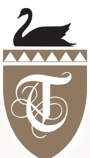
Synergy™ INSIGHTS

SUPPLEMENT

VALUE-CREATING ACQUISITION TARGETING

Active acquirers often use a combination of reactive and proactive approaches for targeting acquisition candidates. Acquirers are reacting when they respond to candidates identified by the "deal flow", which is the parade of more-or-less "for sale" businesses that are presented to an acquirer by sell-side M&A advisors, and sometimes solo by the selling businesses themselves. Alongside this reactive approach, or perhaps instead of it, an acquirer may target candidates proactively, using the acquirer's internal staff or an outside consulting firm to perform a candidate identification project.

Synergy Insights Supplement is a companion newsletter to Taylor Companies' business journal, *Synergy Insights*. For more information about *Synergy Insights*, please visit www.tay.com/publications.



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Candidate identification is typically performed according to a particular notion about the kinds of businesses that would be most suitable to be acquired. These notions of suitability are usually candidate-centric in that they are focused on the acquirer's benefitting from the positive characteristics of the candidate or the arena in which the candidate operates. By acquiring a target with such characteristics, it is assumed that the acquirer will automatically be benefitted. Such desirable attributes can include that the acquisition candidate:

- Is a size deemed desirable by the acquirer
- Is category or segment leader
- Has strong brands
- Has good IP
- Has attributes the market analysts like
- Is a business that the acquirer understands
- Plays in a higher margin product or market
- Plays in a higher growth product or market
- Has higher than average margins
- Has higher than average growth
- Is geographically proximate to the acquirer
- Has strong management
- Etc.

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Sometimes candidate identification may be based on acquirer-centric notions, in which the acquirer's *apparent* weaknesses or leverageable strengths are the drivers of the target identification process. In such cases, it may be that the candidate:

- Fills a product gap of the acquirer
- Fills an end-use market gap of the acquirer
- Fills a geographical market gap of the acquirer
- Is undercapitalized (assuming the acquirer has requisite financial strength)
- Lacks fiscal discipline (assuming the acquirer is fiscally disciplined)
- Etc.

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Both the candidate-centric and acquirer-centric targeting approaches listed above look so compelling on face value as to be self-evident and of unquestionable validity for use in the identification of acquisition candidates. However, even though compelling on face value, these candidate characteristics would not, by themselves, necessarily lead to maximum value creation through acquisitions.

For example, while it may obviously seem suitable to acquire a business that would fill a gap in the acquirer's own product portfolio, such an achievement may not maximize value creation unless the existence of the gap is causing loss of value to the acquirer. In other words, the presence of the product gap in the acquirer's business might not actually be a weakness. Similarly, any of the previously mentioned value-creating candidate characteristics that do not mitigate the acquirer's *actual* weaknesses or leverage the acquirer's *actual* strengths, may not create any value (i.e., synergy) beyond merely obtaining the existing revenue and profit streams of the acquired business.

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Therefore, any acquisition targeting methodology which does not begin and directly proceed from a detailed analysis of an acquirer's weaknesses and leverageable strengths, runs the risk of missing the goal of value creation. Further, the values of mitigating the weaknesses and leveraging the strengths need to be estimated, and the entire list of opportunities ranked in order of potential value creation, so that any subsequent acquisition candidate targeting efforts are focused on achieving maximum possible value through pursuit of the most value-creating acquisitions. The best and most value-creating acquisitions will be those that are profiled to mitigate the most value-suppressing weaknesses and/or leverage the most value-creating strengths.

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This approach results in maximum value creation through acquisitions, as has been the experience of the Taylor Companies who, by using this methodology, has achieved a 90+% success rate versus the 20-30% rate achieved by the more standard approaches discussed at the beginning of this article. Taylor's model, *The Twenty-Five Categories of Synergy*, presents a wide range of common business weaknesses and strengths, translated into the language of mergers, acquisitions, and divestitures. By using the model to discover a business' weaknesses and leverageable strengths, the implied pursuable synergies as well become known and ready for application in a candidate targeting exercise.

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WE WELCOME READER FEEDBACK

We are interested in your feedback and examples of synergy applied in acquisitions and divestitures with which you may have been involved. To share examples, or if you have questions, comments, or are interested in seeing a specific subject discussed, please contact us at SynergyInsights@tay.com, attn: Warren Bellis.

1667 K Street NW, Suite 200, Washington, DC 20006 • +1 202 955 1330 • www.tay.com

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