



GrowthMAPSM

Ensuring the Investment Returns of Acquisitions.

An Ephor Group Briefing on Acquisition and Integration Best Practices.

solving the value equation





Achieving the Growth Objectives of Your Portfolio Companies.

Growth through acquisition has long been a strategy to accelerate revenue and capabilities as well as drive stakeholder value. However history and data have proven this strategy for growth to be quite risky, causing it to in generally fail to accomplish desired business objectives. Despite its anticipated potential, study after study has shown that 70% of M&A transactions actually decrease stakeholder value rather than improve it.

During 2010 Epor Group has compiled our findings and “lessons learned” and offers the following guidance and risk management concepts to effectively manage this identified, but often undermanaged investment risk.

The obvious cause for failure is the current integration process deployed is ineffective. In far too many cases, responsibility for originating and closing a transaction is separated from the responsibility to integrate transition and operate the new business.

This obvious misalignment of interests within acquirers’ organizations is mirrored by the landscape of professional service firms serving them, where investment bankers work to assist corporate “deal teams,” and then transaction services providers assist operating groups subsequent to the close of the transaction.

Epor Group’s guidance includes taking a more holistic approach, managed by a single entity (or project manager), to pull together this fragmented processes.

Epor’s findings included that it is indeed possible to identify the characteristics of the acquisition and integration (A&I) programs that are successful in achieving the desired business objectives. These A&I best practices include:

- **MAPPING:** Integration “MAPPING¹” that begins early in the transaction cycle, and involves numerous teams from different areas in the organization.
- **Alignment:** Combining businesses for optimal performance demands an abundance of resources of the right quality and right quantity. Alignment requires prioritization initiated from “beginning of the project” and must come from the highest levels in the organization.
- **Perspective:** A belief, borne out by decision-making, that operational execution drives value creation, within business in general and A&I specifically; domain expertise and well-directed effort are required for desired success.

MOST COMMON REASONS FOR A&I FAILURE:

1. Hazy targets.
2. Unclear responsibilities.
3. Internal resource constraints and thus a lack of buy-in.
4. People & cultural issues.
5. Lack of investment thesis and/or lack of strategic vision.
6. Fierce economic or competitive pressures.

¹ MAPPING” includes all the planning, preparation and prioritization needed to map the communications, people roles and responsibilities, business processes, systems, cultures, and behaviors that are needed (and the resulting change management).





As with any corporate or strategic initiative, the right place to start with an acquisition is with ample preparation which is a process we call “MAPPING”. Unlike other internal initiatives, A&I (Acquisition & Integration) often competes with other priorities managers, especially operating executives, are contending with.

This leads to a chronic problems, increases risk and a results in a tendency to gloss over details or adopt an approach of “crossing that bridge when we come to it.” If allowed to persist risks and tasks go unrecognized and therefore unmanaged, thus becoming insurmountable barriers to achieving desired objectives.

It is well documented that customers and employees will be watching to see how things go the day, week, and months after the transaction is consummated. Competitors will also be watching and will capitalize on and publicize the failures and negatives that occur.

*“70% OF M&A ACTIVITY
ACTUALLY DESTROYS
STAKEHOLDER VALUE.”*

Clearly the old adage applies: you only get one chance to make a first impression, and poor MAPPING will make it unlikely that this first impression will be a good one. Ephor Group’s guidance here is to simply not take on this brand equity risk.

Alignment, the second key factor, sometimes flows naturally from the others. However, senior executives and institutional investors must realize that they need to set aside time on their people’s calendars for them to do the work and promote success. This will almost certainly mean that other priorities will simply have to be placed on hold, and in some cases may also require temporary shifts in responsibilities to insure that the right quality of skill married with the right quantity of skill is delivered to the holistic process.

Successful A&I is further dependent on having the correct **Perspective**. Many senior executives tend to view acquisitions through a legal or financial lens. At Ephor, we believe, on the contrary, that A&I initiatives are in fact operational initiatives, facilitated by legal documents, with desired financial returns delivered via a “holistic” approach.

Viewing a potential acquisition from this perspective tends to elevate the importance of functional and operational managers, in turn promoting more successful outcomes. In addition, because of their role, these operational leads take greater ownership of the process, and this intangible shift in attitude inevitably results in more positive outcomes and professionally managed execution risk.

