





There are many valid reasons why companies pursue mergers & acquisitions (M&A) as part of their strategic growth plan. These include portfolio diversification, addition of top-line growth, acquisition of key technology, geographical expansion, or some combination of the above.

However, the acquiring company is typically required to pay a premium (*i.e.* more than the current valuation of the target company) of up to 30% in order to win the deal competition, and to satisfy shareholders of the target company. In addition, it is widely held that the majority of M&A transactions fail to create shareholder value, or actually destroy it. So, why would companies overpay by up to 30%, and then be faced with an approximately 30% chance of actually realizing the value of the transaction?

While the drivers behind the deal premium are a separate subject, in this briefing we will discuss and introduce Post-Merger Integration (PMI) best-practices and defined processes whereby the odds of creating value from the deal can be dramatically enhanced. The tools and processes introduced are rooted in the decades-long experience of the authors with large-scale transactions and subsequent PMI work.

When contemplating an integration effort, a company may choose to design and execute the PMI without using outside resources. If the company has key executives and functional leadership with strong experience in PMI, this may result in a satisfactory outcome. However, in our experience this is frequently asking too much of the organization with regards to either bandwidth or experience, and the overall integration suffers. Unfortunately, as will be discussed later, the roots of the long-term consequences of poor PMI are often seeded in the early stages.

Perhaps the opposite position is taken by a company that rightfully questions its ability to capture the deal value with a successful integration. In this scenario, the company may commit to a very expensive contract with a large consulting company, with the concomitant outsized ranks of relatively junior consultants descending upon functional area leaders. This often results in disruption to the day-job of line management as the cumbersome integration effort gets bogged down in trying to come up with perfect answers to every organizational and logistical issue. This can also lead to a situation whereby the company representatives actually feel like they are working for the consultants, rather than the other way around.

## How Catenion Can Help

At Catenion, we believe in the value of a middle approach. Our experienced consultants understand your business and are experienced in the drug R&D process. Our approach is to pair our deep expertise in post merger integration, portfolio management and organizational effectiveness with our client's deep functional expertise. Doing this creates a high-performing team that can effectively derive the value from the deal. We serve vital roles as an external catalyst, conducting due diligence, building high-performance teams, and as an impartial third party. With staff in Europe, the United States, and Japan, we are also effective at bridging cultural barriers, whether they be geographical or organizational.

## Tell Me Again, Why Are We Doing This Deal?

The run-up to a typical M&A starts with a methodical process whereby the company evaluates various strategies for growth, selects a particular approach and then systematically narrows down the target companies that fulfill those criteria. However, once the target company has been approached, negotiations have begun and due diligence has commenced, the environment quickly changes. Competitors may emerge, the target company may insist on compressed timelines, concern over deal secrecy arises, and “deal-fever” leads to a desire to win the deal competition. All of this creates an environment in which the original strategic imperatives of the deal are at risk of taking second place to completing the transaction itself. Further, there can be considerable “horse trading” between the companies during last minute negotiations over roles & responsibilities, titles, independence, and salary. These strategic and tactical choices that are made even before the deal is announced can actually have a great influence on the success of the integration process.

During this pressure cooker environment, it is vital that the integration process has already been started, if only in nascent form. At a minimum, the integration lead should be identified and have visibility into the deal negotiations. It is vital that this integration lead reports to either the CEO, or one level below. Ideally, the Integration Core Office (more on this later) has been formed, and can actually serve as a sounding board about the proposed deal structure and organizational implications. The ultimate manifestation is the creation of a “clean-team” that has full access to the confidential data of the target company derived from due diligence. This team operates in complete confidentiality and prepares preliminary plans for the integration which follows.

In our experience the most important success factor in any PMI process is that a team of people who will be responsible for delivering the value of the deal clearly understand at the outset the strategic rationale, timing, cost synergies, and organizational impact of the final transaction.

