M&A IN THE ERA OF BUSINESS 4.0

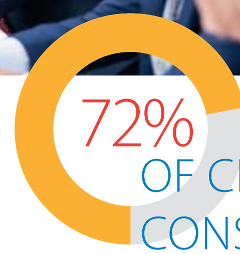
Mastering deal making and integration is now a competitive imperative.

TATA CONSULTANCY SERVICES

AT A TIME OF RAMPANT DIGITAL DISRUPTION, CEOS ARE under enormous pressure to up their games. Virtually every industry is entering—or already well into—the early innings of major technology-fueled transformation. Companies, in turn, are tasked with adopting innovative technologies, bringing in tech-savvy talent, entering new markets and overhauling business models. Given the difficulty of delivering such seismic change organically, more and more are recognizing that deal-making capability is an increasingly critical key strategic tool.

In fact, 72 percent of CEOs are considering some kind of merger, acquisition or divestiture activity in the next three years, according to results of a recent study conducted by Chief Executive and Tata Consultancy Services (TCS). The top two drivers of deals? Acquiring new products or services (39%) and entering new markets/creating new business models (34%).

C-Suite executives gathered for a recent roundtable discussion on M&A activity echoed those survey findings, noting that while companies once pursued acquisitions to realize economies of scale or edge into new turf, buying into Business 4.0 tech transformation is the leading deal-making rationale today. "For us, M&A activity is about seeing the future," said Mark Mlotek, chief strategic officer at Henry Schein, who described an evolution in his company's acquisition strategy over the past 15 years. "We've done about 300 acquisitions during that period. We did 1.0, which was about scale. We did 2.0, which was geographic [expansion]. We did 3.0, which was product oriented. And now we're doing 4.0, which is digital."



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The sheer magnitude of the changes afoot, coupled with the pace with which they must be pursued, is driving deals aimed at jumpstarting transformation, such as Walmart's acquisition of Jet and CVS's deal with Aetna. "We're moving from vertically oriented industry constructs toward more of a horizontal orientation where value creation has no regard for industry boundaries," said Frank Diana, leader of the Future of Business at TCS, who described a broadening of ecosystems. "Think connected car, smart home, smart city—as these ecosystems evolve, there are opportunities for companies to monetize on a number of levels… The shifts that are coming require companies to have a portfolio of innovations, and M&A is a way to drive those innovations and that portfolio."

At the same time, deals are notoriously difficult to do well — and even harder to ace at the speed demanded by today's competitive pressures. All too often, hoped-for synergies go unrealized as newly coupled entities grapple with the challenges of integrating operations, including dissonant cultures and incompatible processes and platforms. Such was the case for HHHunt Corporation, where the company's first foray into M&A growth was bumpier than anticipated. "We struggled because our culture is our brand and the other company's culture just didn't fit ours," recounted COO Dan Schmitt. "Looking back, we probably didn't do our homework."

How, then, can CEOs assess opportunities and position their companies to succeed in deal-making endeavors? Diligent preparation and orchestration

*"Strategic Alignment and Synergy Management," Chief Executive/Tata Consultancy Services, 2018

across a deal's lifecycle can go a long way toward skirting the hurdles that typically plague transactions, agreed M&A veterans, several of whom shared strategies gleaned from experience. "You need to be disciplined," asserted Mlotek. "There are plenty of exciting opportunities to chase but you need to resist chasing the wrong opportunities or the right ones where the price is [too high]."

Tom Harrison, who steered more than 200 acquisitions during his tenure as CEO and chairman of Omnicom, reported that culture was as crucial as finances in his evaluations of potential acquisitions. "Chemistry was incredibly important to me," he said. "I would always say, 'If you're not the kind of person that I want to go to dinner and a Broadway show with, chances are we aren't going to get along and this isn't going to work.'"

The Culture Component

For Harrison, who sought companies where the management would remain on board and be engaged post integration, walking the halls and talking with employees was as central to the due diligence process as pouring over financial ledgers. Seeking companies that would take Omnicom in a new direction, add to its client base or deepen its competencies, he vetted each potential target for entrepreneurialism. "Walking in and talking with the receptionist and the employees really gives you a feel for a company's DNA," he said.

