

Consulting
M&A Solutions

Culture Integration in M&A

Survey Findings

In 2011, Aon Hewitt surveyed 123 organizations from around the globe across various industries to learn more about culture integration during merger and acquisition (M&A) activity. We asked a series of questions to determine how culture was prioritized both pre- and post-close, what methods were used to integrate cultures and how successful organizations were in achieving their objectives. Our analysis revealed that although deal activity is on the rise and cultural integration is cited as a top priority during M&A activity, most organizations do not have a clearly defined approach to addressing culture.

This survey is the third in our three part series on hot topics in M&A.

Survey Findings

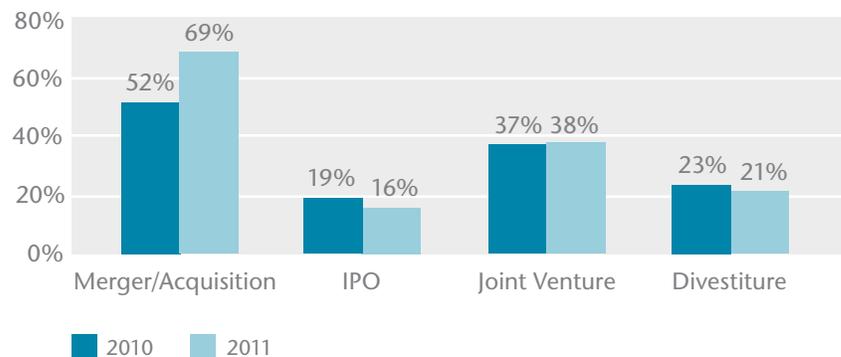
Deal Activity is on the Rise, it's Global and it's all about Growth

As the economy continues to rebound from the recent global recession, M&A activity shows signs of continued growth. M&A activity grew in 2010 from low levels in 2009, and is expected to rise even further.

Sixty-nine percent of organizations participating in our study anticipate an increase in M&A activity in the next one to two years and 38% anticipate an increase in joint ventures over the same time period. This compares to 52% of organizations anticipating an increase in M&A activity and 37% anticipating an increase in joint ventures in our 2010 study. This represents a 33% net increase in anticipated M&A activity in one year.

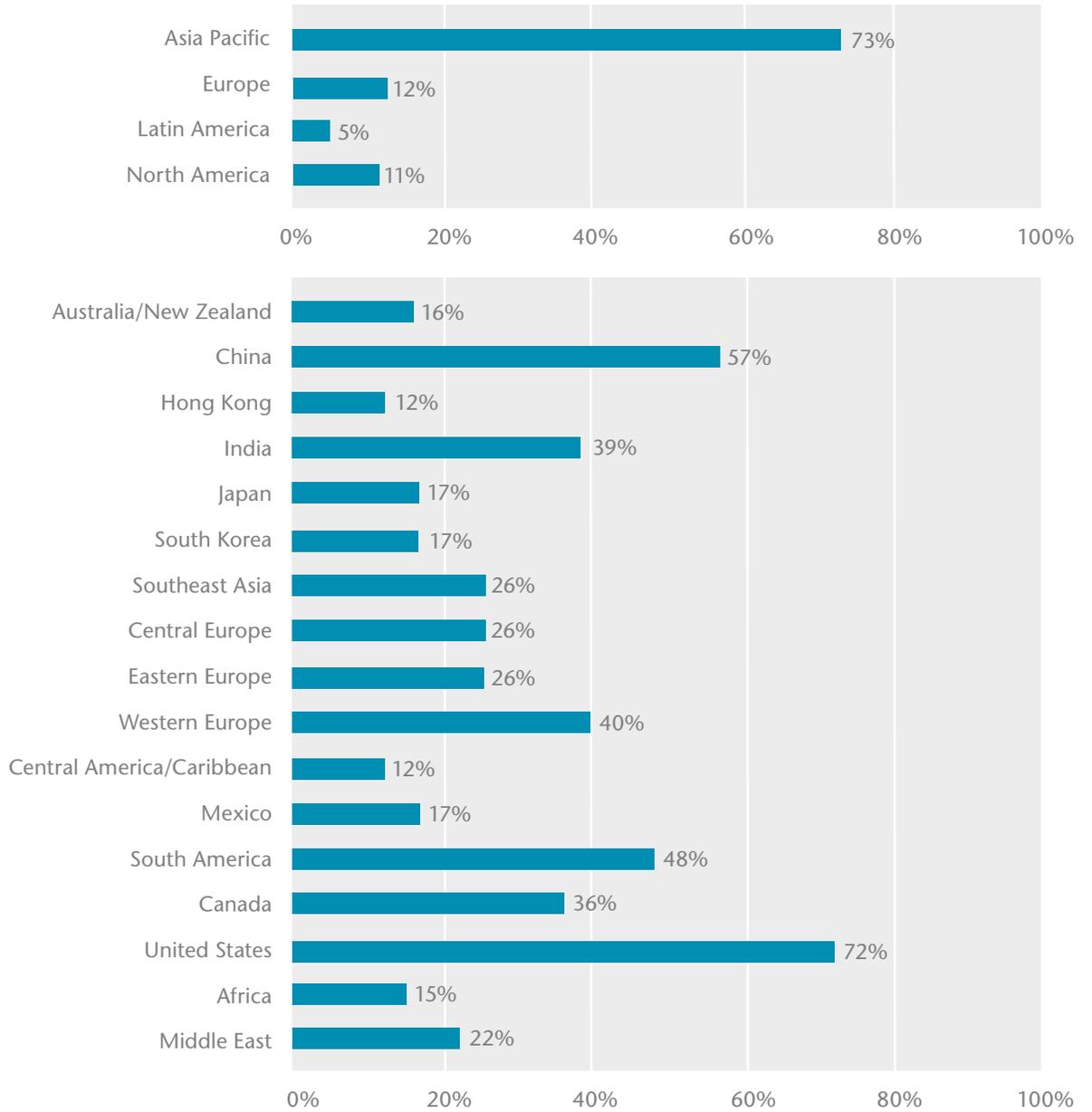
Level of Anticipated Transaction Activity