### If you break it, you buy it

In stores, signs often inform shoppers that “If you break it, you buy it.” Unfortunately, many companies treat the M&A process as having been largely completed when the deal is announced, thereby setting the integration process up for failure. This leads to the opposite analogy of the saying, namely, “You bought it, now break it.”

### The Integration Team Structure

The key to avoiding this scenario is the creation and empowerment of the Integration Team (Figure 1). The role of the Integration Core Office (ICO), led by the integration lead, is to actively manage the translation of the strategic imperatives of the deal into concrete, meaningful goals, synergies, organizational structures, metrics and targets. This is done in conjunction with Integration Functional Teams (IFT), which are led by subject matter experts in functions such as R&D, Marketing & Sales, Operations, HR, and IT.

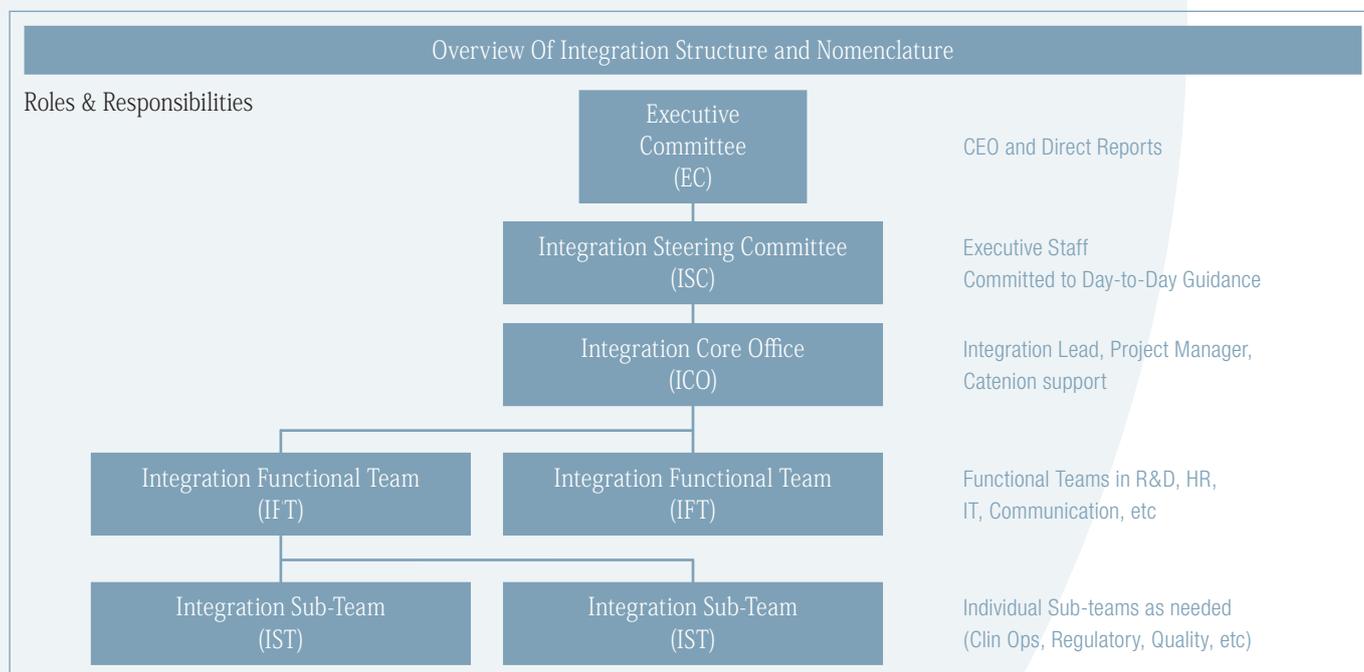
This team, together with a defined process & methodology known as the “Integration Playbook” are the drivers of PMI.

Key success factors in the formation of this team are:

- Selection of the integration lead. He or she should be a well-rounded executive who is broadly familiar with the organization, is effective at influencing others, is able to tolerate ambiguity while the situation on the ground clarifies, and is calm under fire. This person should have the absolute confidence of, and report to the CEO or one of his direct reports.
- Most companies underestimate the time required for integration activities. For absolutely critical teams (HR, IT, Communications, Portfolio Review, others depending on the specific scenario), the IFT lead should be prepared to provide a full-time commitment.