We recently advised and helped a prominent ecommerce company put these “holistic” principles to work as they acquired a noted competitor. Integration MAPPING began the moment a letter of intent was executed and involved approximately 20 people, about 30% of the company’s total headcount. We also involved these same people in the due diligence process, for two reasons: they each had skills that allowed them to spot important things, and it also improved their view of what the integration would involve.

This approach yielded many important insights: for example, the Interactive Voice Response system at the target was able to handle about 35% of the inbound customer inquiries. Because the acquirer did not have





the infrastructure to implement a similar system, headcounts and space arrangements needed to be increased. These changes obviously had important valuation implications as well, which would have only come to light after the deal had closed had we not had the right skill and the right quantity of people looking at this operational issue, well before deal terms were finalized.

In another case we are aware of, a manufacturing company specializing in long-run, standardized production runs bought a smaller, more specialized job shop to complement its existing capabilities. While the financial models were quite compelling, within a couple of days after transaction closed it became apparent that the majority of machinery operators at the target were undocumented immigrants. The parent company, which had a number of government contracts, was forced to terminate all of those workers immediately. Management then had no choice to ship all of the equipment back to their headquarters and hire and train new technicians to run the equipment. Needless to say, these changes in the MAPPING resulted in comprehensive issues with product quality and the timing of delivery, thus "tainting" the brand equities of the well known parent company. This example clearly illustrates the need for the holistic approach.

"TOO MANY PEOPLE SEE M&A THROUGH A LEGAL OR FINANCIAL LENS. IT IS ACTUALLY AN OPERATIONAL INITIATIVE."

Proactive involvement of professionals in the due diligence process would have certainly identified this risk and avoided the oversight. The transaction professionals responsible for due diligence had years of experience, but did not get deep enough into the details of the employee roster to identify and manage this aspect of the transaction. Obviously this unidentified risk and unmanaged risk had a dramatic negative impact on the investment.

Growth whether driven organically, through M&A or strategic partnering simply is not easy especially in the difficult economic conditions we currently face. Therefore we as investors and executives must adjust our thinking and business processes to be more effective and manage all risks.

"A&I initiatives are in fact operational initiatives, facilitated by legal documents, with desired financial returns delivered via a "holistic" approach."





Using Post Acquisition Integration Services to Drive Equity Values

Acquisition & Integration best practices deliver the answer to the following risks:

- How do we get a solid understanding of how due diligence, integration planning, and increasing valuations are all inter-related?
- How do we achieve the pro forma budgeted and forecast results?
- What people, processes, systems, and functions must be integrated efficiently and effectively? How do we focus on realizing all the potential synergies?
- How do we best integrate and align multiple constituencies, mediate the conflicts and align the cultures?
- How do we maintain employee performance and insure customer satisfaction during the integration process?
- How do we identify and effectively manage all integration and execution risks associated with Strategic Transactions?

Ephor Group has identified a proven set of standard best practices that ensure the acquisition will be one of the 30 percent of acquisitions that adds shareholder value and not one of the 70 percent that erodes stakeholder value.

solving the value equation





Post Transaction Acquisition & Integration Best Practices

Most acquisitive organizations do an exhaustive job of financial due diligence and legal documentation when evaluating and executing acquisitions. Unfortunately, due diligence and documentation do not ensure post transaction operating results.

All too often corporate development departments, investment bankers and legal experts simply underestimate the significance of operational and people issues in ensuring successful transactions, and the consequences can be severe.

Numerous studies have shown that *only* 3 in 10 acquisitions create meaningful value (and of special note these results have not improved from the 80's to the 90's or in the 2000's).

Half of all acquisitions actually decrease stakeholder value and close to 80 percent fail to live up to acquisition proforma expectations. The present difficult economic climate and operating environment only makes the challenges more intense.

How can acquirers manage acquisition risks?

Successful acquirers realize that successful acquisitions require effective management of the acquisition process as well as post transaction operations to achieve the desired results. Therefore embedding a strong operational perspective in the transaction process is critical to achieving desired results.