The anticipated level of transaction activity in the next one to two years (% of respondents)



**Anticipated M&A Activity—
by Country/Region**

The anticipated geographic focus of M&A activity in the next one to two years
(% of respondents)



Cross-Border M&A Trends As deal activity continues to be heavily global, a number of noteworthy trends in cross-border M&A activity are beginning to emerge. One interesting trend is that Asia Pacific firms are increasingly targeting the developed markets of North America and Europe for deals. Our survey indicates that nearly 50% of Asia Pacific firms are anticipating doing deals in North America and in Europe.

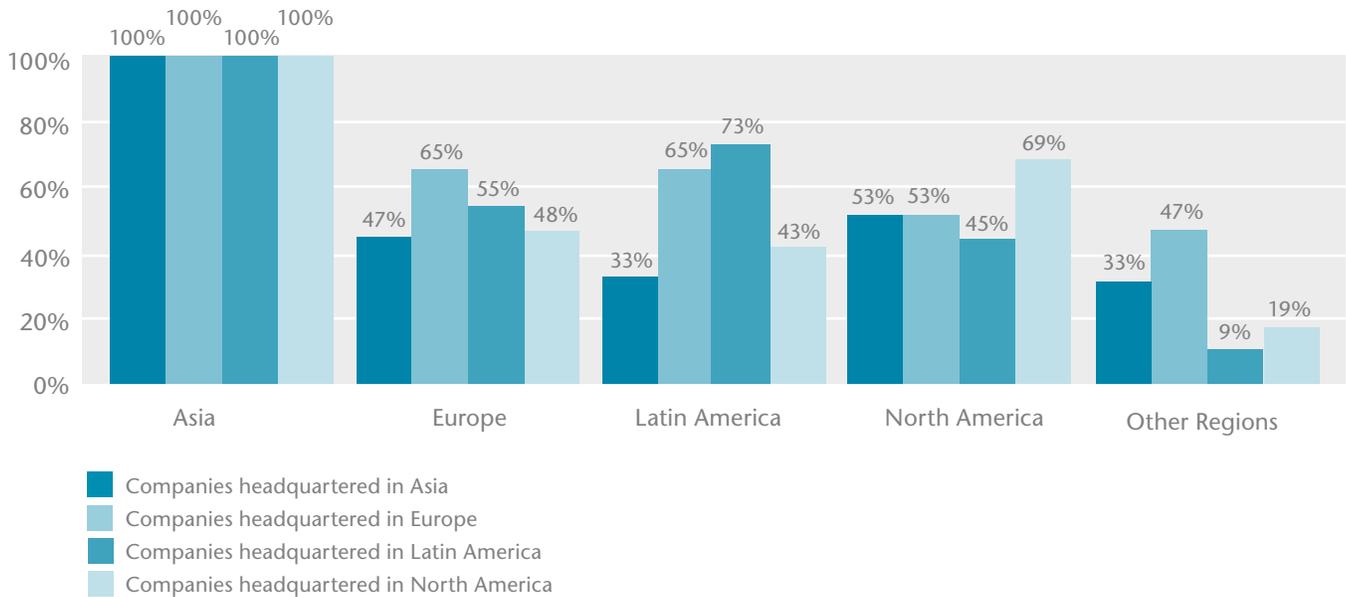
Meanwhile, firms in North America and Europe continue to look to emerging market opportunities and are targeting deals in Asia Pacific and South America, among other places. For example, 100% of both the North American and European participants in our survey indicated that they anticipate doing deals in Asia Pacific in the next two years. The following charts highlight the cross-border M&A trends observed in our survey. The first chart shows the trends in anticipated deal activity based on the region in which companies are investing (inbound M&A perspective). The second chart shows trends in anticipated deal activity based on the headquarter region of participants (outbound M&A perspective).

