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Bad deal: *The dismal record of M&As shows acquirers have wiped more value off their market cap through failures in due diligence during the negotiation process than through lapses in any other part of the deal. In the case of the merger between AOL and Time Warner, some US$200 billion in shareholder value had vanished*

M&As: Are you a value-creation negotiator?

Effective negotiation is about skilfully creating sustainable and mutual value for all parties

By **MICHAEL BENOLIEL**

IT was in 1716 that French diplomat Francois de Callieres wrote the world's first book on negotiation, on the manners of negotiating with princes. It was in this book that he famously observed that the fate of the greatest states depends almost entirely on the good or bad conduct of their negotiators.

It appears that his comments have stood the test of time, for even in today's increasingly competitive global economy, the fate of an organisation depends largely on the skill and conduct of its negotiators.

To appreciate the critical role of skilled negotiators, one has to look no further than at the dismal record of mergers and acquisitions (M&As), especially recent high-profile deals. Acquirers have wiped more value off their market capitalisation through failures in due diligence during the negotiation process than through lapses in any other part of the deal.

For example, despite the grand promises of the "transformative" mega merger between AOL (previously known as America Online) and Time Warner, some US$200 billion in shareholder value had vanished. Similarly, the US$5.8 billion acquisition of Rubbermaid by Newell was described by *BusinessWeek* as the "merger from hell" as it effectively robbed Newell's shareholders of 50 per cent of their investment, and Rubbermaid shareholders of a further 35 per cent.

After the acquisition, Newell's former chief executive officer (CEO) admitted that Newell had overpaid. In another transaction, Quaker Oats acquired Snapple for US$1.7 billion, which some industry analysts said was as much as US$1 billion too much. Twenty-eight months later, Quaker Oats sold Snapple to Triarc Companies for less than 20 per cent of what it had paid.

Are these examples outliers? Perhaps not. A study by KPMG International in 1999 looked at shareholder returns on corporate mergers relative to the performance of other companies in the same industry one year after the announcement of the merger.

Using this commonly cited standard of success, it found that 83 per cent of mergers failed to unlock value.

While there are many reasons why M&As fail to unlock value, an analysis of these factors reveals that the most major mistakes are related to the negotiators' behaviour. These include: hubris; over-optimism; information availability bias; confirmatory bias; escalation of commitment; and "deal fever" – individuals produce many deals because they are evaluated on the basis of the number of the deals done and not on the basis of their intrinsic value.

Pressure tactic

In a recent survey, 250 global executives involved in M&As admitted that there were breakdowns in their due-diligence processes, and half of these individuals reported that this resulted in important issues not being detected.

Among the most common mistakes they reported was a failure to understand that the targeted companies had "perfumed" themselves for sale just before they were acquired. For example, in the acquisition of Rubbermaid by Newell, Rubbermaid used a classic time pressure tactic and gave Newell only three weeks to perform its due diligence. Instead of negotiating a more reasonable time period, Newell accepted the short deadline and expedited the process.

It was only much later that Newell discovered that Rubbermaid "perfumed" its balance sheet and inflated its worth before closing the deal by stuffing the distribution channels with heavy promotions and deep discounts.

But not all companies perform as dramatically poorly as AOL and Time Warner, Newell and Rubbermaid, or Quaker Oats and Snapple. What distinguishes the more successful firms from the less successful ones is that they have, what I call, a clear and disciplined negotiation thesis.

Need for precision

While the concept of having a disciplined negotiation thesis is straightforward, apparently, in the world of deal-making, it is not. "You'd be surprised how many negotiators don't know what they want with the kind of precision that a negotiation demands," former US trade representative Charlene Barshefsky told this writer. She added: "Consequently, they end up with either no deals or bad deals."

This was the case of Robert Campeau, a Canadian businessman who sought to acquire Federated Department Stores. After initiating a hostile takeover, the bidding war against Macy's, another interested acquirer, escalated.

In his last "push" to win the bidding war, Mr Campeau topped Macy's already high offer by roughly US$500 million. Two years after the takeover, Mr Campeau declared bankruptcy. He could not walk away.

Successful deal makers, in contrast, know precisely what their objectives are – the "must-have" (deal breakers) and the "like to have", and are disciplined in their quest to create sustainable value.

They, like former Kellogg CEO Carlos Gutierrez, condition themselves to walk away from the table if and when it is apparent that their objectives are not going to be met. When Mr Gutierrez negotiated the acquisition of Keebler, a deal which he said he "desperately wanted", he said: "I conditioned myself mentally that I might not get it and that helped me to stand firm on my price."

Deal-making is not about getting the deals and signing the contracts. Effective negotiation ultimately is about skilfully creating sustainable and mutual value for all the negotiating parties. Among the serially successful deal makers are Bain & Company, a top-tier private equity firm; Cinven, a leading European private equity firm; and Nestle, a Swiss conglomerate and textbook acquirer.

These companies know how to avoid the traps of deal-making, especially due diligence, and how to create value through superior negotiation capabilities.

In this article, I stressed the critical, and yet unrecognised, value of negotiation as a core organisational capability and core professional competency. In part two of this article, I will highlight why many negotiators fail in the most critical task of negotiation – performing effective due diligence.

The writer is an associate professor of organisational behaviour and human resources practice at Singapore Management University and teaches negotiation. He is the author, co-author and editor of several negotiation books, including his newly published 'Negotiation Excellence – Successful Deal Making'