By employing specific tactics and practices that mitigate both investment and execution risks, the stated transaction objectives have an increasing probability of success.

The following acquisition and integration (A&I) best practices presented are proven to provide near and long-term results. At the highest level successful A&I *is not all about* winning the negotiation around valuation or price¹. **A&I is about effective integration practices aligned and executed timely** to achieve the desired business objectives.

DEAL MAPPING: PLANNING & PRIORITIZATION PRINCIPLES

Failure to effectively plan for all contingencies is the source of poor execution.

There is often a high degree of loss after a transaction announcement. Without effective integration and execution; losses often include customers, talent, focus, and goodwill.

Failure to align all constituents leads to integration timing issues, productivity declines, roadblocks, and loss of confidence in the leaders.

When proper planning is completed, hidden gems such as assets and capability gaps are uncovered, revenue opportunities are highlighted and most importantly people empowerment is made easier.

While successful acquisitions typically target achieving scale economies, improving capabilities and acquiring some unique combination of resources. Winners ensure that that objectives are clear and the proper process and resources are deployed to achieve the desired results.

The winners essentially design their integration activities to support the intended result at all levels, from all required functions and then deliver the resources and activities to garner success.

¹ Bain Consulting Group 2010 M&A finding: statistically there is no correlation between deal premium and success, indicating that in the deal, marketplace prices on average are fair.





Acquisition & Integration (A&I) Best Practices:

- MAPPINGSM:** is all about proper planning, preparation and prioritization that results in the desired outcomes. MAPPING includes defining and mapping all of the following:
 - Defining Key Success Factors.
 - Defining Values & Principles.
 - Defining MAT (milestones, assumptions, and tasks).
 - MAPPING Operational Excellence.
 - MAPPING Product Leadership, Portfolio Management, and Customer Lifecycle.
 - *What is the price and margin and share of each product versus target market?*
 - *What is the portfolio offering? Gaps?*
 - *Where is each client?*
 - MAPPING Assets: Brand, Franchise Equities, Star Performers, etc..
 - MAPPING People, Process, & Systems.
- Alignment:** Constituency alignment ensures that all constituents are engaged, incented and working together in pursuit of a common set of outcomes. This can be achieved by both creating a broad sense of purpose and also showing team members how the transaction benefits them individually.
- Perform-Oriented.** Performance immediately following the announcement of a transaction can decline quickly, even before changes brought by the integration are made. It is therefore key to instill a perform culture geared for growth, and to plan and incent the key individuals on success on the critical activities.
- Prepare for contingencies.** Know what you can and cannot do and contingency plan and prepare for things which could go wrong. In one management consulting survey of acquirers, we found about 80% of successful transactions were based on a clear investment thesis and objective; for failed transactions, the proportion was about 40%.
- Intelligence.** Acquisitions all too often neglect revenue growth to focus almost exclusively on cost synergies. The most successful transactions are treated holistically and not on a functional basis.
- Navigator.** Having a champion, or sponsor, that provides advice and counsel to the project manager, integration team, and key employees is critical to ensure the transaction strategy becomes real. Any integration will face hurdles and obstacles and lose momentum over time, therefore this role ensures priorities and objectives are properly communicated, achieved, and that throughout the process the right quality of skills are married with the right quantity of skills in order to deliver the transaction stated objectives.
- Group Effort.** Involve operations and be sure to create advocates at all levels. Allowing or encouraging functional leaders' absence from acquisitions is a most common mistake. Advocates by nature are respectful and identify with the need for effective integration planning and execution.





“Shared Vision” Checklist:

Did you know that the majority of acquisitions never realize their value?

In fact less than half realize positive returns. There are a few primary reasons for this:

1. Failure to utilize a experienced corporate development team;
2. The dominance of legal or financial perspectives over functional and operational expertise; and
3. Due diligence that is limited to financial and contractual perspectives only.

Before embarking down the time consuming and expensive due diligence process a high level “Shared Vision Check” should be undertaken by all involved constituents, especially operating executives that will have to manage the ongoing business process; post transaction.

The litmus test is simple:

Is there an agreed upon “Shared Vision by all functional areas for the definition of Success?”

