



Maximizing the transformational potential of M&A

Why mergers and acquisitions underperform, and how to attain better outcomes

by Barry Faulkner and Dylan Rhea

Few events have greater potential to positively transform companies — to make them more efficient, profitable and valuable — than mergers and acquisitions (M&A). Yet, most large M&A deals underperform significantly where the new post-merger or post-acquisition entity does not achieve the synergies, economies of scale, growth opportunities, financial targets or other goals originally envisioned for it. According to a *Harvard Business Review* analysis of 2,500 M&A deals, more than 60 percent of them actually destroyed shareholder value. Similarly, a KPMG study found that 83 percent of deals failed to increase shareholder returns.

However, failure is not inevitable. Organizations that take a disciplined, rigorous, methodology-

driven approach can attain highly successful outcomes. It is important for senior real estate executives to understand this because M&A is common in the industry and now occurring with greater frequency. Real estate firms have long pursued these types of deals, hoping to expand, diversify into adjacent sectors and/or gain strength more quickly than they could through organic growth alone. Recently, there has been a notable uptick in M&A activity. Based on RealFoundations' research of SNL-covered global real estate companies, M&A deals announced in 2018 had a combined value of more than \$61 billion, up 81 percent compared with nearly \$34 billion in deals announced in 2017. Meanwhile, experts are forecasting this upward trend will continue in 2019, as reported by *National Real Estate Investor* in February.

Why M&As underperform

Merger and acquisition events underperform for a number of reasons:

- **Complexity.** An M&A transaction has significant financial, operational and technological expectations and goals. It affects all areas of a real estate business, including personnel, systems, infrastructure, day-to-day activities and facilities. Many companies do not fully grasp the complexity of the event, in that all parts of the business will be impacted and undergo some level of change. They often have a misconception that the merger or acquisition only affects people and/or technology; they also underestimate the manpower, time and capital required to properly execute and manage the work. Complicating matters further is the reality that, while the two businesses involved may appear to be similar, very few companies accomplish their work in the same way. They differ, sometimes sharply, in the work that needs to be done, what resources are required to do the work and the information required to run their businesses.
- **Experience.** While corporate officers and employees are experts in their fields, many do not have experience with large M&A transactions, integrations and related project management. They may be able to easily identify efficiency synergy targets or foresee revenue-enhancing opportunities created by scale, but companies often do not have the tactical skills or methodology to deliver results. Investment bankers and attorneys who underwrite the deals, while accomplished in finance and legal matters, do not have operational or technical backgrounds, and they therefore can provide only limited insight or guidance on the issues that their clients will have to address after the paperwork is inked.
- **Constrained resources.** Implementing a merger or acquisition requires a significant amount of extra work for completion on a tight timeline, which is in addition to the enterprise's ongoing daily activities. Even if some team members have M&A experience, they already have full-time jobs and cannot be expected also to handle a sizable amount of the extra post-merger/acquisition work. In most cases, staff can be asked to take on a 20 percent additional workload, but a 100 percent or more increase is clearly not reasonable, although these types of transactions can often require this level of effort.
- **Organizational change.** A merger or acquisition can trigger change throughout an organization, and employees must accept and adjust to new ways of operating and doing their work. At

the same time, they have to meet new financial, operational synergy, and technology expectations and goals under aggressive timeframes. Combined enterprises often struggle with the dual demands of maintaining, integrating or changing multiple operational and technical models, while simultaneously mitigating risks so that the transaction does not negatively impact tenants, vendors, employees and customers. Often, the new company does not implement an effective change-management plan to guide stakeholders through the process and mitigate disruption. A good plan calls for regular communications to share information and manage expectations on a timely basis. It also includes training for team members now tasked with new and different responsibilities.

- **Leadership turmoil and cultural differences.** Key leaders, including members of the executive team and department leads, often leave the company following an M&A announcement for various reasons. They may be uncertain about their role within the new entity, are recruited by other firms, and/or experience a personal capital event such as stock vesting. This can disrupt leadership at a time when the newly combined enterprise needs a fully committed, unified team at the helm to keep all oars rowing in the same direction to generate organizational momentum. Also, the cultures of merging organizations can vary widely and even be at odds with one another, producing problems with how people interact, define their roles, and more, which can lead to poor morale and adversely affect productivity.

