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TECHNOLOGY ACQUISITION UPDATE

Why Acquisitions Fail

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A successful acquisition can transform an acquirer's organizational capabilities and competitive strategy. But not all acquisitions succeed in helping the acquirer build its capabilities. This article discusses the top four reasons why acquisitions fail.

Over the past decade we have seen the success and failure of many mergers and acquisitions. Why is it that some companies can pull it off while others struggle through company dissolution and flailing stock prices?

Acquisitions are strategic alternatives that can help companies promote a better way of doing business and maintain their competitive edge over the long run. Acquisitions can help companies attain strategic goals more quickly, promote organizational change, and attack markets where its technologies can produce higher levels of growth.

Acquisitions do not always work out. In fact, not all acquisitions should be expected to succeed. Like any other strategic alternative, you take calculated risks knowing that not all of them will succeed. You do not want to fail, however, for reasons that are within your control.

We have seen Cisco's successful string of acquisitions including Crescendo and StrataCom and we have also seen the failure of mergers like Cendant. Following is a brief review of the top four reasons why acquisitions fail:

- Flawed Strategic Vision
- Inadequate Due Diligence
- Poor Integration
- Clashing Cultures

FLAWED STRATEGIC VISION

The first step in developing a strategic vision is to shape a clear understanding of the firm's corporate domain -- the product-markets within which the firm deploys its core capabilities.

A company is a cluster of core capabilities. To develop a capabilities-based perspective, management must recognize what the firm's core capabilities are and how they are embedded in the organization. The biggest mistakes are made by companies that are not sure what they want to do in the marketplace.

Once management has identified the capabilities required to build competitive advantage, it should judge prospective acquisitions against this yardstick. What role will the acquisition play in the company's strategic evolution and renewal? Where will value be created?

Too often managers pay attention to financial outcomes rather than to building capabilities. The acquisition review process can screen out opportunities that do not meet the financial criteria but might make sense strategically. It is easier to concentrate on issues that can be quantified, rather than on the qualitative concerns regarding the broad issues of strategic and organizational fit.

Management should focus the justification for

an acquisition on what capabilities a specific opportunity brings to the organization, not based on a predefined strategy.

INADEQUATE DUE DILIGENCE

The purpose of due diligence is to understand exactly what it is you are buying. Why is it that so many companies think they are getting one thing and end up with something different? The answer is poor due diligence.

One of the more difficult elements of due diligence is understanding the market niches if the buyer is not currently participating in those markets. Who are the major players and who are they likely to be in the near future?

Due diligence tends to focus on the expense side of a company. It is equally important to focus on how to maintain the revenue base immediately after the deal is concluded. Try not to place too much emphasis on quantifying estimates instead of the broader strategic and organizational considerations.

Due diligence can also be an opportunity to view the target's management team -- not just the senior team but also the next level down. Some of the best people may not be senior people, but are nevertheless key employees. Due diligence is a good chance to discover them.

Performing due diligence is not fun and it is not easy. It requires a disciplined and thorough approach to ensure that the right questions are raised and discussed.

POOR INTEGRATION

The danger point in a typical acquisition is right after a deal is completed. This is when indecision and aimlessness set it. An effective post merger management program can significantly increase the odds of success.

Spend the time up front to determine the strategy for the new entity and how it will operate. The right integration plan will often determine whether a merger succeeds or fails. The earlier and more thoroughly managers map out a program, the greater the odds are of ultimate success.

Move quickly and decisively to appoint the new management team, resolve cultural conflicts and reassure customers. The vision should be communicated broadly. Create an atmosphere conducive to transferring capabilities to achieve the acquisition's purpose.

Lines of management responsibility and authority must be made clear. Do the top managers have the operating capability to integrate the two companies? Agree ahead of time who is in charge. Does the manager appreciate the political sensibilities in making the combination work? Short cuts that save time may backfire later. Have a good logistical guy manage it and pay attention to team building.

CLASHING CULTURES

If hiring is the merger of one person, an acquisition is the merger of many. People matter. Too many companies leave the merger of cultures to chance. Cultural issues are critical in any acquisition.

Productivity suffers when stress and uncertainties rise. Acquisitions impact important elements of economic and psychic value such as job security, promotion, career opportunities, status and pride of association. Problems of divided loyalties and self-preservation behavior reduce the prospect that economic value will be created for the acquiring firm's shareholders.

Take care of your people; they are the ones who interact daily with your customers. Let them know what the merger means to them, and be honest about it. Don't leave them guessing. Mismatched cultures undermined the Cendant merger that combined CUC and HFS . The cultures proved to be utterly incompatible. HFS ran a very disciplined, tight ship with a hands-on management team. CUC's approach was deliberately haphazard with much looser financial controls. Because of these clashing cultures, mistrust grew and neither side could work effectively with the other.

CONCLUSION

Companies overpay because they don't do their homework, don't integrate properly, ignore culture issues or don't have a handle on their strategic goals. Overpaying is obviously a mistake, but overpaying depends on the value

received as much as the price paid. There are as many expensive deals that create value as there are "bargains" that don't create value. Focus on the value of a potential acquisition, not just price.

Acquisitions can be excellent drivers of growth and increased shareholder value. Companies must ensure that their acquisition strategies create value and that they manage the integration, due diligence and culture issues carefully.

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