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Not All Mergers Fail

The adverse reaction to a number of mergers this past year prompts a reexamination of what causes a merger to fail (either before or after consummation). Most of the following reasons overlap, with one leading to the other or exacerbating one or more of the others. They should be given special attention in the planning of a merger.

1. Culture Clash. The cultures of the companies are not compatible and compete for dominance. If the battle is drawn out, the businesses of both companies suffer while attention is diverted to the contest. If the culture of one of the companies is totally subsumed, it may destroy a key element of its prior success.

2. Premium Too High. Particularly in hostile takeovers, the acquiror may pay too high a premium. While the shareholders of the acquired company, particularly if they receive cash, do well, the continuing shareholders are burdened with overpriced assets which dilute future earnings. This will come into sharp focus next year as companies are forced by the new merger-accounting rules to revalue and write-off "goodwill" booked in prior-year acquisitions.

3. Poor Business Fit. The conglomerate acquisitions of the 60's are the most cogent examples, but the lessons seem to be periodically forgotten. Technology acquisitions where the architectures did not fit are a 90's example, as are the rush in the 90's by some companies to acquire internet companies or other "new era" businesses they did not understand.

4. Management Failure to Integrate. Often the acquiror's concern with respect to preserving the culture of the acquired company results in a failure to integrate, with the acquired company continuing to operate as before and many of the expected synergies not being achieved. A well conceived plan for business integration, without disruptive culture clash, is the single most important element of a successful merger.

5. Over Leveraged. Cash acquisitions frequently result in the acquiror assuming too much debt. Future interest costs consume too great a portion of the acquired company's earnings. An even more serious problem results when the acquiror resorts to "cheaper" short-term financing and has difficulty in refunding on a long-term basis. A well thought out capital structure is critical for a successful merger.

6. Boardroom Schisms. Where mergers are structured with 50/50 board representation or substantial representation from the acquired company, care must be taken to determine the compatibility of the directors following the merger. A failure to focus on this aspect of a merger can create or exacerbate a culture clash and retard or prevent integration. All too often the continuing directors fail to meet and exchange views until after the merger is consummated.

7. Regulatory Delay. The announcement of a merger is a dislocating event for the employees and other constituents of one or both companies. It is customary to have well thought out plans to deal with these problems immediately following the announcement. However, where there is a possibility of substantial regulatory delay, there is the risk of substantial deterioration of the business as time goes on, with valuable employees and customer and supplier relationships being lost. This is a key planning consideration in evaluating whether a particular merger should be undertaken. It is necessary to include in this evaluation the relationship between the desire to limit antitrust divestitures and the costs attributable to the delay in consummating the merger.

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