Deal activity continues to be heavily global in nature. Over 60% of companies in our study anticipate being involved in global deals (deals outside of their headquarter region), with Asia Pacific being the region most targeted for M&A activity, followed by North America and then Europe.

Inbound M&A Trends

Level of anticipated cross-border deal activity by region in which deals are anticipated to occur (inbound perspective)

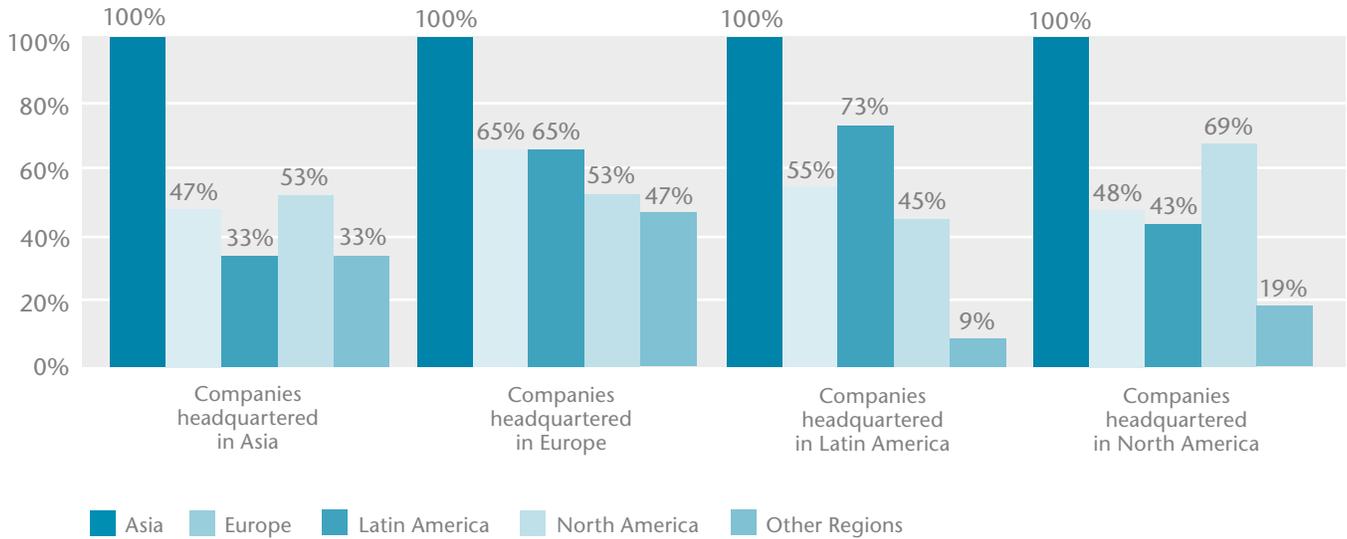
(% of respondents)



Outbound M&A Trends

Level of anticipated deal activity by headquarter region of acquiring company (outbound perspective)

(% of respondents)

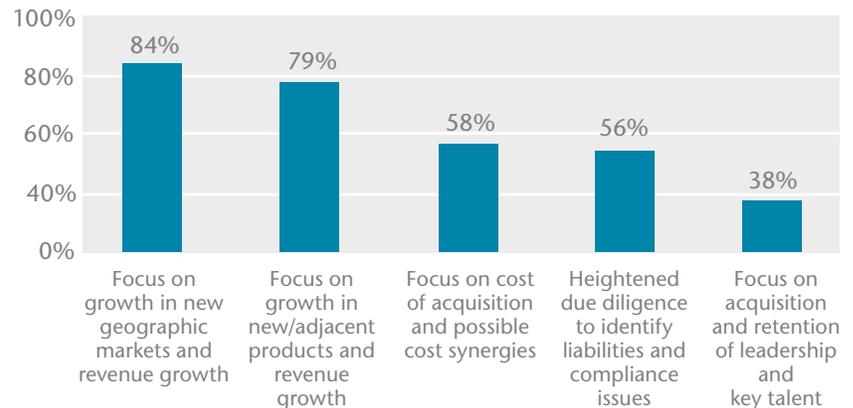


Focus in M&A Activity

Consistent with the emerging theme in our 2010 studies¹, M&A activity continues to be increasingly focused on growth rather than cost savings. While firms are keen to realize cost synergies as they engage in deal activity, their focus remains firmly on achieving growth in new geographic markets and in new adjacent products. This focus comes as firms seek to expand on the heels of the global recession.

