

DO YOUR M&A INTEGRATION STRATEGIES NEED A BOOST?

Challenges and Opportunities to Realize Value in a Disruptive, Digital World



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With unprecedented business model disruption across the majority of industries, integrating acquisitions has never been more complicated. But those who prioritize and resource their efforts appropriately are likely to seize a measurable competitive advantage.

Geopolitical issues may dominate the headlines, but corporate boards and senior management are laser-focused on countermeasures against technological disruption and seizing new routes to growth. Those countermeasures will often involve M&A as a faster route to innovation and expansion.

EY's recent Capital Confidence Barometer, which surveys almost 3,000 C-suite executives from around the world, showed that 56% of companies globally plan to make acquisitions in the next 12 months, and technology and digital disruption are two major drivers of the current market.

Ultimately, for an acquisition or merger to create value, the combination must become more than the sum of the parts. Realizing that potential relies on best-in-class integration strategies that quickly address risks and seize opportunities and synergies. Understanding this, many companies have developed leading-practice M&A playbooks and dedicated M&A teams within functions. But with deal premiums high and no evidence to suggest that will change, and as the pace of technological change accelerates, these approaches will need updating.

In our work with clients, we recognize the importance of integration strategies that address this new environment—to master it can mean gaining a competitive advantage over less digitally advanced peers; to fail to do so can mean unfulfilled potential and exposure to new kinds of risk.

- Big data and data analytics
- Omni-channel customer experience and social media
- Cloud computing
- Cyber vulnerability
- Integrating high tech businesses into low-tech parent companies

With the right strategy, we believe companies can rise to the challenge and reap the rewards of effectively and efficiently integrating organizations in the digital age.



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Inorganic growth lies at the heart of the success of many of the world's largest companies. Over the past decade, companies that routinely grow through mergers and acquisitions have honed their ability to integrate different organizations—their differing cultures, compensation and benefits programs, purchasing protocols, information systems, go-to-market models, and commercial operations. There is little they haven't seen.

But even for such companies there is, suddenly, much to learn. It isn't that the old ways of doing things no longer work, but that in a fast-moving digital world they may not fully address the variety of new issues companies must now manage when combining two organizations.

This white paper examines five areas where C-suite executives and boards of directors may need to rethink how their organizations will work through an integration with another company. They are big data and data analytics; preserving the omni-channel customer experience, including social media; cloud computing; cyber vulnerability; and in some cases, rising to the challenge of melding a high-tech enterprise into a no-tech or low-tech organization.

The decisions companies make in each of these areas will have important implications for their capital strategy and where they will spend their money—before, during, and after integration.

Big Data: Harness Analytics to Enable More Nimble and Informed Decisions

Wherever two integrating companies find overlap—supply chains, product mix, channels, or operations—decisions must be made about what to retain, what to jettison, and what to combine. With the advent of big data and data analytics, companies can harness information technology to allow executives to make faster, more fact-based decisions about what the customer of tomorrow is going to want, how the newly enlarged and integrated enterprise can meet those wants, and how to allocate capital and resources accordingly.

Consider, for example, a bank that decides to buy a competitor and wants to minimize the loss of customers from the acquired entity. By looking at which services individual customers use, their history with the bank, and other key metrics, the acquirer can predict which customers are most likely to consider leaving the combined enterprise

5 Areas of Concern

- BIG DATA AND DATA ANALYTICS
- PRESERVING THE OMNI-CHANNEL CUSTOMER EXPERIENCE, INCLUDING SOCIAL MEDIA
- CLOUD COMPUTING
- CYBER VULNERABILITY
- MELDING A HIGH-TECH ENTERPRISE INTO A NO-TECH OR LOW-TECH ORGANIZATION

Companies can also use data analytics to tailor their approach to **supply chain integration**, or **assess contractual relationships** of the new combined entity.

and implement programs designed to keep their business. Similar analyses can be undertaken to figure out where the best opportunities are to cross-sell customers of the two institutions.

The opportunities don't stop there. Companies can also use data analytics to tailor their approach to supply chain integration, or assess contractual relationships of the new combined entity. All of these processes can use public and private information to identify synergies and even business opportunities. In a recent health care services merger, for example, the acquirer was able to have a proprietary data set developed to evaluate the customer opportunity available from the target company. They used this to establish a clear picture of the total market accessible to the combined entity. The analysis involved combining and querying multiple data sets, enabling the acquirer to identify synergy opportunities and potential risks, both by service line and by market.