- A best-practice is to identify a program manager to serve alongside the IFT leader. This program manager is responsible for maintaining and reporting on the progress of the team.

Catenion can play a vital role in the formation and function of the integration team by providing executive coaching, helping to develop the integration plan and execution, as well as clarification and resolution of specific issues. In addition, since many integrations involve some selection or combination of the pre-merger project portfolios, we provide in-depth support of this vital role, as described below.



**Figure 1:** Creation of an effective integration team that clearly understands the strategic rationale and tactical impact of the deal is an essential part of successful PMI

## Post Merger Integration Process

*Translate Strategy to Goals.* All integrations are not created equal. Each M&A opportunity will require different organizational solutions, synergy targets, timing, and communication. For example, at the simplest level, the target company may operate as an independent unit within the newco, and require very little in the way of organizational alignment and infrastructure. At the other extreme, full integration would require complete blending of the structure, roles & responsibilities, compensation, and information systems. It is possible to have hybrid scenarios, where one part of the target company is set up to operate independently, another portion is fully integrated, and a third unit may be dissolved.

Therefore, the first goal of the ICO and IFT is to translate the deal strategy into the desired targets for the “To-Be” organization. This will obviously be an iterative process, since as the IFT learns more about the capabilities and liabilities of the target company, the strategy and goals may need revision. For example, discovery that a manufacturing plant has major unforeseen quality issues will dramatically affect the integration timeline and cost.

*Develop Team Charters.* The second major goal of the IFT is to undergo a chartering process whereby the team specifically defines what it is, and is not, responsible for. The metaphor here is one of a fly ball in baseball, where two outfielders either compete to catch the same ball, or worse, let it drop between them thinking the other was going to catch it. It is easy for teams, eager to get on with the “fun” part of integration, to skip this step. In our experience, this

inevitably leads to problems later. This is where Catenion consultants and the program manager assigned to the IFT can play an invaluable role, coaching the team through an effective chartering process. This is also the point at which the team receives critical “Dos and Don’ts” about how to interact with their counterparts in the target organization. This includes information on proper communication (more on this later), critical cultural differences, and legal requirements in effect until the deal closes.

*Define Timelines and Deliverables.* Once the team has translated the deal strategy into goals and has defined their area of responsibility, they can begin the process of developing detailed integration plans. These will obviously vary widely by functional area, but will include major integration milestones, synergy targets (if any), organizational changes, communication with regulatory agencies, or clinical trial activity.

The role of the ICO at this point is to roll up all of the functional plans so that a coherent overall integration plan is developed. The ICO is also responsible for communicating and aligning team interdependencies. For example, a potential layoff in a business unit will require tight alignment between the functional area, HR and the communication teams.

*Portfolio Integration.* One of the most common, and often contentious, undertakings in integration is the evaluation of the two company portfolios with the goal of creating a combined portfolio. The tension in this situation is understand-

able. The target company will feel an emotional attachment to their projects, and may view survival of their portfolio as synonymous with job security. The acquiring company is frequently under significant cost pressures, and may be reluctant to take on new resource demands.

In our experience functioning as a third-party facilitator, using a fact-based and objective portfolio review process, we can help defuse the tension and help create an optimized portfolio. Catenion provides a proprietary, proven and best-in-class suite of five tools, processes and methods to assess and optimize individual projects and entire portfolios:

- **R&D Risk Assessment:** An expert system with more than 600 criteria measuring a project's risk level against industry average, differentiated by drug format (small molecules, monoclonal antibodies, recombinant proteins, etc) and stage of the R&D process. Based on the input of hundreds of industry experts and used to evaluate more than 1000 projects to date.
- **Option Space Mapping:** A systematic approach to map out the development options of an early project based on hard biological, chemical, and pre-clinical data regarding target and own compound, competitor compounds, market situation and the project's position in pipeline.
- **Innovativeness Screening:** A method developed to assess market attractiveness for early compounds

before proof of concept and used instead of more elaborate forecasting methods. Key dimensions are novelty, usefulness, theoretical market potential and exploitability by company.