Key Areas of Focus

Top two areas of focus in M&A activity over the next two years (% of respondents)



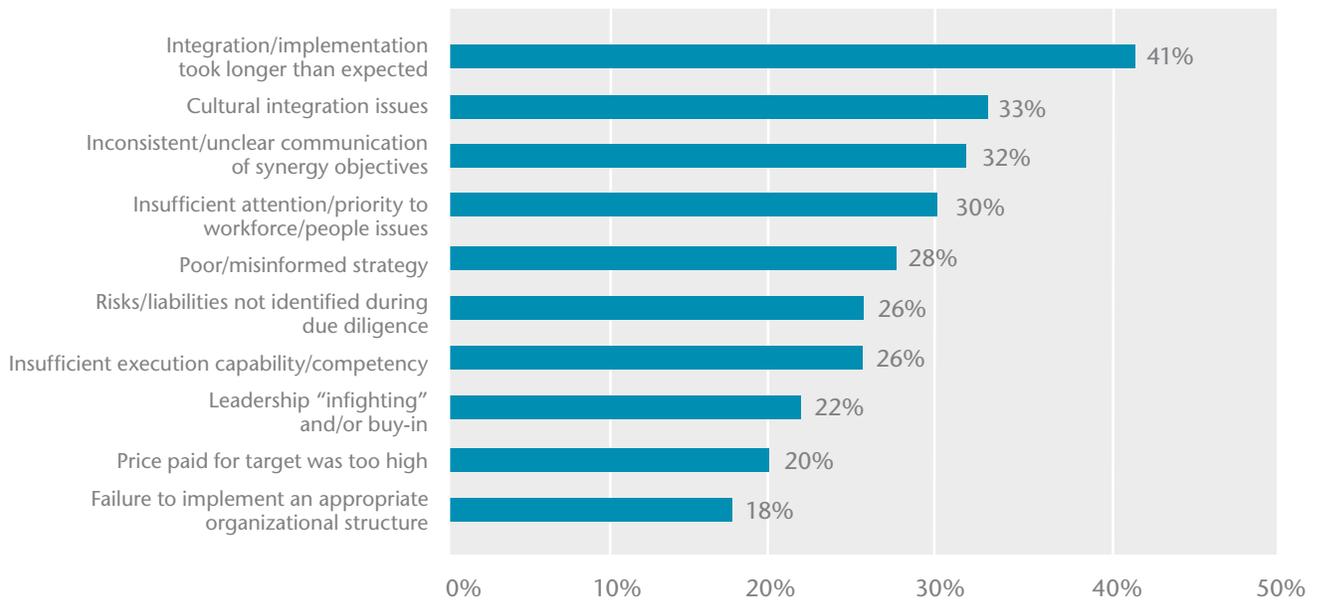
¹ Diagnosing Leadership & Key Talent Practices in M&A (2010) and Total Rewards in M&A (2010)

Deal Activity is on the Rise but Deal Success is Not; Failed Cultural Integration is a Top Direct and Indirect Contributing Factor

While it is clear that deal activity is on the rise, it is not clear that firms are any more successful than they have been in the past at achieving stated transaction objectives. In fact, the rate of deal failure remains alarmingly high. Nearly 50% of companies in our survey reported that they had failed to achieve stated objectives in past transactions. Additionally, over 50% of organizations lose their key talent at the same or even higher rate than non-critical talent. Companies indicated that a variety of issues contributed to deal failure as illustrated in the chart below.

Contributing Factors to Deal Failure

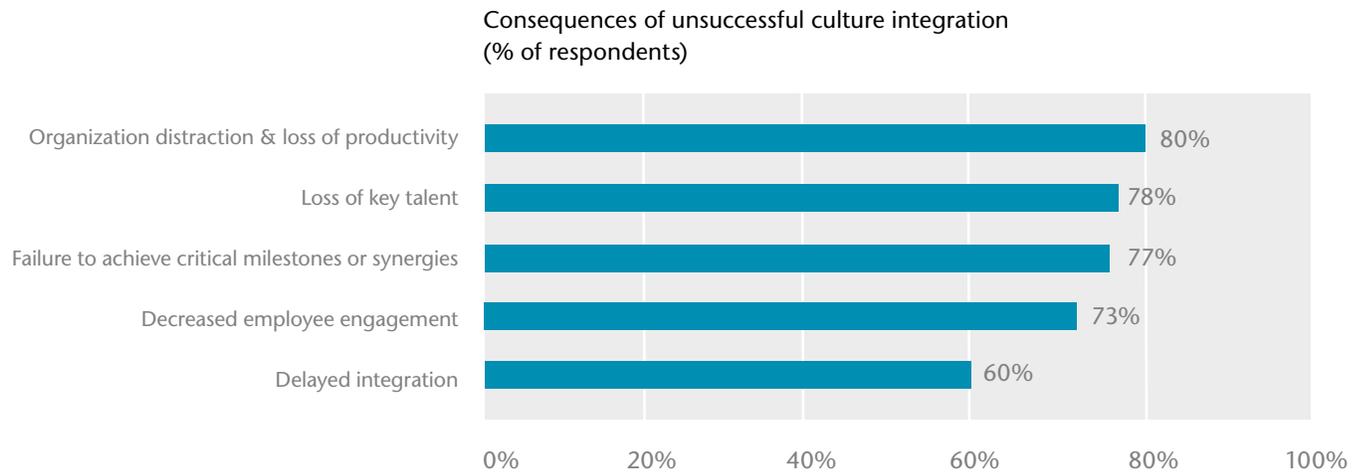
Top 10 drivers of deal failure (% of respondents)



As the above chart indicates, cultural integration was the second most common direct factor cited for deal failure by companies in our survey and has increasingly become recognized as a top issue in M&A.