Customer Is King: Managing Omni-Channel Experience and Online Sentiment

Marketing is no longer a one-lane or even three-lane highway. Companies don't just market to customers via advertising, or direct mail, or in-store promotions. And it doesn't stop there. The whole customer experience must embody a seamless approach to engaging customers and providing them with the service they've come to expect in a digitally connected world. These customers will not look favorably on companies that disrupt that experience while trying to integrate their customer-facing systems. They are likely to leave.

Companies can't afford to duct-tape themselves together when addressing the customer's mobile experiences, transactions, purchase history, or follow-up care. They must identify the issues that matter to their customers and focus on creating an integrated experience and value proposition. And they must keep customers honestly informed about the process along the way.

In a world where social media is quick to call companies out on anything less than exemplary customer service, failure to handle this well could soon eat into profits as online sentiment turns against you.

"Don't sugarcoat things and say it's going to be seamless," warns Mitchell Lee Marks, professor of leadership at San Francisco State University and author of *Joining Forces: Making One Plus One Equal Three in Mergers, Acquisitions and Alliances*. "Under-promise and over-deliver. Instead of saying things like, 'It's going to be business as usual,' you can say things like, 'We're going to try to minimize the hardship,' and 'We are committed to keeping this as painless as possible.'"

Used correctly, social media can be a powerful tool and offer organizations a vast trove of useful information. Smart acquirers will pay attention to what customers, vendors, analysts, and other stakeholders are saying about a potential target, and then what they are thinking and saying about the combined enterprise and the integration process. Social media can also provide an early warning if the process begins to veer off track.

Consider the social media chatter that was present before and after a recent merger in the hotel industry. In this case, customers of the acquired company were passionately loyal to its brands and its rewards program—something that was consistent in social

media commentary. After the deal was announced, however, their sentiment flipped dramatically; many were frustrated and angry at the acquiring company, which they perceived as less aligned with their image of themselves and their expectations. Armed with this information ahead of time, the acquirer could have taken concrete measures to address the specific concerns of these loyal customers in advance of the merger.

Social media has also changed the M&A due diligence process. Today, potential acquirers need to take a full inventory of company websites and web properties; watch for any unauthorized use of the target company's IP; and pay attention to the use of social media by the target company's employees that could harm the company's reputation. Finally, with a new batch of Generation Z employees joining the ranks of integration professionals, the use of collaborative, cloud-based social tools for integration planning is no longer a nice-to-have, but a must.

Cloud Computing: A Shortcut to Synergies?

Any M&A integration is an opportunity for a company to evaluate how it's been doing things and whether change is appropriate—whether it can learn from the acquired company's business processes, for example, or impart some of its own competitive advantages to the acquired organization. Today, part of that opportunity is the chance to evaluate the speed and cost benefits of cloud computing. Especially for highly acquisitive companies, moving enterprise resource planning and other computer systems to the cloud can make future acquisitions easier to integrate, and non-core assets easier to separate.

“When two companies being integrated are each hosting their own data on their own systems, integrating them can be extremely time-consuming, expensive, and complex,” says Michael Towers, vice president and chief information security officer for Allergan plc. “With cloud technology, access and collaboration can happen much more quickly.”

The use of this technology can save time and money compared to integrating traditional on-premises applications and allow you to optimize the way systems work together early on in the life cycle of the new combined entity. Marks says exploring opportunities like this is part of what makes a merger or acquisition an “unfreezing” opportunity. Like changing the shape of an ice cube by allowing it to melt, reshaping the mold, and then refreezing it, he says, an M&A integration is a great opportunity to reshape the way the two parties involved go about their business. And it shouldn't be postponed until things “settle down.”

“First of all, you often don't come back to it,” he says. “Second, people are going to be shook up anyway during the integration. If you wait, you have to start all over again, just when people have begun to settle down.”

For this reason, among others, companies also will want to pay attention to what has become, at many organizations, a self-service approach to human resources. This can add a lot of complexity to IT integration, since so much of what employees need access to—salary information, vacation tracking, performance reviews, and more—is now self-serviced. Migrating this activity to the cloud may reduce complexity and provide a better experience for employees.