Dave Jordan, global head and managing partner of TCS' Consulting & Services Integration, seconded that sentiment. "I call that the barbecue test: Would I want them to come to the home and enjoy a beer and barbecue with the family?" he explained. "I drive some of my clients crazy because I insist on a significant emphasis on socializing during the due diligence process."

Jordan urged CEOs not to neglect this often-overlooked component of M&A success. "Get away from the spreadsheet and spend time over dinner, golf and other events so you really get to know one another," he advised. "Taking the time to build a relationship and test the chemistry is really critical because, at the end of the day, if you don't like each other, it isn't going to work."

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While compatibility is essential, cultural differences aren't always an issue, noted Mlotek, who says Henry Schein draws a distinction between values and culture. "Values are immutable, they're not up for discussion," he said. "But culture can cut both ways, so we try to separate the two." While all of the companies acquired by the healthcare product and services distribution company must share a commitment to its core values, many continue to operate as separate divisions. "We run 400 P&Ls with separate boards where people feel empowered and have decision-making authority within their divisions," Mlotek said, adding that the degree to which acquired companies need to be integrated with existing operations often depends on the strategy behind the deal. "When it's about scale, you integrate; when it's geography, you don't."

While bringing acquisitions into the fold can be tricky, companies that regularly acquire for scale or geographic expansion generally develop and refine a process over time, pointed out Kathleen Camilli, an independent director with UniFirst. "We do eight to ten acquisitions a year, usually of mom-and-pop enterprises where the family that owns the company is looking to cash out," she said. "We put in new equipment, digitize everything and fold them into our operation. We rarely have any problems."

In cases where the purpose is to acquire an inventive product or the capacity for agility, however, integration without assimilation is often the challenge. Large organizations hoping to gain an entrepreneurial or innovation edge by acquiring younger companies often do so only to find themselves unable to nurture, let alone adopt, the very qualities that attracted them.

"We've seen acquisition as a way to inform the whole only work in limited cases," said Rob Biederman, founder and CEO of Catalant, who reported that skepticism about how integration would play out led his company to pass on six potential deals. "The idea that something that is one-one thousandth of the size of our company is going to come in and make us more entrepreneurial, more digital or more nimble—it usually doesn't work because the body rejects the transplant. We've seen the things that made that small company great eventually get beaten out of it, the good people leave and the positive impact just [doesn't happen].

Those who've honed their approach to acquisitions into a core competency, however, say there are ways to overcome that challenge. "It comes down to how receptive the acquirer is to the acquisition," said Harrison. "In our case a lot of the small, digital acquisitions really did change the way we thought and did business, even though they were literally a fraction of our size. We set out to acquire the right companies, and we allowed them to influence the way we did business."

In fact, managed well, the acquisition process can be a cultural win-win, added Jim Reagan, CFO of Leidos, whose company merged with Lockheed Martin's Information Systems & Global Solutions unit in a Reverse Morris Trust transaction that created a $10 billion entity. "The Lockheed culture that had been developed over decades had a little bit more structure than we had at Leidos," said Reagan, who reported that the combined company was able to work with consultants to develop a brand-new culture. "In the process, the two separate companies identified their differences, but when we said, 'What do we want to be?' everyone agreed we wanted to come in somewhere in between on cultural dimensions like structure and the degree of regimen to put around policies."

Driven from the Top

One big factor in developing a successful approach to acquisition strategy and integration, added Mlotek, is leadership. "Acquisitions are hard, and there is a natural tendency to reject them," he said. "You need a CEO who

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—Frank Diana, leader of the Future of Business at TCS is bold, who understands where the future is going and who pushes the company. It requires giving people some independence so they're not just subsumed, and a leader who is willing to spend time connecting the dots on even the small things."

That leadership component is even more critical at a time when so many transactions involve acquiring technical capabilities or moving companies into adjacent businesses. "The success rate of transactions, I'd imagine, is probably lower when it's about acquiring technology as opposed to [scale]," noted Dave Brous, president of dental APAC and specialty solutions at Henry Schein.

