APRIL 2024

Revenue synergies in Mergers & Acquisitions (M&A)

Whitepaper

WWW.BRIGHTWOLVES.COM

REVENUE SYNERGIES IN M&A

INTRODUCTION

Synergies have been used to justify some of the worst and best M&A transactions in history. M&A is supposed to be about value creation, and for many deals, synergies are cited as the primary means to that end. In contrast, Aswath Damodaran famously quoted that “If you look at the collective evidence across acquisitions, this is the most value destructive action a company can take”. Damodaran’s statement is supported by academic research as it repeatedly confirmed that about two-thirds of all mergers and acquisitions among public companies destroy value for the acquirer, at least in the short term. How come that so many M&A transactions are not achieving their main objective, namely, to create additional value?

SYNERGIES IN M&A

Before tackling this problem, let’s first take a glance at synergies and their sources. When synergies are realized after an M&A transaction, the value of the newly merged firm becomes higher than the summed pre-merger valuation of the individual companies. These synergies may arise for various reasons and origins, including:

- Cost synergies
- Revenue synergies
- Financial synergies

However, there is more to value creation than simply identifying synergies and executing strategies to realize those. Value-creating acquirers not only vary from others in their synergy realization capabilities but also in the way how they manage M&A transactions pre-, during and after-closing:

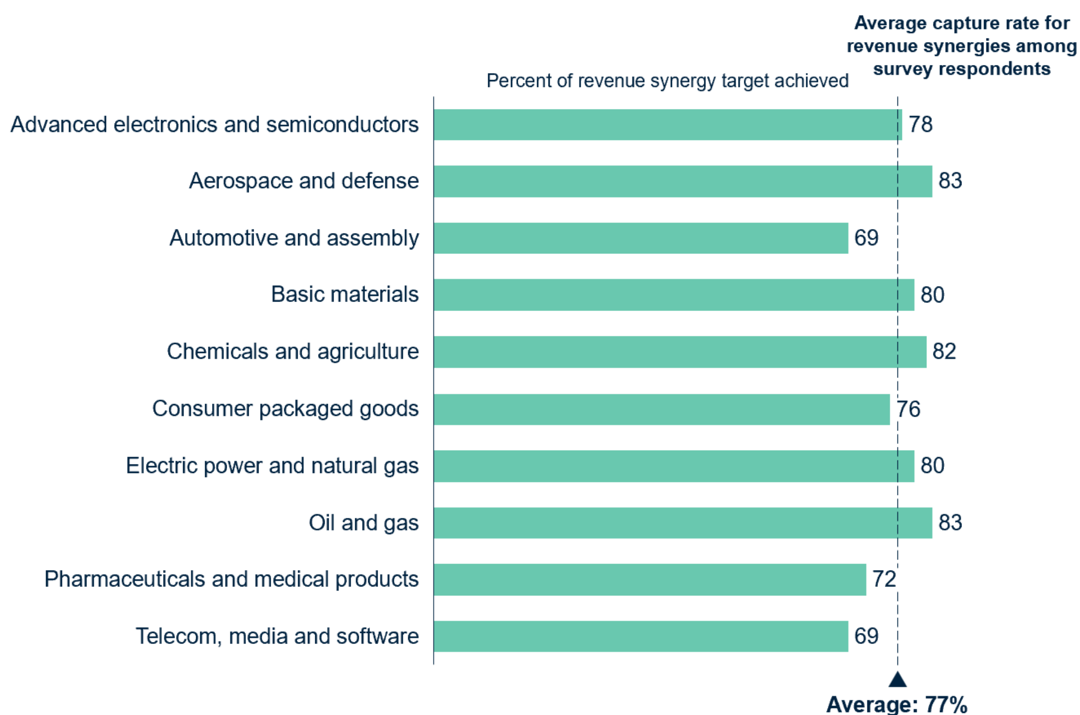
- They limit the “premium” they pay to the seller on the basis of a rigorous analysis of the synergies they expect to achieve;
- They communicate candidly about their synergy expectations, publicly committing to synergy targets when they announce the deal;
- They execute punctilious Post Merger Integration (PMI) to fully and rapidly capture the synergies. They also communicate transparently about their progress.

The M&A landscape is characterized by a huge spread in the Return on Invest (RoI) different actors achieve. This variation in ROI can be largely explained by both the success of those actors in realizing synergies and their approach to managing M&A transactions. In this paper, we will focus on the realization of synergies and more specifically revenue synergies.