THE COMBINED LOYALTY MINDSET

Combining two companies operationally is always complex, but so is combining the way they manage their approach to customers. Each of the companies being combined will have its own methodology for classifying customers based on their cost of acquisition, current profitability, long-term value, and likelihood of attrition. So, while it's important for acquirers to focus on integrating the operational parts of an acquired company, it's just as important to spend time understanding the economics of the combined enterprise and its different customer bases. Go-forward assumptions will need to change. Predictive models that were driving decisions will require realignment. Relative decision-making, and definitions for best customers and most valuable long-term customers, will change overnight. Rather than waiting for the integration phase of the merger to be completed before thinking about these issues, companies should begin addressing them from day one. Doing otherwise may delay strategic investment decisions around marketing investments by as much as a year or more—a brutal, unaffordable delay in today's fast-moving markets.

MOVING ENTERPRISE RESOURCE PLANNING AND OTHER COMPUTER SYSTEMS TO THE CLOUD CAN MAKE FUTURE ACQUISITIONS EASIER TO INTEGRATE, AND NON-CORE ASSETS EASIER TO SEPARATE.

THE CONVERGENCE OF THE INTERNET, MOBILE COMPUTING, AND SOCIAL MEDIA HAVE LED TO THE EMERGENCE OF CYBERSECURITY AS A GREAT NEW BUSINESS RISK.

ROBOTIC PROCESS AUTOMATION: HOW SOFTWARE ROBOTS MAY EASE INTEGRATIONS

It's a given of business integrations: many people will spend a lot of time merging lots of data. Soon, it may not be necessary.

Robotic process automation, or RPA, is a relatively recent technology that refers to automating clerical and other business processes using artificial intelligence software, effectively creating what some are calling software robots. These robots can perform relatively simple business processes, like data entry, but also can be configured to handle complete end-to-end activities in which they might automatically process transactions, manipulate data, trigger responses, and, where necessary, communicate with other information systems.¹ RPA is already being used in a wide variety of industries, and some business leaders believe it will have application in business integrations, too.

"It's a way to substantially accelerate the integration of business processes and their corresponding technology without having to go do a full integration," says a managing director in the corporate private equity business of a highly acquisitive asset management firm. "It allows you to achieve the synergies or business capabilities you're seeking much faster than you otherwise would. At some point, you probably still need to make the longer-term, full integration investment. But it's both an accelerator to value as well as an opportunity to at least cut some of the costs of integration. It can have a pretty substantial impact."

While the technology has only started to go mainstream over the past 12 to 18 months, early adopters are already factoring it into their integration strategies. "We have not used it yet in any of our acquisitions," the managing director says, "but we're working on one right now where that is part of our plan."

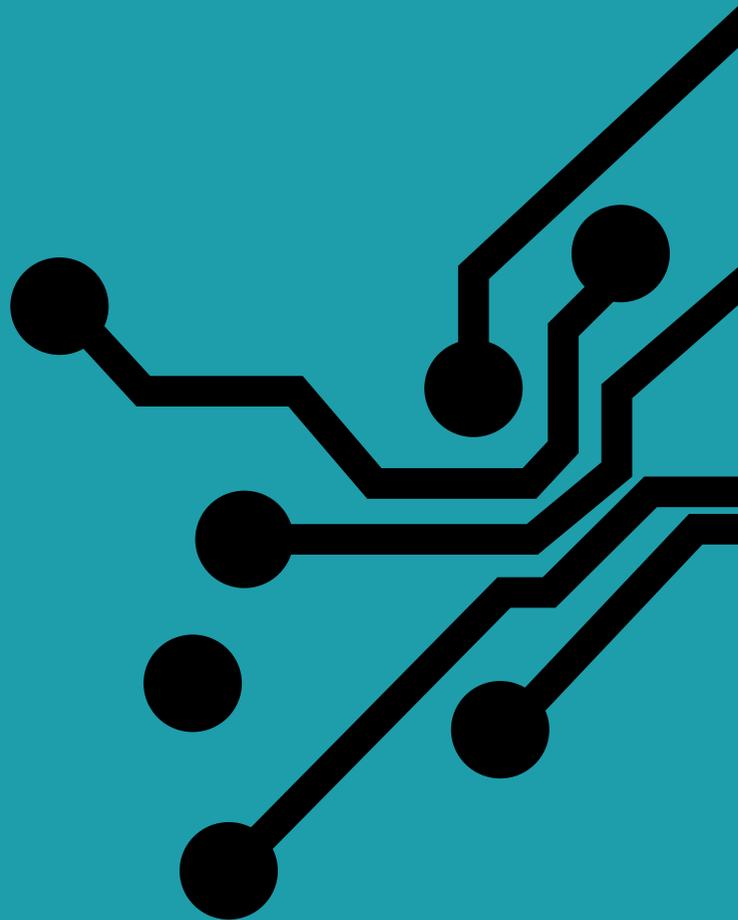
Live by Technology, Die by Technology: Addressing Cyber Vulnerability

