



Whitepaper

The Advantage Series

Lifecycle of Mergers and Acquisitions

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Before leaving on a journey it's always useful to have a map to navigate your way from where you are to where you want to go. As part of our series of white papers called: *The Advantage: Getting the Edge With Intelligent M&A Strategy*, Marx Group Advisors has identified five phases of the lifecycle of a merger or acquisition. We trust this helps you embark on this journey with greater confidence.

Phase #1: Pre-Deal Preparation and Evaluation of Transactional Assumptions.

Mergers and acquisitions have received mixed reviews in terms of their success. While there are plenty of reports and studies about mergers and acquisitions that have failed, there have been in fact more instances of highly successful mergers and acquisitions in discrete one-time transactions by organizations that have an intelligently designed M&A strategy.

All of our clients know the state of their industry on the domestic level and some are aware of the state of the international industry. Often times an examination of the current metaview of the national and international economies, traditional and untraditional avenues of deal financing or structuring, and or tax avenues can bring strategies to the table that would not have been possible otherwise.

The management that is disciplined and takes the time to gather necessary information and take prudent actions before they begin to move ahead with their plans are the companies that will end up with the best transactions. In preparing to divest or acquire, companies that intelligently design their needs in light of an honest and rational assessment of the marketplace, the potential candidates, and the banking and investing environment are the ones that are most efficient in the process and most likely to be satisfied with the end result. A 2001 study by Texas A&M University analyzed the acquisition history of Fortune 500 companies and drew a number of interesting conclusions.

First, the study established that in periods where there are shifts in the capital markets, i.e. in periods of high interest rates or when capital accumulation is difficult through external means, companies pursue mergers and acquisitions using internal capital, such as their own stock or existing cash flow. Second, significant M&A activity is driven by external forces, such as changes in tax laws like the tax Reform Act of 1986 which resulted in a significant amount of restructuring activity. Third, corporations undergo significant M&A activity when they can no longer accumulate capital internally at an adequate rate.

This study demonstrates that an inquiry into the strategic positions that your company faces is often dictated by forces external to the

industry and/or the marketplace as you know it. Therefore, taking any action to buy or sell without fully understanding the dynamic complexity of the market and the industry in which you operate could seriously impact your outcome; akin to operating from a position that the world is flat, not round. Areas of blindness may include being unaware of relevant tax strategy, foreign market alternatives, monetary policy implications or a shift in perspective on the economy.

Pre-deal preparation and evaluation of the transactional assumptions is not just about unearthing potential issues in the transaction but it's also about assessing one's thinking. Consequently pre-deal valuation requires not only an examination of the balance sheet and operational strengths and weaknesses that you have or seek, but a keen analysis of the macro conditions both domestically and internationally that can impact your world. Marx Group Advisors encourages clients to spend more time in the pre-deal preparation and evaluation phase than any other phase because we know that a pound of planning is worth a ton of results.

Phase #2: Due Diligence

Closely related to Pre-Deal Preparation and Evaluation of Transactional Assumptions is the Due Diligence phase. Due diligence is one of the most overlooked and poorly executed aspects of M&A deals. Far too often transactions are penciled on paper and many strategic discussions are held. Yet all too often the grounding of the underpinnings of the deal through sound due diligence is not validated.

We all know that due diligence involves investigation of the financial, legal and strategic elements of a transaction, and involves obtaining detailed information not usually found from public information. Due diligence is meant to validate transactional assumptions, unearth possible problems, and begin to plan for transition.

Different levels of due diligence will be performed with different levels of intensity all through the deal lifecycle. Most of us are aware that we need lawyers to do the legal due diligence and accountants to do the financial due diligence.

However we often overlook the fact that strategic due diligence should be done with the assistance of experts in that type of analysis. A fatal mistake is made by business owners or acquirers who believe that their knowledge of the industry is sufficient. We advise our clients to lay down their pride and certainty and engage the support of those with experience in designing and validating strategy.

Establishing a plan and assembling a competent team to identify key issues and translate the issues and to value structure is essential intelligence required for this phase.

Phase #3: Pre-Close Planning

While merger and acquisition activity increased at a steady pace over the last decade, thanks largely to a stable economy, a low interest rate environment and the opening of international markets, we also know that many mergers failed to accomplish their goals. While there is no one reason why transactions fail, it's clear to MGA that underlying the success or failure of most deals is the quality of leadership that conceives, initiates, sponsors, drives, and is accountable for pursuing a given transaction.