But, in addition to being cited directly as a leading cause of deal failure, culture integration is also linked as an underlying, indirect driver to a number of other immediate causes of deal failure, including delayed integration or implementation (the most common factor cited for deal failure). Our survey confirms that culture is indeed a key underlying force in many of the most vexing challenges experienced in a deal from both a people perspective as well as from an overall business perspective. The chart on the following page highlights the top areas where culture has both a direct and an indirect linkage to deal failure by highlighting the consequences of unsuccessful culture integration.

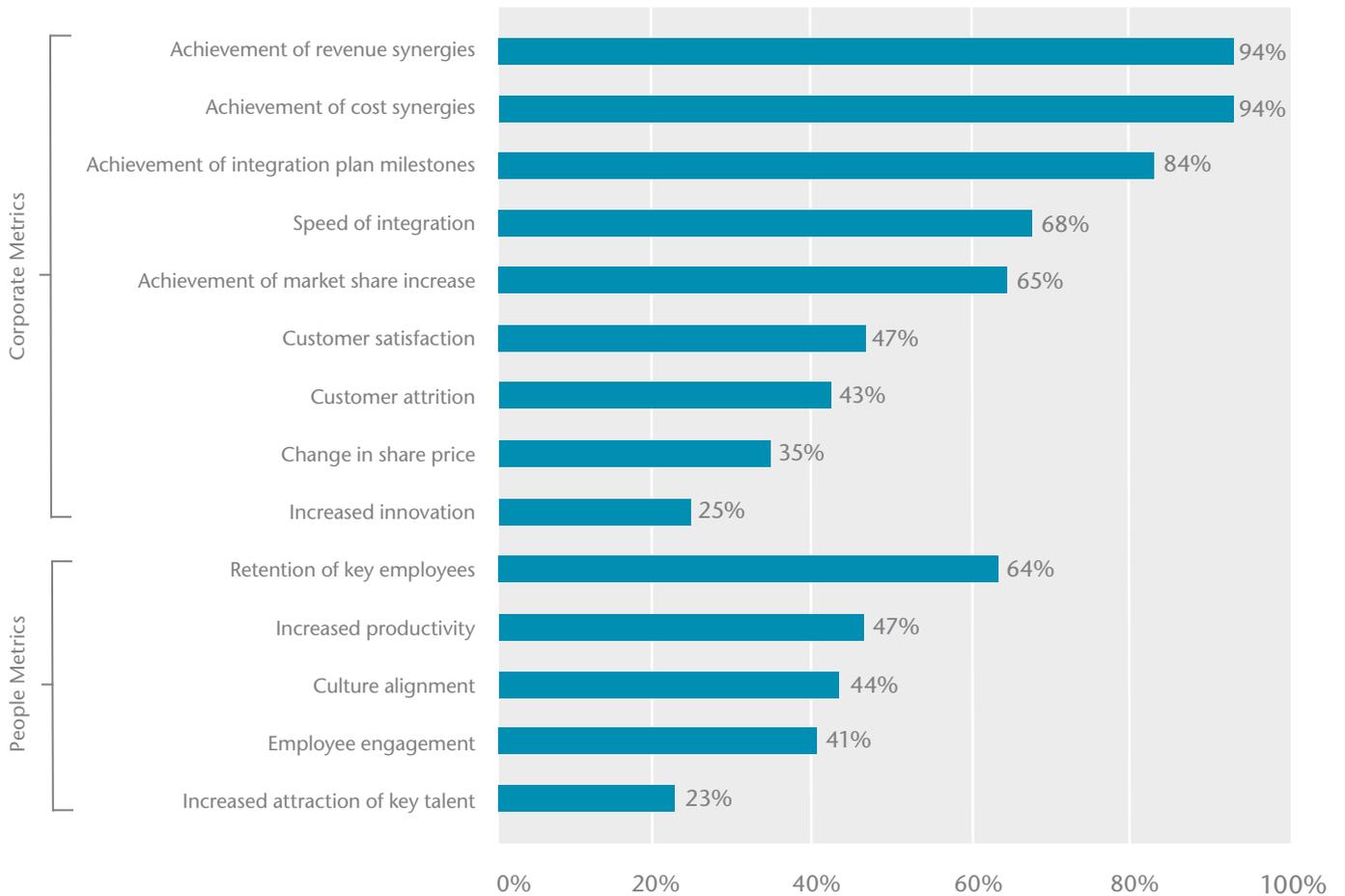
Impact of Culture on Deal Success



As reflected in the chart above, many of the consequences of unsuccessful cultural integration are direct drivers of deal failure. However, despite the clear linkage between culture and deal success, many organizations fail to even track culture and other people-related metrics as part of their overall transaction metrics. Although nearly 80% of respondents in our study track formal measures of deal success, a significantly lower number track culture alignment (44%) as well as some of the other key people-related metrics that the survey has shown to be directly related to culture alignment. Given the significant influence of culture on deal success, it clearly is a topic that leaders cannot afford to ignore during a deal.