REVENUE SYNERGIES IN M&A

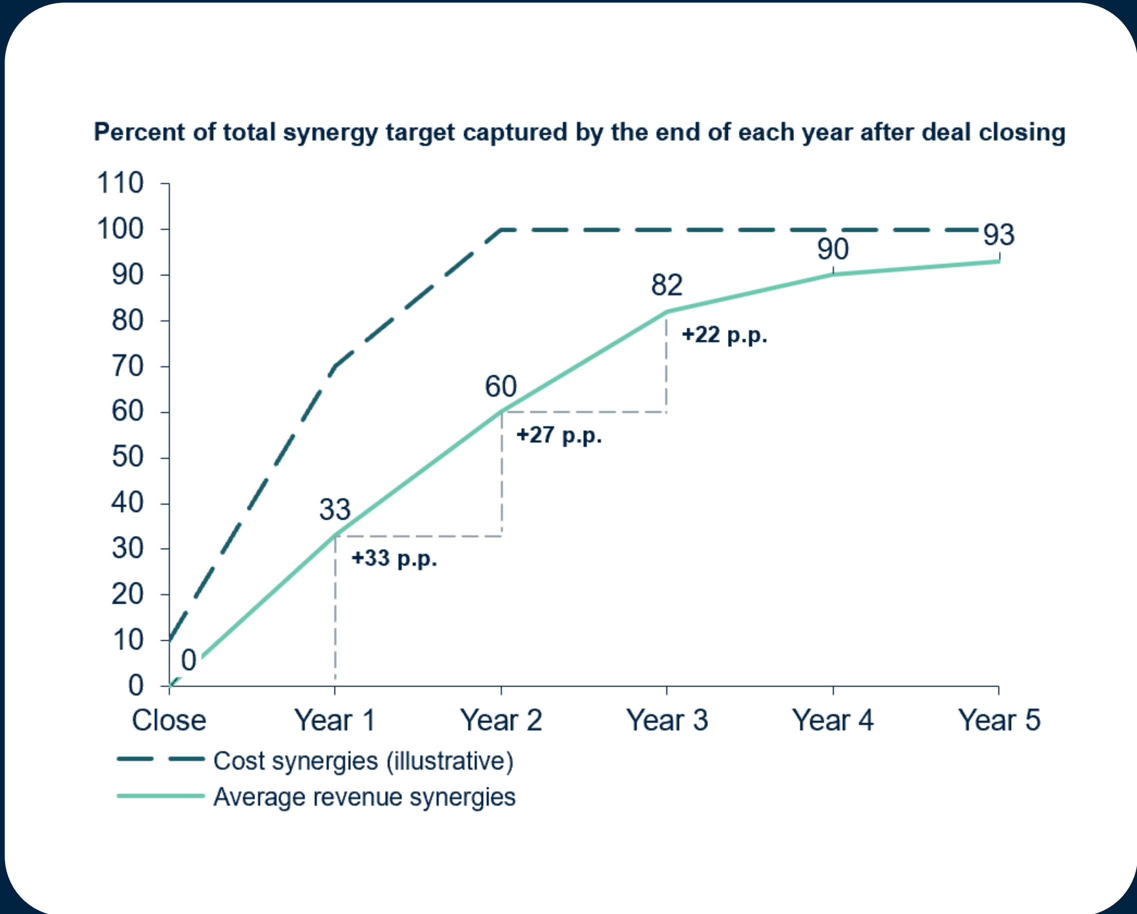
Most acquirers who seek to create value by capturing synergies are mainly focused on cost synergies. However, revenue synergies are becoming critical for deals in a high-valuation M&A environment as we've experienced over the last decade. Unlike cost synergies, revenue synergies are more difficult to obtain and often go unrealized.

The intense M&A activity over the last years has led to unprecedented competition for deals, increasing the importance of revenue synergies in the acquisition rationale. Although its growing importance, revenue synergies are proving to remain elusive to capture. Different studies conclude that less than a quarter of acquirers' report achieving 80% of their revenue synergy targets. In 2018, 200 seasoned M&A executives from 10 different industries were surveyed. Remarkably, the majority reported that their company had fallen short on its revenue synergy aspirations. On average, only 77% of their revenue synergy targets were realized.



Graph 1: Percent of revenue synergy target achieved across 10 industries

Even for the "leaders" who managed to capture 100% of their targets, the process typically took considerably longer compared to the realization of the cost synergies. On average, it took a company ~2 years to realize its full cost synergies potential compared to ~5 years to achieve its revenue synergy targets.



Graph 2: Percent of total synergy target captured by the end of each year after deal closing

So how come that so many M&A transactions fall short to realise their revenue synergies?

Compared to the traditional approach for cost synergies, buyers often limit themselves to a bird's eyes view on revenue synergies during diligence and do not keep good track of the progress after closing the deal. Additionally, revenue synergies are difficult to size and to realize. Within academic research, there is consensus that revenue synergies are a fundamental reason for unsuccessful deals.

So how can acquirers manage to realize their revenue targets, what sets the "leaders" apart from the "laggards"?

To create value in today's high-valuations M&A market, acquirers are forced into a more rigorous approach to estimate and commit to top-line growth. Leaders are:

- Incorporating a proprietary and data-driven approach during diligence to size and realize synergy revenues;
- Leveraging the pre-close period to prepare the acquisition target's product roadmap and to adjust its sales model in order to accomplish revenue synergies as of day one;
- Tracking the revenue synergies once the deal is completed and updating their revenue synergies playbook with each deal.