Managing the challenges

Real estate firms involved in M&A deals must be realistic about the complexity and challenges of these transactions as well as the expertise, time, resources and effort required for successful post-transaction integration. They must be honest about what they can handle on their own, where they fall short regarding capacity and capabilities, and whether they need outside assistance. Ultimately, company leaders will be measured by their ability to meet financial, operational synergy, and technology targets and milestones on schedule, while also mitigating risks and shielding ongoing operations and customers from disruption. The pressure to execute is especially strong for public companies due to constant scrutiny from shareholders and analysts.

Collaborating with an external consulting group with a specialization in real estate M&A can help companies avoid common pitfalls and bring structure and governance to the process, all of which are key for goal attainment. A qualified team

consists of consultants who are experienced in all aspects of M&A and also have a deep knowledge of what is required to run top-performing real estate companies across all asset types and market sectors.

Broad and deep real estate expertise matters because retained consultants need to fully understand how the merging companies operate: the work each does, the systems that support that work, who does the work, the information needed to run the business, and the best ways to operate once the merger or acquisition is completed. These qualifications can help to minimize disruptions when moving from two different operating platforms into one. Additionally, individual practitioners can supplement their personal knowledge by tapping into the firm's vast base of industry-specific institutional knowledge to get ideas on approaches and solutions that their colleagues have successfully implemented for clients in other real estate sectors.

Secure more successful outcomes

To increase the likelihood of a successful merger or acquisition, consider taking the following actions:

- **Engage an experienced adviser as early as possible.** The ideal time to engage a consulting team is when an organization first contemplates any type of M&A activity, typically more than six months prior to the planned transaction. That is when the enterprise initiates discussions with investment bankers, attorneys, and audit and tax support teams to determine the expected benefits of the transaction, and it is also when formal due diligence processes commence. The next phase occurs in the months before closing, as the companies begin deciding how to combine their operations effectively. They identify potential synergies, make key personnel decisions, figure out options for streamlining or modifying technology systems, propose opportunities for cost savings and new revenue streams, and set timelines and milestones for accomplishing the work. Outside consultants can assist substantially with this heavy workload so that the enterprise can concentrate on running the business with minimal disruption and avoid costly and time-consuming missteps. Engaging consultants too late in the process can make the entire effort lengthier and more difficult.
- **Lock down key personnel early in the process.** As soon as possible, identify and retain key executive leaders and functional leads from the two companies — typically those with the most appropriate experience and expertise for managing the post-transaction integration. Incentivize them to remain and serve as an integral part of the new entity, as they have critical knowledge

and perspective regarding their respective organizations and can immediately help the team make better decisions and move the process forward more quickly. Also, having familiar leaders in charge can provide a sense of continuity and certainty for other employees.

- **Build and support a strong delivery team.** Involve company employees who have relevant backgrounds to work closely with outside consultants on all facets of the M&A integration. A large transaction may require a sizeable team of company personnel and consultants divided into groups that will work on dozens of projects within multiple functional areas, including property management, information technology, accounting, construction management, marketing, customer experience, finance, investor relations and legal. Additionally, establish an Integration Management Office to serve as a central governing body that oversees the many work streams and helps manage ongoing risk.
- **Establish executive sponsorship and active participation from the start.** Senior executives must function as overall thought leaders and drivers of the merger or acquisition work. For mergers, in particular, leaders need to be visionaries, establishing a roadmap for how the new company will go forward. They must also keep internal delivery team members inspired and motivated, as these people are essential to the project's success. Corporate leaders should press the delivery team to continually think critically and find ways to improve existing processes where possible.

Key takeaways

Mergers and acquisitions can be difficult undertakings, and companies often underestimate the complexity, time, effort and risk management required to achieve successful outcomes. However, with timely and thoughtful planning, firms can avoid the obstacles that too often cause organizations to fail in achieving defined goals and milestones. One of the most important things a real estate enterprise can do to succeed in its M&A journey is collaborate with the right consulting firm — one that utilizes a proven, real estate industry-focused methodology. This better enables the client to meet and ideally surpass target synergies, consolidate and streamline its technology infrastructure, and implement a cohesive and efficient post-transaction operating model to carry the combined company into the future. ❖

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