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Corporate Finance

Improve your M&A marksmanship with these 12 acquisition must-dos

Ask first, shoot later

Contents

So, **you've decided to pursue an acquisition**

You're poised to strike a deal. Market volatility, Brexit, economic uncertainty, and fluctuating currencies are no deterrent – you see the opportunity while others sit on the sidelines.

You have one or more targets in your sights, and your finger is on the trigger.

There's really only one question to answer . . .

Are you **ready?**

Seizing the right opportunity is hard work. A successful M&A deal depends on many critical factors.

Are you confident you have:

Identified the right target that fits within your M&A strategy?

Secured the appropriate resources and expertise to execute the deal, including the right funding package?

Devised a sure-fire plan to seamlessly integrate the target and align to an overall strategy for growth?

Easier said than done? Maybe.
Here's how to do it . . .

1. Tone from **the top**

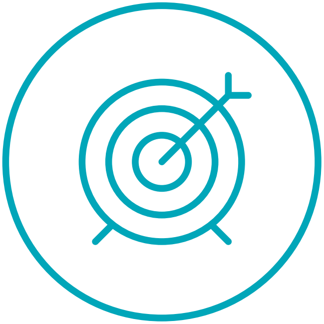
A clear M&A strategy will articulate your growth priorities and how you will succeed within your competitive landscape while still staying true to your overall corporate strategy.

Your M&A strategy will drive your investment approach and filter throughout your M&A lifecycle from target screening through to due diligence and integration.

Now let's get a bit more disciplined on this. . .

2. There are **plenty of targets** in the gallery

While it may be tempting to hold out until conditions seem to guarantee you'll hit the bull's-eye, good deals are hard to find.



A structured approach will make sure you stick to your strategy, define your acquisition criteria, and find the right fit.

Patience is a virtue, but so is ***decisiveness***.

Which is not to say you shouldn't still . . .

3. Approach with caution

Now that you've found the right target, full steam ahead, right?

Not exactly.
Slow down – check your blind spots and start gathering the right information. Get to know the company, the upsides and the downsides, and start to assess the indicative value as a baseline for negotiations. For the record the same rules should apply if you're on the other side - fail to prepare, prepare to fail.

However, a lot of targets move – so don't wait too long before you pull the trigger . . .

4. Zero in on the **right price**

You’ve done your initial homework and now you need to make some important decisions. What is this business worth? How will you fund the deal?

Identify potential synergies early, but be careful not to let them impact your negotiating mindset and position. While reflecting potential upside, synergies are hard to achieve and are typically diluted due to costs and execution risk.

4. Zero in on the **right price** (Cont.)

Also understand the seller's preferences and expectations. You may need to be creative to bridge value gaps through vendor notes or earn-outs, which can also be used to mitigate risk. And you might need to consider raising funds with a bank, alternative lender or private equity firm in order to facilitate the transaction, which will have timing implications and need to be carefully thought through.

The point is: ***be clear on what you are buying and what you are paying, and get the funding in place.***

Put a strong offer on the table to get to the next stage, but leave room for negotiation . . .

5. Time may not be **on your side**

Congratulations – your letter of intent is signed but now the clock starts ticking and there's much work to be done before your exclusivity expires. This will likely include integration planning, which shouldn't be left until it's time to actually integrate.

Due diligence, meanwhile, needs to be swift, but you only have one shot at getting it right. Do you have the right team /advisors to execute in a short window? Is your diligence coordinated across multiple work streams to address key risks and value drivers, and to validate your deal assumptions? . . .

5. Time may not be **on your side** (Cont.)

Diligence execution is within your control – don't let an incomplete process get in the way of a successful transaction.

Now you need to run a few things to the ground . . .

6. Scrub thoroughly

The target's numbers may look clean at first glance but they need a proper scrub before you let them hang to dry in your model.

The quality of the company's earnings needs to be carefully scrutinized. Private businesses often have related party transactions, owner-manager compensation, and other expenses that may not represent market value.

Assessing normalised earnings and the true quality of historic and forecast profitability should be one of the key outputs of due diligence.

6. Scrub thoroughly (Cont.)

You need to strip away all the noise to truly understand the target's normalized, sustainable earnings. Equally important is sufficient rigor to uncover any hidden costs or contingencies that could otherwise spell very unpleasant post-deal surprises.