When discussing the “Shared Vision” put together a “high level” preliminary operations integration plan that includes the following components:

- a. Proforma Organization Chart & Compensation structures for the combined entity.
- b. Client analysis of Satisfaction, turnover, pricing/margin, forecasts, years on Service, Frequencies, Revenue and Services by client, etc.
- c. Operations: Technology mapping and usage, Review of service delivery process and tools, Review of third-party partnerships and alliances
- d. Cultural behaviors, events, and initiatives, to indentify a few.

The outcome of this “work session” is to establish the concept and understanding of a “Holistic Organizational Perspective”, while “MAPPING” the key functional areas that need to be involved, and identify the key advocates or sponsors who are required to achieve the desired results.

MOST COMMON REASONS FOR ACQUISITIONS:

1. Capabilities.
2. Growth.
3. Expand.
4. Consolidate.
5. Increase Scale.
6. Diversify.
7. Innovate.
8. Technology.
9. Management.

MOST COMMON REASONS FOR FAILURE:

1. Hazy Targets.
 2. Unclear responsibilities.
 3. Internal resource constraints or competition or buy-in.
 4. People & Cultural issues.
 5. Lack of investment thesis and/or lack of strategic vision.
 6. Fierce economic or competitive pressures.
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Conclusion

Strategic transactions all too often fail to perform to financial expectations because operating and people issues are not mapped and aligned.

While numerous research studies have found that financial performance is on average 200% higher with effective integration and change management practices companies: organizations continue to go execute acquisitions without appropriate integration planning and project management support.

The business climate today is less forgiving, more tightly regulated, and more risk averse. Therefore the concept of a “holistic approach” to Post Transaction Integration Services cannot be underestimated or over deployed.

Ephor’s guidance is simple: “MAP” your way to success!

Contact us for more precise details on: Post Transaction Best Practice and Processes to achieve effective integration activities.





Ephor Group Approach to A&I: GrowthMAPSM

The goal is sustainable growth in equity value. Ephor Group's methodologies were developed specifically for leaders who want a business that is built to last. It is comprised of the tools and skills to guide platform enterprises as they grow. Our approach is based on managing the relationships between due diligence, valuation, and integration planning; and accounts for the intangible factors that support tangible results.

What Distinguishes Ephor Group

- ☑ **Track-record** of realizing quick performance improvements and improving financial results.
- ☑ **The Talent** of Ephor's performance improvement professionals who have a combination of consulting, finance, turnaround, growth, and senior level operating experiences.
- ☑ **Deep expertise** in services, healthcare business services, distribution, and technology.
- ☑ **Speed-to-value** to obtain measurable and sustainable results.
- ☑ **Quantitative results** - Ephor does the strategic, operational, and tactical work while improving organizational effectiveness through constituency alignment and change management best practices.
- ☑ **Pedigree of success** using proven methodologies, lasting tools, and utilization of best-in-class processes.

"A&I is one of the most powerful tools managers have to increase the value of an enterprise. Our role is to ensure it is used effectively." - Houston Lane, 2010 fall webinar.

A&I Team Overview

The Ephor story is one of wealth creation. Garry E. Meier founded Ephor Group to pass on the management methodologies and wealth creating strategies he and his colleagues developed over the past three decades.

Every member on our team has a rare combination of both operating (CEO, CFO, CSO) experiences for the industries they serve as well as institutional investment experience with private equity and related investment types which allows our team to tie strategy to tactics on any issue and solve each challenge with industry domain expertise, solutions that increases valuation, and methodologies which guarantee meaningful ROI. Drawing on experiences gained running entrepreneurial businesses, as an investment banker, and as a strategic consultant, our team couples insight with practicality to teach leaders how to effectively use A&I to drive value.

Nothing is more important to us than the success of our client companies. Along with serving as a guide and partner for our clients as their wealth advisor, our proprietary methodologies provide a framework to guide growth.

Completed Platform Assignments

- IT Managed Services.
- National Provider of "Beyond Payroll."
- Payment Processing bring banking to the "unbanked."
- Emergency Medicine Billing Services for Revenue Cycle Management.
- National Radio Consolidation.
- Telecommunications.
- Online Subscriptions.
- Technology Enabled Business Services.
- SaaS