Measuring Deal Success

Key metrics used to measure deal success
(% of respondents)



The Culture Conundrum: Companies know it's important but don't know what to do

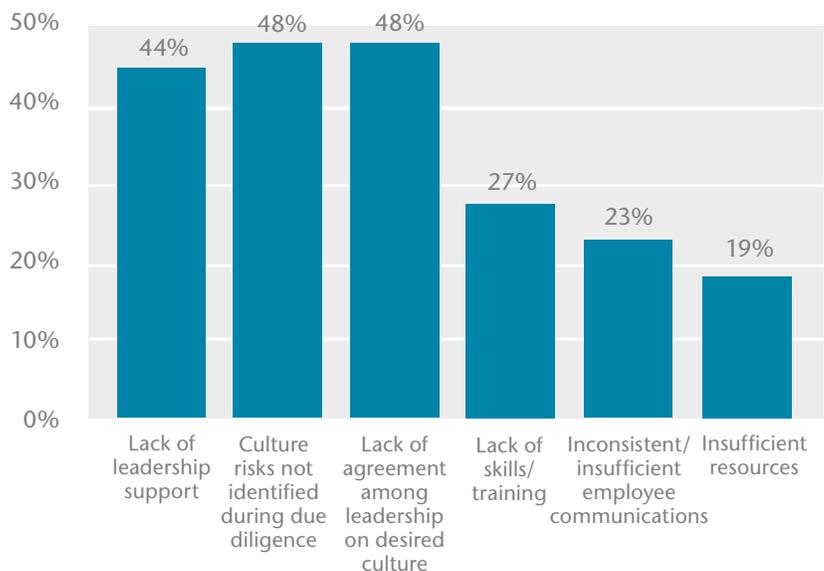
While successful cultural integration is clearly a critical element in deal success, many companies do not know how to successfully navigate it during a transaction. **Fifty-eight percent of companies** reported that **they did not have a specific approach to assessing and integrating culture in a deal**. Of those firms who lost critical talent at a higher-than-normal rate during a transaction, 68% did not have a specific approach for culture. Further, none (0%) of the responding organizations in the survey reported that its cultural integration practices were effective.

According to Elizabeth Fealy, EVP and Practice Director of Aon Hewitt's Merger and Acquisition Solutions practice for the Americas, "This is very telling. The bottom-line is that while organizations understand cultural integration is critical to deal success, they continue to struggle to translate their assessment into actionable initiatives that drive cultural integration forward."

Interestingly, while nearly half of organizations rank culture assessment and integration in the top three areas of importance in due diligence (30% rank in top two priorities), we see a drop in prioritization during integration (only 24% rank cultural integration in top two priorities), just when organizations have more access to information and employees. Based on this declining focus, it is also no surprise that we see lack of leadership support and resource commitment among the top contributing factors to unsuccessful cultural integration. To achieve successful culture integration, a proactive approach to culture that has the firm support of leadership is critical.

Contributing Factors to Unsuccessful Cultural Integration

Top reasons cited for unsuccessful cultural integration
(% of respondents)



Three Practices Around Culture that Make a Difference

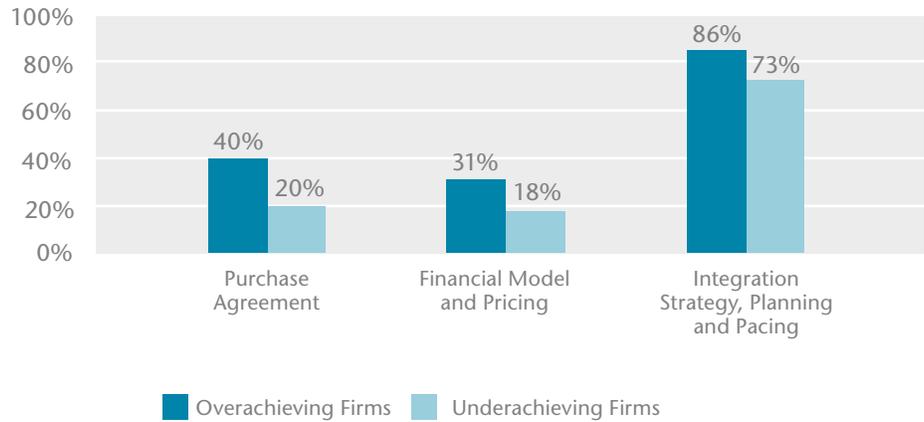
Aon Hewitt continues its comparative analysis of “Overachievers” (those organizations that exceeded some or all of their deal objectives and targets in past deals) to “Underachievers” (those that did not) to understand the contributing factors to transaction failure. When it comes to culture integration, we found three key differences that separate Overachievers from Underachievers and fuel their success in meeting deal objectives. First, Overachievers focus on culture early, starting during the due diligence process. Second, Overachievers spend more time on culture and build dedicated approaches to address culture. Third, Overachievers communicate change more proactively than Underachievers. While Overachievers do not yet believe they have the final answer on cultural integration, their approach has certain distinctive characteristics that make them more successful.