- **Competitiveness Modelling:** An elaborate forecasting tool developed by Catenion for post-proof-of-concept compounds. The tool permits rating of product features against those of current and expected competitors, and forecasts the whole market, rather than just one company's compound.
- **Value-at-Risk Monte Carlo Simulation:** Portfolio values based on risk-adjusted, expected values are not risk-free, as every practitioner knows. Our approach shows the level of unacceptable risk (i.e. the likelihood of not reaching a minimum level of return) a company incurs with its portfolio and how to reduce this risk by adjusting the portfolio.

Together, our approach results in a combined portfolio that is aligned with the deal structure and the needs of the new organization (Figure 2, Page 8).

*Iterate and Communicate.* At this point, with all teams striving towards their goals according to their IFT plan, the process becomes one of ensuring alignment and communication. When problems or issues arise that are beyond the scope of the IFT, the ICO is available to bring these issue to the executive team for resolution.

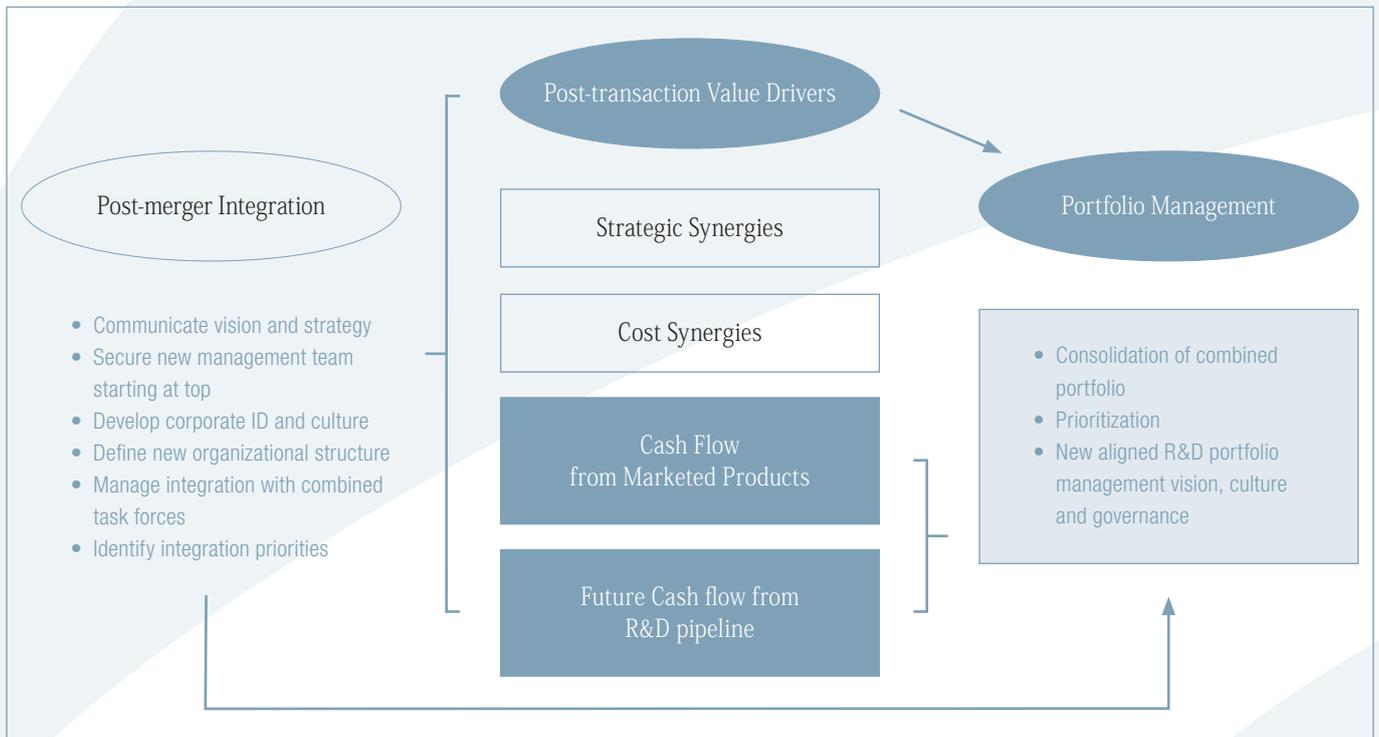


Figure 2: Catenation post-transaction expertise. Portfolio management is one of the top priorities of PMI since suboptimal approaches destroy value

## Teams that are Always Critical

In addition to the critical role of the portfolio review team described above, there are three other teams that are always critical, no matter the integration. These are Communications, Human Resources and Information Technology.

*What's Going On?* It is important to realize that being acquired is usually an intensely upsetting event for the target company. Different organizations, and even different pockets within the

same organization can have wildly different reactions, depending on their history, cultural make-up, and perceived fate. The target organization is always hungry for information.

However, the acquiring organization is often prevented from being able to fully disclose their intentions. This is due to the fact that until the deal legally closes, the two organizations must operate independently. Equally important, the acquiring

company must operate under a principle of “Do No Harm.” This means that if the deal eventually falls apart (*e.g.* due to anti-trust regulations), the target company must be able to resume normal business operations. If, for example, the acquiring company announced that a certain business portion was expected to be dissolved, those personnel might leave for other jobs. If the deal did not close, the target company could claim significant damage to their business had been done.

This highlights the importance of effective communication. Often, in the early stages of the integration, the most important role of the communication team is to educate the IFT members of what *not* to say with regards to compensation, layoffs, titles, and organizational issues. Later on, as more information is able to be disclosed, the timing, content, and forum of these disclosures is critical. The following are some key points regarding communication:

