L.E.K.

EXECUTIVE INSIGHTS

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Six Minutes With…

Michael Connerty, Managing Director at L.E.K. Consulting

Recently, L.E.K. Consulting analyzed the performance of more than 2,500 M&A deals between 1993 and 2010 and found that nearly 60% destroyed shareholder value. In a new *Executive Insights*, "Mergers and Acquisitions: What Winners Do to Beat the Odds," L.E.K. Managing Director Michael Connerty identified some of the strategies he sees consistently applied in the minority of deals that end up exceeding shareholder expectations.

Shortly after publishing the paper, Mike sat down to discuss some of the insights gained from advising clients through the deal and post-merger integration process.

You talk in the paper about 'beating the odds' on the way to M&A success. When you crunched the numbers, were you surprised how long the odds actually are?

Michael Connerty: There are a lot of previous studies that come to a similar high-level conclusion that deals destroy value, but our study shows the time it takes, and the magnitude of destruction. It really takes a long time, about 20 months, to stabilize following a merger. From a value standpoint, for a majority of companies it's a traumatic event, not the bonanza they envisage. So the results beg the questions: what can be done to reduce or even reverse the magnitude of loss? And how can you shorten the learning curve?

In the paper you identify revenue synergies as particularly difficult for acquiring companies to correctly predict and realize. Why is that?

MC: Assumptions around revenue synergies tend to be overly optimistic in our experience, and are in need of pressure-testing against market realities. I'd add one more point: not only are the variables around revenue synergies highly complex, but your ability to control the outcome is very low. If you go to a customer and say "we have a great combined set of products or services," the customer may not be as interested as you thought, no matter how you sell it. It is absolutely critical to pressure test revenue synergy assumptions well ahead of a deal close.

For more information, contact L.E.K. at transactionservices@lek.com.

You also discuss the importance of time as a variable in realizing revenue synergies. Can you explain?

MC: In the valuation process it is important to get a sense of when the synergies can be realized so you can price the deal accordingly. Companies tend to be optimistic about how quickly they can achieve synergy gains. Operational complexities, for instance, can be overlooked early on, but have significant timing implications once more closely examined. Even if the deal model turns out to be off by six months or a year versus the time it actually takes to realize synergies, you are pushing the synergy-valuation curve out and that has significant impact from a net present value standpoint on value creation and ultimate share price.

A recurring theme in the paper is the importance of analytic rigor. You argue that holds true for post-merger integration as well. Can you really bring rigor to a process that is fundamentally about culture and people?

MC: One of the things that came out of our research was the long period of time after a deal close to stabilize two or more companies coming together. The root of that tends to be people related. Taking an analytic approach way upstream can be helpful when dealing downstream with people, capabilities and talent retention. There's no reason planning for change can't be effective in mitigating the upheaval.

> "In our experience, assumptions around revenue synergies tend to be optimistic."

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