1. **Focus on Culture Early and Walk the Talk.** Overachievers’ timing and effort around cultural assessment and integration are better aligned to the transaction lifecycle and have more meaningful results. Overachievers are strongly focused on acting during the time between when a deal is announced and when it closes. While **Underachievers rank culture as a higher priority** in due diligence than Overachievers (37% vs. 21%), **Overachievers actually spend more time on culture** during due diligence.

Further, cultural issues influence the transaction terms and underlying financial model at a materially higher rate for Overachievers than they do for Underachievers. The purchase agreement, financial modeling and pricing and integration strategy, planning and pacing are all impacted at a significantly higher level for Overachievers in relation to Underachievers. The chart on the following page illustrates how addressing culture early on in the process can impact these key components of the deal process and how Overachievers influence the purchase agreement and financial model, in advance of close, at a two times higher rate than Underachievers. By focusing on culture early, firms can set the stage for a more successful transaction and effective integration.

Key Deal Process Components Impacted by Culture Efforts

Deal process components influenced by culture integration efforts (% of respondents)

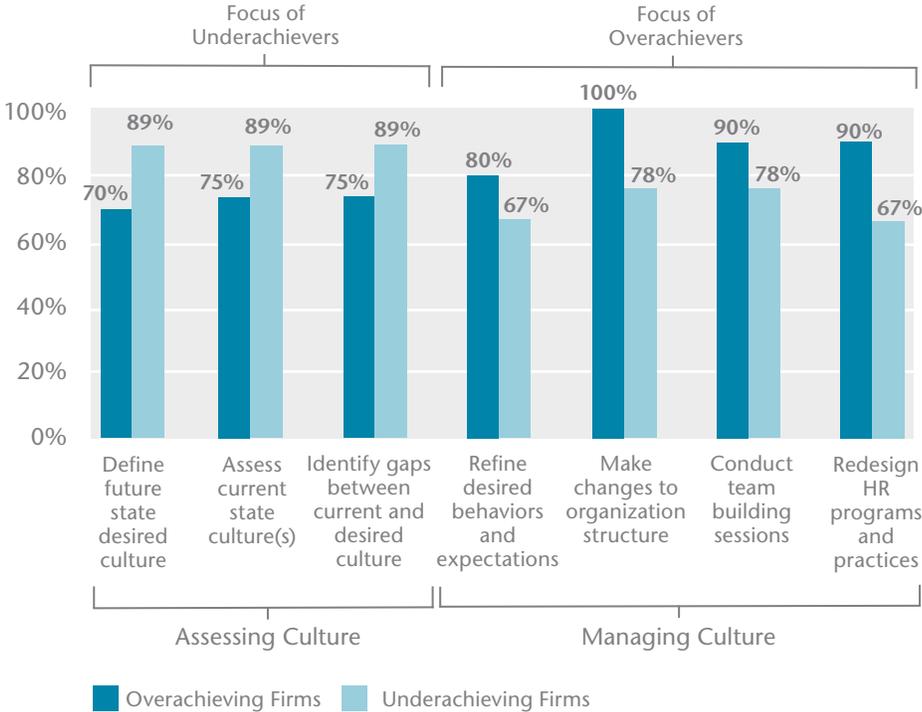


2. Spend Less Time Assessing and More Time Proactively

Managing Culture. Overachievers also spend more time managing culture and less time assessing culture as compared to Underachievers. **Eighty-nine percent of Underachievers** said they focused on assessing current state cultures, defining future state cultures, and identifying gaps between current and future states while **over 90% of Overachievers focused on making changes** to organizational structure, redesign of HR programs/practices, and team building sessions. By focusing more on managing culture, Overachieving firms direct their efforts on actually addressing the challenging culture-related issues that may arise during integration.

Culture Management Focus

Top areas of focus in culture management during a transition (% of respondents)



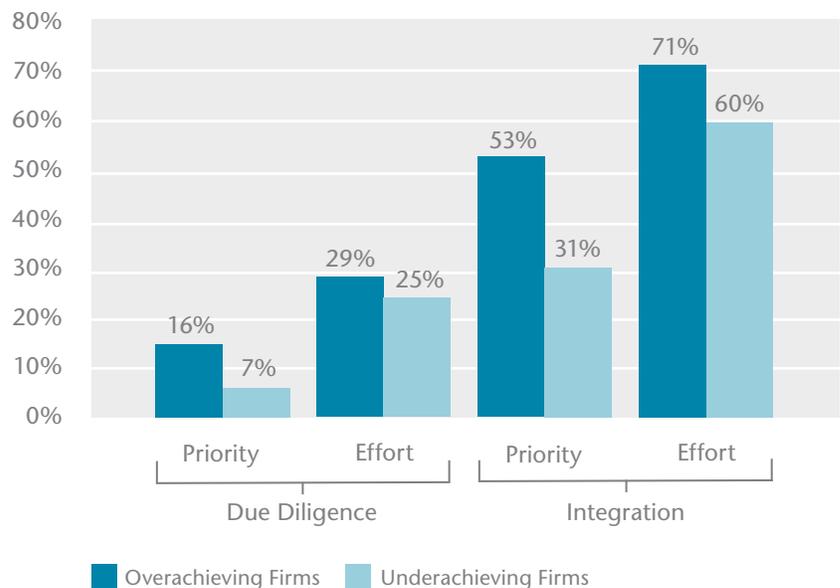
3. Communicate and Actively Manage Changes to Culture.

