Merger Mania – An irresistible temptation

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Mergers & Acquisitions are changing the face of MR with a vengeance. Two insiders report from the war room presenting the innards of M&A transactions and explaining the dominant interests of the key players.

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Has anything in our profession – be it stratified probability sampling, ethno-based consumer insights or CRM – made so many people so happy or unhappy so quickly as the string of mergers and demergers, acquisitions and sales: tying and untying in rapid order a wide and wild diversity of research companies all over the world?

It affects everybody: founders who harvest, buyers who boast, sellers who smile, clients who wonder and employees who look every which way. No wonder that each issue of industry newsletter *Inside Research* fascinates readers with another report on 'merger mania'. Since Jack Honomichl founded IR in 1990 he and editor Larry Gold have reported on more than 500 deals under this headline.

M&A has changed the face of market research with a vengeance. It was, and in many respects still is, the express route to the worldwide coverage that the beloved Global Key Clients (read, the 50 international companies who spend more than US$ 75 million annually on research) are asking for. And it is the way to scale, to new technology, branded products, business sector expertise, market share and to dominance.

Many sometimes beautiful, sometimes acrimonious deals unfold before the eyes of a curious public in full daylight. But then, some of the realities of the M&A business are a little less easy to discover.

The metrics of ordinary deals

There have been enormous deals. Dutch media conglomerate VNU paid a combined US$ 5 billion for Nielsen Media Research and ACNielsen. Interpublic valued NFO, itself an ultra-active acquirer through the Nineties, in 2001 in a share deal at an initial worth of some US$ 850 million. This summer TNS acquired healthy NFO from Interpublic for some US$ 425 million. The debt-plagued advertising giant desperately needed the cash.

But, 25 companies now control 63% of world research revenues and another 5000 potential acquisition targets share the rest. five countries attract 83% of world research revenues and there are 150 more countries for the Top Ten to conquer some day.

According to *Inside Research*, during 2001 and 2002 the Global Top 25 acquired 71 research firms with an average revenue (ex Nielsen) of US $11 million. Some players are seen at many parties: Kantar, TNS, GfK, Ipsos and late-but-fast entry Synovate have each done more than 10 deals in these two years. A normal success rate is one deal completed out of five to ten tries. Between 1998 and 2002 US agencies alone have finalised 152 transactions. The median value of these deals (ex Nielsen and NFO) hovers at around just US$ 4 million. Plus there are the vast majority of deals between mid-sized companies who desperately try to escape the so-called 'squeeze of the middle': big research companies will thrive – as will niche companies. Other places may get increasingly more uncomfortable.

An ego no price can match

Founders of agencies may secretly wonder how much they would get if they ever sold their precious brainchild. Some develop an ego no price can ever match. Others stay in their comfortable Chairman's seat until it is too late for proper estate planning. Smart entrepreneurs start the grande finale in good time.

All the Top Ten have highly developed M&A standards, tools and procedures, sometimes more standardised and sophisticated than their core business. Their targets can't match this in-house expertise. But they can buy the services of competent external advisors, perhaps the best ▶

investment they will ever make. Key players and intermediaries in M&A transactions are:

- investment advisors: experts in the whole M&A process management (investment bankers like Goldman Sachs are powerful allies but affordable only for the crème de la crème);
- commercial bankers, providing growth money for the ordinary course of business as well as financing acquisitions;
- attorneys/lawyers: normally specialised and seasoned in the intricacies and pitfalls of international M&A;
- auditors: providing very detailed information and opinion on the seller's side, meticulously checking thousands of data and documents with any potential relevance for buyers;
- tax advisors: quite complicated structures are necessary to optimise the tax requirements of two parties of normally very different size and ownership structure.

A good sale need years of careful preparation

The inner mechanics

M&A deals affect many people including clients and researchers for whom M&A's are quite frustrating. Many rumours and wild speculations, then total silence and - bingo, a memo from the desks of the CEOs to the public, to the stock market, to shareholders, to clients and, yes, finally also to the cherished employees. But who could ever design a truly satisfying communication process? Negotiations are always complex and competitive, volatile and vulnerable. The pressure gets evident when one looks at the main stages of an acquisition process:

The cold phase: A good sale needs years of careful preparation, generating the maximum value of an agency for the moment of truth. An owner has to decide which value drivers to push: design competence, regional coverage, sectoral expertise, key client control, branded products, advanced technology? He should also decide what kind of transaction to envisage: own acquisition, cooperation, joint venture, merger or eventually an outright sale? And finally, which timing to choose to retain maximum flexibility, feeling out the future state of the economy, the stock market and the company itself?

The warm-up phase: A delicate and dangerous phase, full of crucial decisions. From the first informal meeting... who takes the first step? Is this the golden opportunity? Turning to a financial or a trade investor? Through many tactical manoeuvres... Exclusive talks? Simultaneous negotiations? Auctioning?
This is the peak time for the 'sales team', consisting of internal top decision makers and their M&A advisers, all constantly trying to outsmart their counterpart while going through the ups and downs of painfully slow and then suddenly ultra-fast moves, wrestling for the draft of a deal or a letter of intent.

The hot phase: The highest hurdle, agreeing on price and conditions. Both sides will insist on their preferred evaluation method, running complex financial models. Valuation is applied mathematics and pure combat - interpreting the past and forecasting the future; mountains of data to be disclosed and verified in 'due diligence' procedures.
The dream of each publicly listed company is a purchase price which is 'immediately accretive' meaning that the acquired company will contribute more to the next consolidated p&l than the cost of the capital invested. This is an ambition rarely fulfilled. Study after study has shown that most acquisitions destroy wealth of the acquiring company's shareholders (there are no statistics that M&A in market research fares better or worse).
At the end of all the negotiations: a final set of contracts and enclosures (under Anglo-Saxon law easily exceeding a thousand pages) and the permissions/approvals of numerous governing bodies and authorities.

The 'after-sale-service' phase: Buyers want predictability. Many transactions are therefore structured as a multi-step-deal. The buyer initially acquires only a minority/majority stake. The remaining shares may be bought or sold during the next few years according to artfully predefined rules (put and call rights).
Price packages often contain earn-out elements, where parts of the compensation are dependent on meeting certain key performance indicators in the future. A successful transition also needs a well 'incentivised' management, contractually and financially chained closely to the company.

Creating new jewellery from old gems

Some mergers fail to deliver, suffering from naked under-integration or from ruthless over-integration. Earn-out and incentive elements do not incentivise an acquired management at all to go for the highest value-added to the business of their new owner. And even the most seasoned buyers often face inordinate difficulties in this people-business to achieve a well-balanced in-corporation of 'New Members of the Group', skilfully converting old gems into new jewellery.
Many agencies lose culture and competence when joining conglomerates, diluting value for their puzzled clients who only want to benefit from superior, smartly integrated services. In M&A joining forces needs a very careful management ...and some new thinking. ■