Merger Integration: Delivering on the Promise

Our Hypotheses

Mergers often fail. Ask any consulting or research firm and they will produce a recent study to support this contention. In fact, according to the data, the likelihood of failure is greater than 50 percent, however you measure success — shareholder value, stock price, profitability, attrition rates, etc.

Booz·Allen & Hamilton was interested in understanding what makes merger integration so difficult. What are the primary causes of failure? What is the fallout from that failure?

Hypothesis 1
The more aspirational the strategic intent of the deal, the higher the likelihood of failure.

Hypothesis 2
The larger the deal relative to the acquirer's size, the higher the likelihood of failure.

Hypothesis 3
Execution issues, stemming from poor early stage decisions, are the primary cause of integration failure.

Hypothesis 4
CEOs of failed mergers tend to depart within a short span of time.

Our Methodology

We examined global mergers representing more than $1 billion in value that closed within calendar years 1997 and 1998. We then screened these deals to ensure broad and fairly equal representation from different industry groups. We analyzed 78 deals over the two-year period.

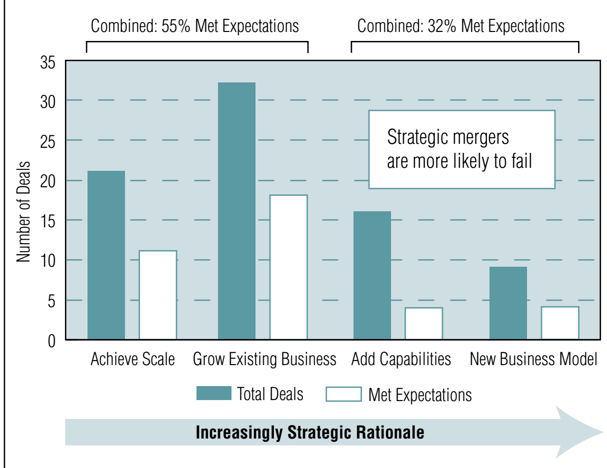
Next, we noted the stated vision and objectives for each deal. Data sources included company press releases, business press coverage, and analyst reports from the time of the deal closing. We then revisited these same sources two years later to determine whether the company had indeed delivered on its purported vision and fulfilled its objectives, in its own opinion and that of the financial and business community. In other words, did the merger "meet expectations"?

Findings

We found that two years after the deal close, 53 percent of the surveyed transactions had *not* met the expectations articulated at the time of the merger announcement.

Moreover, we found that mergers that were more strategically aspirational failed more often. When acquisitions were made within the same business or industry to achieve scale or to expand existing operations, the success rate was 55 percent. However, when the intent was more strategic (e.g., vertical integration, development of new capabilities), the success rate sank to 32 percent.

Extent to Which Deals Met Expectations Two Years After the Merger Close

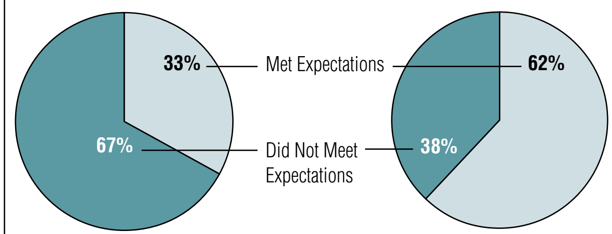


Source: Booz•Allen & Hamilton

In so-called mergers of equals — in which the acquiring company purchased a target company of comparable size — the likelihood of failure was almost twice that of smaller acquisitions.

Mergers of Equals More Often Fail

Mergers of Equals | **Dominant Acquirer**



Source: Booz•Allen & Hamilton[1]

The most commonly cited reasons for mergers not meeting expectations are primarily execution related and result from a lack of readiness and poor guidance.

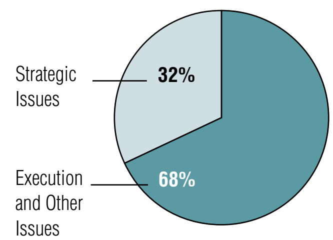
Why Mergers Fail

Most Commonly Cited Reasons

Strategic Issues
- Poor strategic fit
- Overly ambitious strategy

Execution and Other Issues
- Loss of key staff
- Culture clash
- Weak management team
- Poor due diligence
- Slow execution/hesitation
- Loss of key customers
- Poor external communication
- Poor/clumsy integration

Percentage of Reasons Cited for Merger Failure by Category

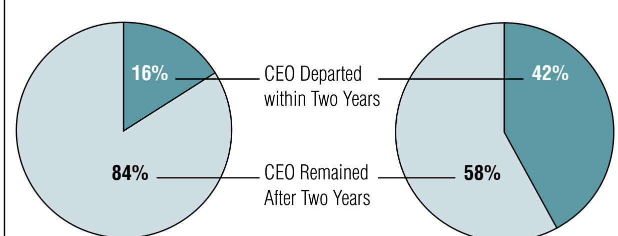


Source: Booz•Allen & Hamilton[2]

Not surprisingly, in mergers that failed to meet expectations, the CEO who led the effort was more than twice as likely to depart within two years when compared with the CEO of a successful merger.

Poor Merger Performance Leads to CEO Departures

Mergers That Met Expectations | **Mergers That Did Not Meet Expectations**



Source: Booz•Allen & Hamilton[3]

[1] BAH analysis of premerger sales data. Mergers of equals defined as mergers in which the acquirer's sales did not exceed target's by more than 2.0 times. Dominant acquirer mergers are defined as mergers in which acquirer's sales exceeded those of the target by more than 2.0 times but less than 10 times.

[2] BAH analysis of secondary research of 78 1997 and 1998 mergers. Multiple reasons per merger were allowed.

[3] Percentages calculated based on total CEOs, not total deals, since in two cases the merged entity had co-CEOs. In mergers that met expectations, six CEOs departed within two years and 31 remained for at least two years. In mergers that did *not* meet expectations, 18 CEOs departed and 25 remained.

Founded in 1914, Booz·Allen & Hamilton pioneered the business of management consulting. Today it is one of the world's leading international management and technology consulting firms, with more than 10,000 employees in 100 offices worldwide and sales in excess of $1.8 billion. Booz·Allen & Hamilton's corporate headquarters are in McLean, Virginia.