For all that technology has to offer acquisitive companies, it's also true that the convergence of the Internet, mobile computing, and social media have led to the emergence of cybersecurity as a great new business risk. Hackers can bring corporate operations to a standstill with a denial-of-service attack, or severely damage a company's reputation by causing sensitive customer data to fall into the wrong hands.

Companies merging with or acquiring another organization must quickly assess its new partner's current cyber vulnerabilities and how seriously that partner took cybersecurity. The acquirer also has to oversee the integration of the two firms' information systems in ways that do not expose the combined entity to new risks. This undertaking needs to begin early in the due diligence process and continue through the post-close integration and evaluation. This is fraught with pitfalls that many companies may not have considered just a few years ago. Companies need to be aware of past breaches and any liabilities they may inherit, and prevent risks to the business.

Verizon Communication Inc.'s deal to acquire Yahoo Inc. is an egregious example of how big the issue can be. In July 2016, Verizon announced a deal to buy Yahoo for \$4.8 billion. Verizon contemplated pulling out of the deal in January 2017, though, after Yahoo disclosed that in 2013 it had been the subject of the largest known data breach in history, one that exposed details on more than a billion Yahoo user accounts.² According to current and former Yahoo employees cited in a *New York Times* article, Yahoo for years had been "slower to invest in the kinds of defenses necessary to thwart sophisticated hackers that are now considered standard in Silicon Valley."³ In February 2017, Verizon decided to go through with the acquisition, but only after getting Yahoo to accept \$350 million less and agree to share any future costs associated with the 2013 data breach and a 2014 hack that affected 500 million user accounts.⁴ Towers outlines several ways that companies can help tame cybersecurity risk during an M&A integration.

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“To expect that you’re going to be able to replace certain pieces of technology or certain security controls quickly is probably a nonstarter, so the key is to make sure you have a common aggregation point for cybersecurity analytics,” Towers says. “If you’re acquiring a company that is running, for example, completely different software on its laptops, or a completely different firewall, it may not make sense to replace those systems immediately; they’re probably doing an okay job. But in the early stages of integration you have to make sure you have a plan to coordinate them at the analytics level. If you’re running one firewall technology and you’re buying a company that runs another, you can still have both of your event logs pointed at the same analytics engine to look for instances of compromise or potential breaches.”

Towers says acquirers also need “a common set of incident response processes almost immediately,” even if the two parties employ different types of information systems. “It could be as simple as having daily calls where the acquired company and the acquirer are on the phone sharing what they are seeing from a security perspective and making sure that if they’re seeing anything suspicious, it’s handled with full transparency between the two entities,” he says.

To make sure everything gets done, Towers adds that it is important for the head of cybersecurity at an acquiring company to work closely with the acquired organization’s chief information security officer and its head of human resources. If the target company doesn’t have a chief information security officer, Towers says, he’ll usually work with the company’s general counsel and head of compliance. “If there is any kind of incident, there are always legal implications and there’s likely a compliance requirement even if the company is small,” he says.

Working with the head of HR is important too, Towers adds, because HR organizations typically own the identity and access management process at their companies, and “that process—the access to tools based on who you are and your role in the company—is almost always a security issue.”

Culture Clash: Integrating a High-Tech Business Into a Low-Tech Parent or Partner

In industry after industry, traditional companies are making high-tech acquisitions to help them adapt to and compete in the digital age. For many companies, buying a high-tech business raises a host of new issues and risks: how to value a tech company; how to retain its intellectual property, which may be in the form of human capital; and how to blend—and how tightly to blend—what often will be two very different corporate cultures. In some cases, the acquirer may wish to “harvest the cultural DNA” of the acquired business without imposing itself so strongly on that business that it destroys its culture or DNA. But this is no easy task. Where the acquirer operates in a heavily regulated industry—in financial services or health care, for example—the acquiring company may have to help the acquired company learn to operate in a regulated environment.

