Why Mergers and Acquisitions Fail: An HR **Practioner's Perspective**

By Robert Purse

A significant percentage of mergers and acquisitions fail to deliver the benefits promised to stakeholders. A 1999 study by KPMG, which drew upon the top 700 European mergers between 1996 and 1998, found that 53% of participating companies had lost value as a result of their M&A activity. A subsequent KPMG study found that 83 percent of these deals hadn't boosted shareholder returns. KPMG's most recent study, however, was less negative: Only 32% of participating companies had lost value, 37% experienced a neutral impact and 31% experienced a positive impact. Certainly an improvement – nonetheless, nearly 70% of deals still did not produce a positive impact.

Taking a very charitable view, the success rate for mergers and acquisitions is currently no more predictable than tossing a coin. Moreover, target firm executives – the very people who could or should be assisting in managing successful integration, depart at an alarming rate. According to M&A research by Jeffery Krug and Ruth Aguilera almost 70% of these executives depart in the five years following completion, though my personal experience is that their finding is wildly optimistic. Many key executives depart, voluntarily or otherwise, in the 12 months immediately following completion, which only serves to unsettle the remaining staff.

These figures suggest there is something seriously wrong in the management of the M&A process. My own experience suggests the problem, like so much that is wrong with business today, lies in the narrow financial view of M&A strategy led by investment bankers, CEOs and CFOs. Valuing these deals only on the basis of the numbers needed to make the deal attractive to investors and themselves, means that shareholders are not seeing the promised benefits.

About the **Author**

Robert **Purse**

Robert Purse is the Director and General Manager of Human Potential Accounting (www.hpa-group.com). An alumnus of Henley Management College, he is a highly experienced HR practitioner and General Manager, with extensive 'hands on' experience of mergers and acquisitions. He is passionate about Human Capital Management and the benefits it can deliver to organisations, whatever their sector or size. His mantra is quite simple, "People make the difference!"

robert@hpa-group.com

Ignoring the human capital element of an organisation is a clear example of the short-sighted and self-serving view invariably taken by advisors, analysts, executive directors and intermediaries. I find this attitude bizarre, not least because much of the value of companies today is represented by so-called intangible assets. The reality is that, in the long-term, an organisation's intangible assets (especially its human capital) add to an organisation's future worth.

The value of a firm's intangible assets invariably far outweighs the value of its tangible assets. A brief look at a subset of the wide range of intangible assets demonstrates the point: Copyrights, customer lists, customer relationships, brand names, patents, trademarks, computer programmes, product formulae, research, new product development, reputation – these are all key elements of an organisation's value. They derive from a single source: the organisation's human capital. The reality is, as David Creelman and Laurie Bassi have stated, "Human Capital is the primary source of competitive intangibles for organisations today. Competitive intangibles are the source from which competitive advantage flows or is destroyed."

So mergers and acquisitions are good news for the accountants, bankers and lawyers but (excluding the advisors and intermediaries, who will get paid whatever the outcome) will anyone else benefit? Due diligence is supposed to uncover the truth about the strengths and weaknesses of companies but it rarely does. In part, this is because it is too fast but also because it is all too often done by the wrong people: not those who will have to make the deal work but those who will, when richly rewarded, just walk away. When advisors and intermediaries are assigned to due diligence, they often don't understand what they should be looking for. They aren't – and usually never have been – operational managers, so the critical dependencies within a business operation can elude them completely. The target organisation's human capital is rarely, if ever, given proper consideration.

While people use the terms acquisition and merger interchangeably, the reality is that there is no such thing as a merger. There is always, in the world of commerce at least, a dominant party. In a recent substantial acquisition in which I was involved, due diligence (undue diligence might be a better description) failed to ask the fundamental question: Are there any major incompatibilities between the two companies?

There were, in fact, many red flags:

1. The acquiring company was perceived by all staff (except the directors) of the 'target' as an unwanted predator;

2. Staff at the target were blissfully unaware that, without a massive cash injection, their employer was about to hit the rocks;

3. The acquiring company had always taken steps to ensure acquisitions were fully integrated with a common culture and universal values, whereas the target might best be described as a loose affiliation of disparate organisations – each with their own culture and values, with no real attempt at integration; and

4. Staff in the target company were imbued with a Public Sector 'Not For Profit' ethos, which was totally at odds with the culture of the acquiring company.

"Ignoring the human capital element of an organisation is a clear example of the short-sighted and self-serving view."

The resultant acquisition was an unmitigated disaster and, if possible, the situation was exacerbated by removing the very people who might (I am not overly optimistic here) have made the acquisition and subsequent integration work. Consequently, the newly acquired subsidiary was left with the "B Team" in charge. As they were ill-equipped, unprepared and largely ineffectual, the acquisition did not yield the promised financial benefits and some 3,000 people ultimately lost their jobs.

In another case, where the chairman of the acquiring company was renowned for the "Our People are Our Most Important Asset" mantra, HR due diligence was undertaken by a team of one and had to be completed in just one week. Although I was very well compensated, I still wonder how they expected one person (me) to undertake proper HR due diligence of an organisation with several thousand employees in only five days?

There are exceptions to my experience but they are far from being the norm and I have been involved in just one exception. The predator was an unquoted company, which may be significant as it meant there was less pressure from external market forces, so a more strategic (long-term) view was possible. On this occasion, the Due Diligence team, in addition to the usual professional advisors, included the HR professionals and operational managers who would have to make the acquisition work. Our (HR professionals and operational managers) advice was that the proposed acquisition should not proceed. Fortunately our judgement, centred largely around human capital issues, was accepted. The target was later acquired by another predator, which found that the acquisition had been unwise.

So why do these mega-deals, involving perhaps billions of pounds persist? They're glamorous, high-profile and make vast amounts of money for the advisors and intermediaries. They feed the CEO and CFO's ego and vanity, even though they are often no longer there when the chickens come home to roost. These deals also persist because they are often determined by executive directors who nowadays rarely have relevant operational management experience. They then influence institutional shareholders and non-executive directors – those who are at the furthest remove from the company's operations and, frankly, do not know what questions to ask. This is not a judgement on the competence of the individuals concerned but rather on the fact that they will not be involved in the post-acquisition integration work required to make the acquisition a success.

Unless and until directors and institutional shareholders take the human capital element of a proposed acquisition seriously, they could save a lot of time and money by just tossing a coin.

References

A New Dawn: Good Deals In Challenging Times A KPMG Global Survey, 2011.

http://www.kpmg.com/CZ/cs/IssuesAndInsights/ArticlesPublications/Press-releases/Documents/KPMG_MA-New-Dawn-2011.pdf

30 Years Of Mergers And Acquisitions Research: Recent Advances And Future Opportunities by Susan Cartwright and Richard Schoenberg, British Journal of Management, Volume 17 Issue S1, 2006

http://onlinelibrary.wiley.com/doi/10.1111/j.1467-8551.2006.00475.x/full

Top Management Team Turnover In Mergers & Acquisitions by Jeffrey A. Krug and Ruth V. Aguilera in Advances in Mergers and Acquisitions, Vol. 4, pages 123-151, (Elsevier Ltd, 2005)

http://business.illinois.edu/aguilera/pdf/Krug&Aguilera_CH05_2005.pdf

Reporting On Human Capital: Why, What and How by Laurie Bassi and DavidCreelman, The Washington CPA, January-February 2013

http://issuu.com/wscpa/docs/1-2_13_wacpa

> "Unless and until directors and institutional shareholders take the human capital element of a proposed acquisition seriously, they could save a lot of time and money by just tossing a coin."