How Unsuccessful are Acquisitions?

‘Nobody really explained the risks or the sorts of problems we could run into. Our advisers had a first-class reputation. To be fair, their procedures were faultless – absolutely smooth. But any mention of future difficulties was dismissed as untypical of the deals the bank handled. We were led to believe that failure statistics came from obscure academics with sampling problems.’

(Managing Director, engineering)

What do we mean when we say an acquisition underperforms? Most managers have come across the statistic on acquisition performance – *half to three-quarters fail*. But what does it really tell us? Apart from acting as a warning to would-be acquirers, by itself it says very little. If the statistic is to have any practical value, we need to know more about how it has been arrived at. In particular we need to know the following:

- What is meant by an acquisition failing?
- By how much do acquisitions fail?
- How is performance measured?
- What specific causes of failure have been identified?

These are highly complex questions. Teams of researchers throughout the world have been investigating them for decades and have not come up with a consistent set of answers. But they have given us the next best thing – clusters of answers which reflect the researchers’ academic disciplines. Each of the disciplines (mainly finance, economics and strategy) acts like a lens illuminating different aspects of the acquisition process. When these different perspectives and findings are put together, a composite picture emerges about acquisition performance which makes for uneasy reading.

Every manager involved in merger and acquisition activity, whether as acquirer or as target, should be familiar with what this work has to say. However, with much of it tucked away on library shelves and in academic...
journals, access can be difficult and time-consuming. This chapter and the
next are devoted to summarising what is known about acquisition under-
performance in a readable and accessible way. Digesting what they have to
say should more than repay any effort involved.

How is Acquisition Performance Measured?

There is no single, universally agreed measure of acquisition performance,
and for good reason. An acquisition usually sets out to achieve several goals,
not just one. The various parties who have an interest in the acquisition
usually have different expectations and have a preference for different
outcomes. Some of these outcomes are easy to quantify; others are more a
matter of judgement.

Thus, in practice, we find acquisitions and mergers being judged across a
wide spectrum of measures ranging from hard (numerical) measures through
to soft (judgemental or impressionistic) measures, depending on which per-
spectives and interests are being taken into account, and also – most
importantly – the time period over which performance is being assessed.
There are five different types of measure in common use:

1. **Financial measures.** Has the acquisition improved earnings per share
   (EPS) or return on investment (ROI)? Has the acquirer’s share price
   risen relative to the industry or sector average, or compared to estimates
   of the share price had the acquisition not been pursued? Are cumulative
   abnormal returns/residuals (CARs) positive?

   These measures are solidly numerical and usually allow direct
   comparison between firms in the same country. However, different
   accounting and regulatory regimes in different countries can distort
   straight cross-border comparisons.

2. **Economic measures.** Has the acquisition delivered higher efficiency and
   profitability? Have synergies and economies of scope or scale been
   realised? Does the acquirer have more market power? Has the
   acquisition allowed the company to grow faster than by internal effort
   alone?

   Some of these outcomes can be difficult to quantify accurately on a
   before-and-after basis. Major restructuring, for example, can result in
   operating units no longer being recognisable for comparative purposes.
   However, if efficiency or synergy outcomes are realised, they should
   translate into improved *profitability*, which can be quantified.