BrightWolves' has developed a 4-step approach to support companies in unlocking the revenue synergy potential and become leaders in today's M&A market.

Step 1: Plan the work

Best-in-class acquirers build a target list from an outside-in perspective years ahead of live deals. When performing diligence on a specific target company, extensive research is performed to map customers, identify potential new products, and evaluate customer needs. A crucial step in this diligence is to conduct a data-driven sales planning based on the information provided by the seller in the clean room. In addition, it is vital to include the voice-of-the-customer in each diligence by means of in-depth customer interviews. These customer interviews in combination with a review on win-loss records from the acquisition target generates insights for potential product bundles and are the foundation of the product roadmap.

Step 2: Define the combined customer value proposition

A customer-centric approach is critical when pursuing growth-oriented M&A deals. Acquirers should test existing and new combined product offerings during diligence to uncover value creation opportunities which otherwise would go overlooked or deferred. A detailed customer segmentation should also be designed during the pre-close period to tailor the anticipated combined value proportion on the specific needs of each identified customer segment. This approach provides the opportunity to offer a combined value proposition from which the customers will benefit as of day one. Before closing the deal, the acquirer should finish its long-term roadmap for product integration, cross-selling activities, and joint value proposition. The focus of this roadmap should be on the integration of products, offerings and features which will be of value for the customers.

Step 3: Enable the sales team to win from day one

Acquirers should strive to generate momentum for revenue synergies from day one. To achieve this, they should capitalize on the pre-closing period to identify initiatives that can be launched within the first 90 days post-closing and incorporate them into the roadmap. A common pitfall for acquirers is waiting for long-term product and sales transformations to commence, delaying the leveraging of momentum immediately after the deal closes and overlooking opportunities for immediate revenue synergies. Acquirers can mitigate this risk by aligning their long-term vision with short-term actions, leveraging existing products, sales teams, and structures to capture immediate upside.

Step 4: update your revenue synergies playbook

The first three steps outlined above offer companies a data-driven approach to identifying and capturing revenue synergies from their acquisitions. However, an additional proprietary angle can be incorporated by tracking synergies across all deals executed by the M&A team. Acquirers can extract valuable insights from each deal, discerning which revenue sources materialized and which did not. Over time, this accumulation of data enables the determination of critical success factors and the identification of key performance indicators to monitor. Through continuous revenue tracking, acquirers enhance their capabilities in realizing revenue synergies. This, in turn, enables the M&A team to focus on pertinent data, improve diligence in subsequent deals, and position the company for greater success in future acquisitions.

How can BrightWolves support your M&A transactions?

Over the last five years, BrightWolves has partnered with investors in private equity and venture capital, offering support in more than 70 deals. This extensive experience has allowed BrightWolves to cultivate expertise across a diverse range of sectors, solidifying its position as a prominent player in the M&A arena. BrightWolves offers a broad suite of services to facilitate M&A transactions, spanning pre-, during, and post-closing phases. Whether you require assistance in realizing synergies, particularly revenue synergies, or in navigating the complexities of transactions to establish leadership in the M&A landscape, our team of experts stands ready to assist you.

For further inquiries, please don't hesitate to contact our specialists:

Miguel Vandamme, Joris Vanthienen, and Marnik Willems

REFERENCES

(1) McKinsey. (2018). Seven rules to crack the code on revenue synergies in M&A. Retrieved from: https://www.mckinsey.com/capabilities/growth-marketing-and-sales/our-insights/seven-rules-to-crack-the-code-on-revenue-synergies-in-ma

(2) Corporate Finance Institute. What are Synergies? Revenue, Cost, and Financial Synergies Explained. Retrieved from: https://corporatefinanceinstitute.com/resources/valuation/types-of-synergies/

(3) Deloitte. Revenue synergies in acquisitions. Retrieved from: https://www2.deloitte.com/us/en/pages/mergers-and-acquisitions/articles/acquisition-synergies-revenue-examples-survey-results.html

(4) Bain & Company. (2022). Bringing Science to the Art of Revenue Synergies. Retrieved from: https://www.bain.com/insights/revenue-synergies-m-and-a-report-2022/

(5) Harvard Business Review. (2021). The Sales Playbook of Successful B2B Teams. Retrieved from: https://hbr.org/2021/08/the-sales-playbook-of-successful-b2b-teams

(6) Boston Consulting Group. (2013). How Successful M&A Deals Split the Synergies. Retrieved from: https://www.bcg.com/publications/2013/mergers-acquisitions-postmerger-integration-divide-conquer-deals-split-synergies.

(7) Boston Consulting Group. (2016). The Real Deal on M&A, Synergies, and Value. Retrieved from: https://www.bcg.com/publications/2016/merger-acquisitions-corporate-finance-real-deal-m-a-synergies-value

(8) Institute for Mergers, Acquisitions & Alliances. M&A statistics. Retrieved from: M&A Statistics: Transactions and Activity by year. M&A Trends | IMAA (imaa-institute.org)

BRIGHTWOLVES