- It is better to say nothing than to say something inaccurate. Credibility erodes incredibly quickly when inaccurate information is given.
- If you cannot communicate *what* is going to happen, then communicate *when* you will be able to. Be careful giving a date, you must stick to it.
- Cultural differences and company slang can easily distort messages. Ill-considered jokes or “off-the-cuff” remarks can do great damage.
- Redundant messaging is better than radio silence, within reason.
- All communication will reverberate through the organization. If a business unit gets a communication specific for them, count on the entire organization hearing it.

*What’s Going to Happen to Me?* Closely following the shock of an acquisition is the inevitable questioning about what this may mean to each individual. Questions regarding title, potential relocation, compensation, and reporting structure ricochet around the organization. As discussed above, much of this cannot be communicated directly prior to the close. This often means the HR team works feverishly in the background to prepare for business unit integrations, reorganizations or layoffs. The goal of the team should be to communicate full, accurate information on organizational structure, compensation, or severance as soon as possible after the deal closes. While some employees may be disappointed with the eventual decisions of the acquiring company, they should always feel that they have been treated as respectfully as possible.

*Can I Get My Work Done?* As employees and business units feel more informed and comfortable with the integration process, the question becomes one of practical considerations of doing their jobs. Once the deal closes, it is essential that required information technology be in place. The specifics of this are obviously dependent on the model of integration (*e.g.* full or independent). For example, a new research unit may require access to specialized databases. Failure to provide this connectivity immediately after close can create intense frustration and delay effective integration.

## The Catenion Difference

By deploying a highly effective and experienced Catenion team with a small footprint to your organization, and in partnership with your executive leadership and functional expertise, we can create a high-performing internal team that can effectively derive value from the deal.



## Catenion: Your Partners for Pharmaceutical Strategy and Innovation

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Catenion is a management consulting firm devoted to helping pharmaceutical and medical products companies significantly increase the returns on their R&D and Marketing investments by creating more innovative and effective strategies and organizations.





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