Acquisitions that bring a business into an adjacent space or redefine it as a multi-industry player involve a whole different level of risk than gobbling up smaller competitors, agreed TCS' Frank Diana. "There's significant risk inherent to any proposition that expands a company out of its primary industry into other areas, and that can be hard for stakeholders to embrace," he noted. "You're looking at the future and you're seeing a potential path for future value creation or a value proposition—but it's all brand-new stuff that an organization may have trouble absorbing."

However, failing to incorporate M&A in a company's transformation roadmap is just as risky, if not more so, than the potential for an acquisition stumble, agreed several CEOs, who cited dangers like being displaced by more aggressive peers or innovative upstarts. "In a lot of spaces, if you're operating at the $10 billion-plus scale, it's almost impossible to do meaningful development of new products," said Biederman. "Sometimes there's just no other way to do it."

In fact, embracing "acquisitional risk" may well be a competitive imperative. "You have to redefine that risk as opportunity," said Harrison. "Because you're either going to stay in this lane and still be in it in five years or you're going to have a vision of what this new marketplace is going to be and acquire one of the adjacencies to take your business from here to there."

Ultimately, creating a competitive advantage in an era of Uber-style disruption means moving beyond simply talking about adopting transformative technology to actually using it to manifest a reimagined and sustainable enterprise. Increasingly, CEOs are recognizing the advantages of buying rather than attempting to build their way into closing Business 4.0 gaps. "The most effective CEOs understand not only the need to embrace innovative processes, systems and business models, but the role M&A can play in accelerating that process," said TCS' Diana. "At the end of the day, continuously and optimally capturing value from mergers, acquisitions and divestitures should be a part of every CEO's playbook."

SIX STEPS TO SUCCEEDING AT IT INTEGRATION

1 **EMBRACE M&A**
Adopt the view that M&A is a strategic muscle that companies, especially those in mature and fast-consolidating markets, must exercise to remain competitive.

2 **BUILD AN M&A CENTER OF EXCELLENCE (COE)**
Assemble a core team charged with building critical skills, creating a deal "playbook" and using lessons from each deal to refine best practices.

3 **MEASURE, MANAGE, REPEAT**
Set aggressive timetables for identifying key IT-intensive business processes, applications, infrastructure and personnel to help ensure integration efforts are swift and effective enough to realize potential synergies.

4 **KNOW YOUR OPERATIONAL INFRASTRUCTURE**
Have an in-depth understanding of both companies' infrastructure to increase the speed of their IT departments' integration by as much as 35-50%, as well as ensure that superior systems and people of the combined entity don't fall by the wayside.

5 **ADHERE TO STANDARDIZED ENTERPRISE SYSTEMS**
Avoid the need to struggle to integrate different kinds of customized software by adopting a standardized enterprise system mindset—ERP, CRM, supply chain management, HR, etc.

6 **MAINTAIN NARROW INTEGRATION FOCUS**
Focus time and resources on the 20-30 percent of strategic processes and systems that provide core differentiation for the combined company.

Business 4.0

Intelligent, Agile, Automated, and on the Cloud

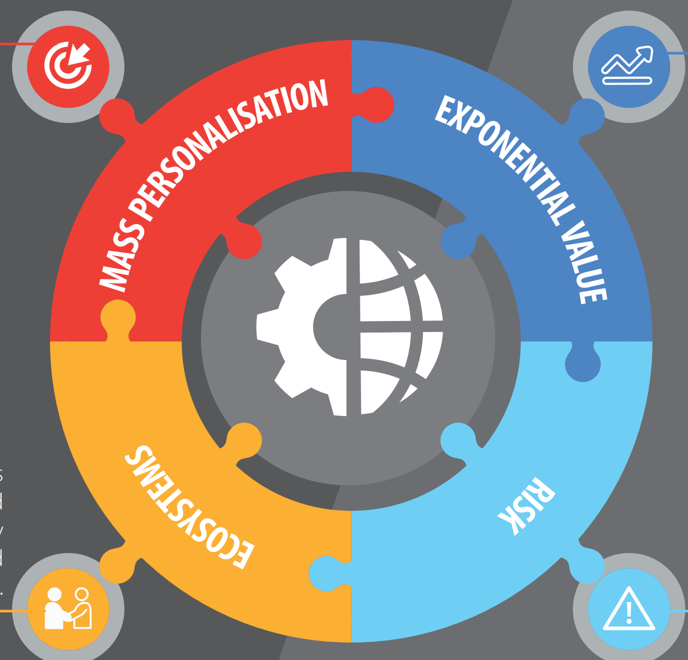
> *Applying the principles of Business 4.0 demands that organisations challenge deep-held operational assumptions and rethink relationships with employees, the wider ecosystem and competitors.*
>
> —Rajesh Gopinathan
> CEO & MD, TCS