Finally, Overachievers placed more emphasis and spend more time on communicating and managing change during a transaction than Underachievers. **Overachievers rank communication and change management as one of their top two highest priorities** during integration, trailing only retention of leadership and key talent during integration in priority level (53% for Overachievers vs. 31% for Underachievers). They also invest their time in supporting cultural integration from a change management perspective. Overachievers also focused on communicating around culture (85% vs. 78%) more than Underachievers. The priority and investment of time that Overachievers placed on change management and communications during both due diligence and integration indicates that managing and communicating change starts early and continues throughout the lifespan of a deal for successful firms.

Focus on Change Management and Communications

Level of priority and effort placed on change management and communications

(% of respondents)



Aon Hewitt's Point of View

While organizations recognize that culture is important and that it is a top contributor to transaction failure, they often struggle to determine how to successfully integrate two cultures. Aon Hewitt recommends the following approach to achieve a successful cultural integration.

1. **Have a point of view on culture.** While culture is not good or bad, there are certain high performing culture profiles that are more supportive of specific business strategies. Organizations should try to implement a cultural profile that is aligned with their specific business strategy during integration. Determine early on what a high-performing culture looks like for your business. The chart below shows what typical high performing cultures look like for certain business strategies.

High-performing Culture Profiles

All High Performing Companies	Primary Strategy within High Performing Companies				
	Innovation	Customer Service	Quality	Cost Leadership	Niche Player
Decisive	Decisive	Decisive	Proactive	Enterprise-focused	Proactive
Long-term oriented	Risk-taking	Open/Transparent	Long-term oriented	Long-term oriented	Long-term oriented
Proactive	Long-term oriented	Long-term oriented	People-oriented	Collaborative	Decisive
Open/Transparent	Proactive	Proactive	Open/Transparent	Results-oriented	Risk-taking
People-oriented	Growth-focused	Action-oriented	Decisive	Decisive	Enterprise-focused

Bold = Unique strategic cultural characteristic

Source: Aon Hewitt Engagement 2.0 Study, 2010

2. **Focus not only on the “what” but the “how” of culture.** Often we see organizations focus on the comparison of cultural traits (**what the culture is**) and ignore cultural drivers underneath those traits (**how culture works**). By analyzing the drivers of culture, organizations will have concrete data on cultural opportunities and obstacles and will be able to develop an action plan to drive cultural integration. The chart below shows a sample framework for analyzing the drivers of culture and illustrates how specific drivers of culture work by identifying the level of threat or opportunity to the organization posed by each driver. This type of analysis helps identify where culture integration efforts should be directed and helps take the conversation around culture from theory to practice.

Culture Driver Analysis

Example analysis of threats and opportunities in culture integration



Source: Aon Hewitt Culture Impact Analysis, 2010

3. **Actively manage the cultural integration process.** Develop a holistic plan for managing the cultural integration process. This includes defining specific targets to gauge progress, ensuring cultural work streams are aligned and relevant to business processes, conveying how and why culture is experienced at the employee level and developing a comprehensive change and communication plan. This gameplan will not only make managing the cultural change easier but it will provide leadership with a clear, tangible roadmap to follow and garner more leadership buy-in and commitment (currently the primary cause of culture integration failure-see page 9).
4. **Take Action.** Address the cultural drivers identified in your culture assessment and take action accordingly at the organizational, program or individual level. Ensure that these activities are visible, coordinated and driven to demonstrate your commitment to building an action-driven culture, which is a cultural trait that is universally shared by companies with high-performing cultures across all strategy types. Active management of culture is key to successful integration and ultimately realizing deal objectives.

In Summary Our study confirms that deal activity is on the rise and will be carried out on a global level as firms look for growth in new markets and products while growing their core businesses. While deal activity continues to increase, deal success continues to be challenging, with nearly half of all deals failing to meet their objectives. While the causes of deal failure are complex and varied, culture is one of the big obstacles hindering deal success and is a driving force behind many other immediate causes of deal failure. While there is no single best approach to cultural alignment, addressing culture early on, developing a point of view on culture, focusing on the “how” of culture, actively managing culture during integration, and, above all, simply taking action around culture can directly contribute to a successful transaction.

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