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Why Half of All M&A Deals Fail, and What You Can Do About It

This article is by Robert Sher, the founding principal of CEO to CEO, a firm that advises chief executives of mid-market companies who are navigating major shifts in their business or marketplace. He is the author of the book The Feel of the Deal.

Would you risk your life savings on a coin toss? Of course you wouldn't. But leaders of many mid-market companies will risk their business this year with the same odds—by making disastrous acquisitions.

Most research indicates that M&A activity has an overall success rate of about 50%—basically a coin toss. Chief executives of mid-market companies (generally speaking, businesses with between $20 million and $300 million in revenue) should keep those odds in mind, because many more deals will be offered to them this year. The investment banker Robert W. Baird says that the number of deals in the U.S. valued between $100 million and $500 million jumped 78% in 2011 over 2009, and he expects this year to be strong as well.

The consequences of a bad deal are far greater for a mid-market company than for a big corporation. Large companies usually have enough managers and resources to patch things up. Most mid-market companies lack the finances or bandwidth to absorb a bad deal.

Why is M&A success such a crap shoot? The sad fact is that most deals look great on paper, but few organizations pay proper attention to the

integration process—that is, how the deal will actually work once all the paperwork is signed. Here's a list of questions I've developed while helping CEOs navigate the M&A process and after growing my own mid-market company a decade ago through acquisitions. CEOs considering a deal need to have honest answers to these questions:

- *Do you have sufficient management capacity to take on the integration process, or are you already stretching to run your business?* GSC Logistics, a $35 million trucking firm based in Oakland, Calif., gained a small footprint in the Pacific Northwest through a successful acquisition mainly because the deal has not distracted GSC's team and infrastructure. The 2011 acquisition has produced excellent results.

- *Have you thoroughly assessed the culture of your target acquisition, and is it compatible with your company's culture?* In 2007, after a 25-year relationship, the personality assessments publisher CPP acquired its master distributor in Australia. Because of the close relationship, there were no surprises. The compatibility of the two cultures was already proven, and both the deal and the integration went incredibly smoothly.

- *Is the deal in line with your corporate strategy?* A deal that delivers on a key strategy could offset the cost of a difficult integration; if it is a diversion in strategy for the core business, it can become a very costly diversion. Ken Ansin, the CEO of United Site Services, executed a well-disciplined region-by-region acquisition strategy in the portable toilet business. United Site Services bought a $15 million portable toilet firm, Handy House, and grew it into a $120 million business by adding dozens of similar companies in 23 states.

- *Is the deal priced so that you can afford to pour adequate resources into the integration—and still have a return on investment that passes the hurdle rate?* In the early 2000s, the Internet search engine Ask Jeeves looked at more than 100 companies in a series of technology and talent acquisitions. The company refused to overpay for acquisitions, believing that most would double in price

counting the cost of properly leveraging and integrating them. (Ask Jeeves itself was acquired by InterActiveCorp in 2005 for $1.85 billion.)

- *Is the acquisition, along with all the costs and risks associated with it, a better choice than all other alternatives?* The optical and laser components industry is known for intense rivalries and low margins, and organically growing market share is nearly impossible. In 2009, when Bookham (NASDAQ:BKHM) and Avanex (NASDAQ:AVNX) merged to create a new tier 1 company, Oclaro (NASDAQ:OCLR), the risks appeared huge. Yet thanks to diligent planning, Oclaro generated double-digit growth and is now a top-tier player in optical components.

If the situation looks weak in any of these five areas, the integration will likely stumble. The recovery alone could cost as much time and resources as two or more good deals, and that's assuming that the deal is salvageable. Many aren't, and no amount of management can fix an acquisition that should never have happened to begin with.

Meticulously and diligently screening deals for integration success will always increase your odds of success. Think hard about that coin toss. Mid-market CEOs who can't do the homework are better off keeping that coin in their pocket.

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