WHAT BUSINESS 4.0 MEANS TO GLOBAL ENTERPRISES ACROSS INDUSTRIES

TCS is guiding many of its customers through Business 4.0 digital transformations—defining value propositions, creating new business models, winning over new customers, and creating exponential growth. Successful adopters of Business 4.0 will embrace its four primary characteristics.

Embrace greater segmentation and respond to individual transactions, customised for a single customer in a single instance.

Create "jobs to be done"-focused value propositions including best products, world-class services, instantaneous delivery, and incredible price points.

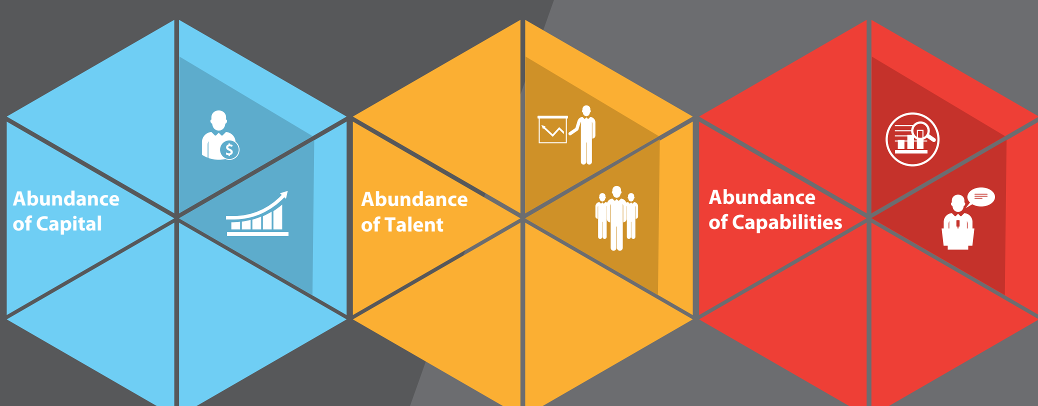


Rapidly tap into the capabilities and resources of partners and competitors through technology platforms to enhance value and supply chains.

Respond to threats and deliver new capabilities much faster, by rotating the risk-mitigation mindset 180 degrees to that of "embracing risk" and "adapting and transforming continuously."

HARNESSING ABUNDANCE FOR BUSINESS 4.0

Companies' infrastructure and assets are increasingly becoming insufficient to meet today's rapidly expanding needs. Business 4.0 organisations are shifting mindsets from "optimising scarce resources" to that of "leveraging abundant resources"—such as:



The convergence of **intelligence, agility, automation and the cloud** has allowed for the creation of **technology platforms to** effectively harness abundant resources in **real-time**.

Chief Executive

ABOUT CHIEF EXECUTIVE GROUP

Chief Executive Group, the leading community for business leaders worldwide, publishes Chief Executive magazine (since 1977), ChiefExecutive.net, Corporate Board Member magazine and BoardMember.com, as well as conferences and roundtables that enable CEOs to discuss key subjects and share their experiences with their peers. The Group also runs the Chief Executive Network, the leading CEO membership organization arranged by industry, and facilitates the annual "CEO of the Year," a prestigious honor bestowed upon an outstanding corporate leader, nominated and selected by a group of peers. Visit ChiefExecutive.net and BoardMember.com for more information.

TATA CONSULTANCY SERVICES

ABOUT TATA CONSULTANCY SERVICES (TCS)

Tata Consultancy Services is an IT services, consulting and business solutions organization that partners with many of the world's largest businesses in their transformation journeys. TCS offers a consulting-led, cognitive-powered, integrated portfolio of IT, business and technology services, and engineering. This is delivered through its unique Location Independent Agile delivery model, recognized as a benchmark of excellence in software development.
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