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In a changing world, people are critical to M&A

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Originally published on BRINK news on May 26, 2020.

While events driven by COVID-19 have not stopped the world from turning, they certainly have shifted the axis a bit. Amidst the loss and suffering, business leaders are pivoting from responding to these events to planning a path forward for their organizations. A prism of moderating costs, mitigating risks and maximizing value guides this planning — along with an emphasis on empathy as well as economics, as the workforce adjusts to new realities in a post-COVID-19 landscape.

An underlying urgency — rarely, if ever seen before — influences this planning. Leaders face a sobering laundry list of to-dos, such as performing a realistic review on balance sheet health, re-evaluating their business model (including supply chain changes, consumer interaction and workforce environments), and dealing with external pressures from investors and shareholders.

The urgent need to move forward will require a look at both organic and inorganic strategies. This includes a return to deals. For some organizations, divestitures will generate the cash needed to survive in a radically changed environment. For others, the combination of a relatively stable balance sheet and greatly reduced valuations will present an unparalleled opportunity to transform the business through an acquisition or joint venture. What COVID-19 has not changed is this: People remain critical to driving deal value.

A call to action — Strategically addressing people risks

The idea of capital-P People being the value catalyst in deals is nothing new. The majority of deals fail. One of the most commonly cited reasons is the failure to adequately and strategically anticipate and address people issues. Yet in the 1,200 deals Mercer's global M&A Advisory team works on each year, we continue to see business leaders put people risks in the tactical bucket versus more strategically considered areas such as operations, supply chain, tax planning or legal and regulatory considerations.

It is unlikely that a CEO would say, "Can we just address the tax and regulatory issues of this deal post close?" Yet more often than not, this is the mindset related to people risks. The increased business risk due to the uncertainty and the reduced timeframes due to the opportunistic nature of deals in the current macroeconomic environment make this reactive posture even more likely. Leaders who identify and plan for these people issues early and strategically will be building a foundation for delivering full value.

In addition to defining people issues in a mostly tactical sense — relegated to paychecks and benefits, mainly — the topic of people is often dismissed as too conceptual to address strategically. That does not have to be the case. Ten elements ultimately shape the people dynamic at any organization, but note that the criticality of each element must be determined on a deal-specific basis: Vision, Mission and Values leads the list, followed by Leadership, Organization Design, Governance and Decision-making Rights, Communication Style, Work Processes, Work Environment, Rewards & Recognition, Talent Management, and the Employee Value Proposition.

Current events are causing business leaders to rethink everything about their business models and how they and their organizations consider the people elements in future transactions.

Taken as a whole, these elements represent an organization's operating environment. They message and reinforce intentionally and unintentionally on a minute-by-minute basis how leadership wants business conducted. This will be true for a potential transaction partner. These elements are, or should be, part of any deal thesis development and analysis. Questions that need answers include: What are the most critical elements in achieving strategic objectives and financial, modeled values? How will the transaction affect the current operating environment? How aligned or misaligned are these elements between the organizations involved? What actions will align or keep aligned the most critical elements?

As with other areas of the deal, the evaluation of people issues is not a one-time event. It should involve the constant testing and refining of an initial thesis. This strategic consideration is at the core of successfully anticipating and navigating issues that will negatively influence your ability to deliver value.

Deal types frame the people risks

An urgent need in some organizations to create business sustainability and in others an opportunity to transform is expected to fuel increased deals activity over the next six to 12 months. In recent polling, approximately 40% of respondents indicated the current market conditions would not change their deal strategy over the next 12 months. There are patterns to the inherent people risks in different types of transactions. While each deal brings its own unique set of circumstances, it is possible to anticipate these risks in your initial deal thesis creation and prioritize them in early due diligence. Following are the anticipated near-term deal trends and associated prioritized people issues.

Joint ventures and partnerships
These deals provide a path for pursuing new business models (e.g., supply chain reconfiguration or digital transformation) while dampening some of the risk and capital requirements present in other deal structures. Business leaders often underestimate the associated people risks that work to destroy value creation. Key people issues that need to align with performance objectives are organization design, governance, leadership selection, incentives and talent retention.

Divestitures
Many organizations will leverage divestures as a way to stabilize their balance sheet and pursue new strategic imperatives. Key people issues include understanding the impact that the spin-off will have on workforce costs at both the remaining company as well as the carve-out, selecting talent to stay versus go, determining retention strategies for key talent, and executing the required stand-up expectations (e.g., Transition Services Agreement delivery or full Day One functioning).

Acquisition of distressed and devalued assets
For financially well-positioned organizations, this is an opportunity to acquire assets that were previously unattainable. This type of opportunistic acquisition involves people risks including selecting the right leaders to capture the intended value, retaining key employees to drive the value and creating aligned incentive programs.

Current events are causing business leaders to rethink everything about their business model and related processes. Just as importantly, leaders need to rethink how they and their organization consider the people elements in future transactions. Let this be a wakeup call around how to approach deals moving forward. Early and strategic consideration of these elements will set the foundation for successfully mitigating risk and delivering value — in a post-COVID-19 business climate that focuses on the human factor as much as the financial one.

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