Understanding the working capital requirement will be key to making sure the vendors leave you with adequate working capital to fund the business post-closing. Assessing debt and debt like items which the price should adjust for is also key.

After spending time in the weeds, you still need to look up and out . . .

7. Watch out for headwinds

Unexpected changes in the macro environment like commodity price declines, foreign exchange fluctuations, disruptive technologies, competitive pressures, and changing demand patterns can wreak havoc.

External headwinds can be a deal-breaker. Commercial and customer due diligence is crucial in understanding and quantifying the impact of market factors and customer spending decisions on the target's financial performance.

Now you need to think about getting the house in order . . .

Commercial and customer due diligence is crucial in understanding and quantifying the impact of market factors...

8. Don’t forget about the tax structure

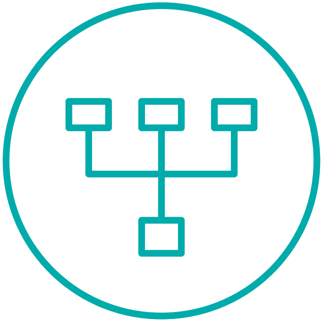
There is often a natural push and pull between buyer and seller on the optimum tax structure – you want this to be tax-efficient and to protect against exposures, while the vendor wants to avoid adverse tax impacts and minimize transaction tax costs.

Assessing and agreeing the optimum structure early in the process, can help avoid unnecessary headaches when trying to complete the process. For the vendors, early tax planning and structuring can make all the difference to the net benefit of a sale.

8. Don't forget about the tax structure (Cont.)

Simplifying the corporate structure may also facilitate a smoother transition and alleviate post-acquisition headaches. On the other hand, a more complex structure may help you maximize the after-tax return on your overall investment.

Agreeable middle ground can be negotiated – the challenge is to find the right balance.



But if you thought tax was hard, this will be harder . . .

9. Making the hard call

Retention of key management and employees is paramount. As the buyer, do you have the resources you need to manage this new business? Does the target? What about when you put the two teams together? Should organizational restructuring be on the table? How will you ensure alignment of goals with top talent? How will you incentivise and retain key people? If the founders are exiting, will there be a mass exodus?

9. Making the hard call (Cont.)

These questions and more must be asked – and answered. You need to be confident you will have the management capabilities required post-transaction. Use the best both sides have to offer – but be wary of potential redundancies, change of control costs, and other conflicts.

Tough choices are often part of the game. Expect to make them.

Now it's time to make sure everyone is aiming in the right direction . . .

10. Get your stakeholders on board

You must ensure the majority of your stakeholders – family members, management teams, other shareholders, key customers, etc. – are out of the line of fire and supportive of any deal you're considering.

This alignment is crucial. Dissenting views and dysfunctional groups should be managed in advance. Avoid any eleventh-hour surprises that may put the deal in jeopardy.

You're getting close, it's time to put pen to paper . . .

11. The last line of defense

All of your due diligence findings should be captured in the negotiation of the purchase agreement. Purchase price adjustment mechanisms, indemnities, representations, and warranties can all act as safeguards against potential exposures.

Traditional completion accounts will have adjustment mechanisms for net working capital and net debt. You need to invest the time to properly assess historical trends, set definitions and negotiate a working capital target to ensure you are properly compensated for any working capital shortfalls or avoid overpaying in the event of higher than normal levels at close. Other deal structures such as locked box can also make this process more seamless.

Don’t break out the champagne just yet, though. One more step to go . . .

12. Bringing it all together

The final stage in a transaction is the most imperative. A poorly planned and managed integration is the most common reason for deal failure.

The complexity of Day One and end-state integration will vary depending on the target and whether the acquisition is a tuck-in or transformational. Synergies and any step-up costs also need to be carefully considered to assess how they might impact your strategy.

Solid execution of your plan during those ever-critical first 100 days demand your team's full attention in order to achieve the value you expect.

Looks like you're getting the handle on this . . .

Now you're getting closer to preparing for a successful close

When you're finally ready to shoot, you want to be confident you're going to hit exactly where you're aiming.

After all, even 'friendly fire' has potentially dire consequences.

So, take a little care and pay attention to the details. When you do, your aim is more likely to be true.

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