, frequency and rapid response to potentially disruptive misinformation. Novartis Chairman and CEO Dan Vasella has noted that he had been repeating the same messages for six months about the company's merger and post-merger plans. He assumed the employees were tired of hearing the same thing. In fact, he learned that they were only just beginning to hear the message and that he needed to keep repeating it.

Words are only one aspect of an effective communications strategy. Symbolic gestures, such as the promotion of high-profile executives in the acquired company, take on outsized meaning in a post-merger context. Executives of famously hierarchical companies have signaled a new start by abolishing executive parking spots, eating in a common cafeteria or even repairing washrooms.

Following the merger of Cingular Wireless and AT&T Wireless, the new company temporarily retained the blue-and-white-striped globe of AT&T in its logo, sending a message of inclusion to employees. This decision was not just cosmetic; internal branding—the effort that management makes to help adjust the way

## Executive exodus

A 10 percent attrition rate is average for companies that have never gone through a merger. But for those that have, the rate remains twice that, even nine years after the event.



employees feel about the company—is the foundation of external branding. Anecdotal evidence suggests the logo gesture was widely appreciated within the employee ranks, a factor that can only help the company in the intense competition for customer loyalty.

Ten years ago, direct executive experience with mergers was less common than it is now, and only a handful of companies had completed multiple acquisitions. Today, many executives have more than one merger-integration experience in their portfolio, and more companies have some accumulated institutional memory of merger-integration lessons learned.

When simply completing a merger integration was the primary challenge at hand, the mechanics of the process tended to be the focus. Now, as direct M&A experience and best-practice knowledge have diffused, leading practitioners are focused on the more fine-grained, value-centric aspects of integration. In the M&A marketplace, post-merger organization design stands where more basic merger-integration practices stood a decade ago—embraced by a few market leaders and on the cusp of acceptance by organizations and individuals interested in emulating those leaders.

## About the authors

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