“It’s really challenging,” says the managing director at an asset management firm. “At a previous employer of mine, we tried to bring what ultimately was a social media business into a very low-tech consumer packaged goods company. It wasn’t the technology piece that was challenging. It was trying to get people who were used to

running a traditional product business figure out how to run a high-tech business. Frankly, we failed. We put a lot of money into it, and in the end, we did not come close to getting the value we had anticipated. I attribute it solely to a culture clash.”

To help mitigate culture clash, acquirers can make sure that a newly acquired management team has a seat at the table, to identify early on which aspects of the culture in the acquired company need to be preserved for employee retention and employee engagement and what changes need to be made to the culture, and to develop a timeline of rolling out changes on a gradual, manageable basis. To help foster cultural integration, rotating talent from the acquired company into the acquirer’s organization to give them a better sense of how it does things—and vice versa—is a highly effective method for aligning the combined workforce and reinforcing the same common purpose of the combined organization.

Marks warns, though, against pro forma efforts at collaboration. “I’ve seen situations where someone from the acquired organization was given a seat at the table, but they weren’t listened to,” he says. “It’s important to engage them in a meaningful way. That doesn’t mean you have to do things their way, but you can use their input to help in planning their movement from their way to your way.”

Marks also notes that acquirers have to guard against the sense of superiority that buyers sometimes have toward those being acquired—especially among senior leadership below the executive suite. “Your CEO might have announced that you were buying this company to help bring you into the 21st century, but senior leaders on the buying side may pooh-pooh that idea and literally tell their people to keep doing what they’d been doing.”

To avoid the problem, Marks encourages acquirers to make sure the senior team is on board and understands the strategy, vision, and “what’s in it for them” behind buying the other company. “Back to the unfreezing point, building a new corporate culture starts with ending the old culture.”

Marks also urges companies not to pretend they’re engaged in a merger of equals if they really are making an acquisition rather than merging. Communicate clearly to the acquired company what changes will be made, and why they need to be made to support the value to be achieved from the transaction. “If you’re going to dominate, just dominate. Don’t window dress. If you start setting expectations that we’re all in this together, one happy family building on the best of both, and then come in and dominate, you will lose credibility. It will be worse than having made no promises at all.”

M&A Integration: Time to Get Digital

Attempting a business integration today without using the latest technology tools is akin to driving across the country with a paper map rather than a GPS-based navigation system. You can do it, but you’re going to spend more time figuring out where to go

TO HELP MITIGATE CULTURE CLASH, ACQUIRERS CAN MAKE SURE THAT A NEWLY ACQUIRED MANAGEMENT TEAM HAS A SEAT AT THE TABLE.

EY INSIGHT

55%

OF SURVEY RESPONDENTS HIGHLIGHTED INTEGRATION AS A SIGNIFICANT CHALLENGE TO SUCCESSFULLY ACQUIRING A HIGH-TECH, OR DIGITAL, COMPANY.

YET ONLY 37%

SAID THEY’D AMENDED THEIR INTEGRATION STRATEGY FOR DIGITAL TRANSACTIONS.

Source: EY.com/DDE

“If you’re going to dominate, just dominate. **Don’t window dress.** If you start setting expectations that we’re all in this together, one happy family building on the best of both, and then come in and dominate, **you will lose credibility.** It will be worse than having made no promises at all,” says Mitchell Lee Marks, San Francisco State University.

and will be more likely to make a mistake due to human error or outdated information. Ultimately the route may be longer and more painful, using more valuable resources in the process. Such inefficiencies may be fine if you’re taking a leisurely vacation, but in a competitive business environment they could be devastating.

Many companies are investing substantial portions of their capital budgets—and grounding their growth targets—in merger and acquisition activity. It is critical to both take advantage of digital technology and proactively address the challenges technology brings ahead of and during the integration process if an inorganic growth strategy is to deliver on its promises.

ENDNOTES

- 1 “Robotic Process Automation: The New IT Job Killer?” by Bob Violino, *InfoWorld*, March 23, 2015
- 2 “Verizon Executive Says Company Unsure about Yahoo Deal,” Reuters, 1/5/17, <http://www.reuters.com/article/us-yahoo-m-a-verizon-idUSKBN14P215>
- 3 “Defending Against Hackers Took a Back Seat at Yahoo, Insiders Say,” by Nicole Perlroth and Vinu Goel, *The New York Times*, September 28, 2016
- 4 “Why Verizon Decided to Stick with Yahoo Deal after Big Data Breaches,” by Ryan Knutson, *The Wall Street Journal*, February 21, 2017



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