Failure in mergers and acquisition transactions begins and ends at the top of each organization. It can begin in the earliest stages of a transaction when questions such as: why a transaction may or may not benefit one or the other company, or both; how it might change the competitive landscape; alter a distribution model or leverage a core competency, etc. are assessed.

One thing is clear -- today's deals should involve all levels of an organization as soon as the deal is cut. Planning and implementation are critical; i.e. making sure that key people as well as other important constituents including suppliers, customers and providers of capital are involved is essential no matter what size the merger, particularly in cases where leadership is staying on.

Making sure that the vision and benchmarks that the acquirer is relying upon are well communicated and well-integrated in the Pre-Close process as well as the Post-Close process are essential. Disciplined leaders, who take responsibility to learn the new skills they need to rise to the new level of their business, and who pay attention to the human aspects of these transactions, are the ones most likely to obtain the benefit of their efforts.

Phase #4: Post-Close Planning

Understanding what methodologies and best practices make for successful mergers and acquisitions is critical. There is much data that indicates that the post-close execution destroyed many otherwise successful M&A transactions.

Why is it that management thinks that because they ran a successful operation before they acquired a company equal to or larger than their own, that they can apply the same lessons to this new venture that is now twice the size with double the complexity in information technology issues alone? Too often it is because people forget the

lessons they gradually learned over the years as they grew their existing business and the time it took to integrate those lessons.

Entrepreneurs have an admirable trait of conserving resources and capital with an often damaging consequence of not reaching out for expertise when they need it most. Experience and literature indicates that the Post-Close Planning and Post Close Execution are areas that are most overlooked and most likely to cause the effort and expense involved in an acquisition to be wasted.

Some of the important questions that need to be asked and answered include: How can you keep morale high during a merger or acquisition? How can business drivers be used to add value for the merger or acquisition? What IT issues are involved?

Phase # 5: Post-Close Execution

There are several constraints to successful merger integration. The most important constraint is people. Without the support and buy-in of primary management the transaction is doomed to failure. Frankly, management personnel is key to every aspect of a deal and most employees and employers are painfully unaware of how the dynamics of the human element in M&A transaction will work, what is required of them, how they are to be personally affected, etc.

All this uncertainty creates fear, protectionism and barriers to success. These human elements need to be proactively managed throughout the process. Failure to do so may result in conscious and unconscious sabotage and other interventions in the smooth flow of a deal.

This may show up in the form of simple resistance or actual departure of key personnel. Addressing the concerns of management personnel should be put in place in the beginning of the transaction through the post-integration process. Clear communication of the vision behind the deal is important. Giving people the opportunity to raise concerns and have their concerns addressed to their satisfaction is even more essential.

Other constituencies need to be addressed as well. From regulators to customers, to suppliers to industry organizations and unions, each needs to be managed. Equally important, lenders need to be included in the deal and included in the progress of the transaction.

Considering the customer's and the competition's reaction is essential as well. The point is that merger integration does not end with the closing of the transaction and it doesn't even end when companies are fully integrated. The goals and benchmarks established at the outset

need to be continuously monitored and become a part of the operating standards for the company.

Conclusion

The measure of success of a merger or acquisition can be calculated by the amount of planning and quality of planning that is executed for each of these M&A lifecycle phases: Pre-Deal Preparation and Evaluation of Transactional Assumptions, Due Diligence, Pre-Close Planning, Post-Close Planning, and Post-Close Execution.

It is not enough to just complete the deal according to financial goals. Smart financial moves alone can still spell disaster after the deal is closed. A well designed M&A strategy will identify why the deal is a profitable undertaking and help position it to be positive for all involved. Asking for help early in this complex transaction may be the smartest move your company can make.

About Marx Group Advisors

Marx Group Advisors is a consulting firm that assists buyers and sellers in the automotive and heavy duty aftermarket with mergers and acquisitions (M&A), divestitures, along with capital formation for private equity placements. A highly experienced team of specialists provide buyers and/or sellers with a full range of services, including: M&A strategy, planning, investigation, buyer/seller identification, negotiations, due diligence support and integration. With offices in Boston and San Rafael, Calif., MGA specializes in middle market business transactions with company revenues of \$10 to \$150 million.