



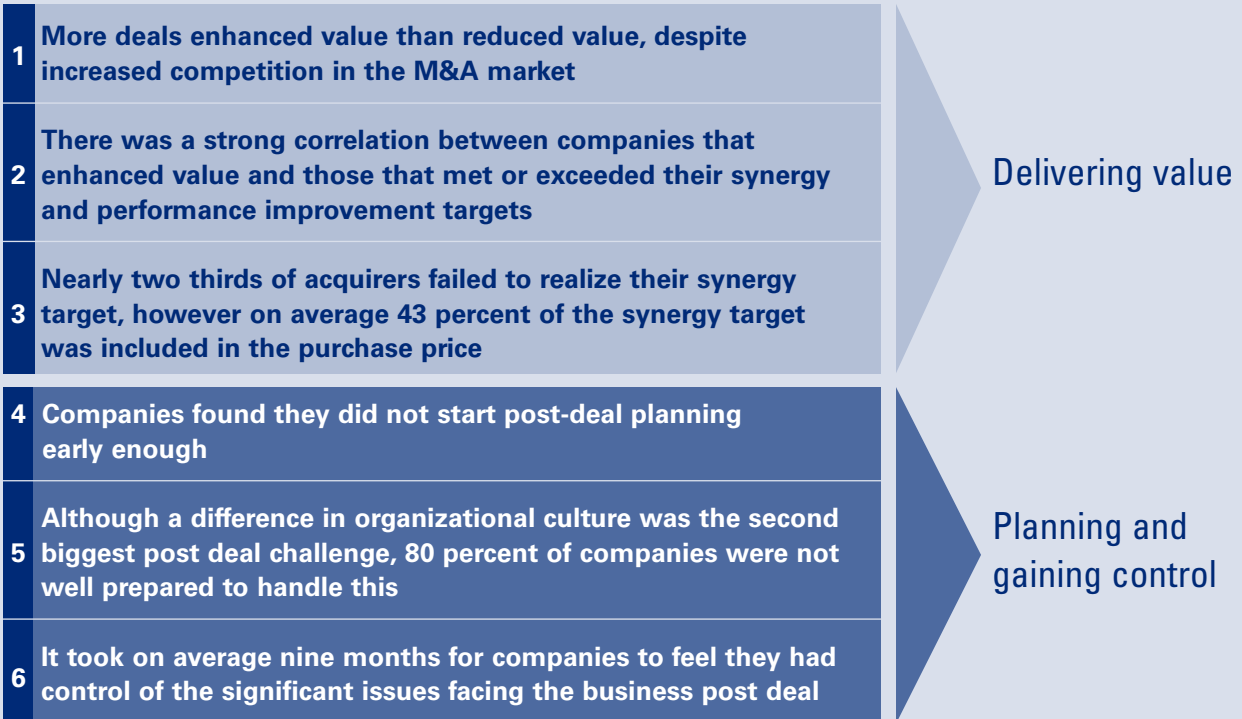
TRANSACTION SERVICES

The Morning After

Driving for post deal success

ADVISORY

Six key findings from our research



Introduction

Many CEOs and CFOs may be familiar with that 'Morning After' feeling when the intensity of the deal negotiations are finally behind them. Rather than relief and celebration, there is a realization of the enormity of the task ahead, and pressing questions can include:

What have I bought?

How do I deliver the value paid for?

The deal environment has changed significantly in recent years. A greater number of acquisitions are now subject to an auction process. With a more competitive market, higher premiums are being paid and trade buyers may often lose out to Private Equity houses who now account for an increasing proportion of acquisitions. At the same time, the competitive tension of an auction process can limit the amount of information which is available to acquirers before close. This creates additional challenges for CEOs and CFOs in the pre-close period, with a knock-on impact post completion.

Simultaneously, the market continues to professionalize, on both the buy-side and the sell-side and acquirers appear to be undertaking much broader based due diligence than in the past and thinking earlier about their post deal plans.

This most recent KPMG's Transaction Services practice global M&A survey, sets out to understand what acquirers are doing to enhance value from their acquisitions and what challenges they face in taking control of the target business. The results show that fewer deals reduce value than enhance value, despite increased competition in the M&A market, with 43 percent showing value neutral. We also find some interesting distinctions between the approaches of European acquirers, who appear to be more successful compared with those in the Americas and Asia.

For the first time, Private Equity houses have been invited to participate in the survey as well as corporations and the findings highlight some differences in approach to the pre and post-close periods.

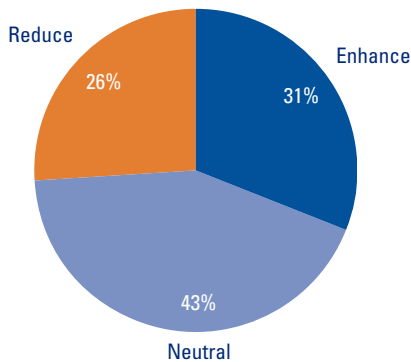
I hope you will find these insights as thought-provoking as I did.

Gopal Ramanathan
Chairman, Global Transaction Services
KPMG in the Netherlands

Delivering value

1 More deals enhanced value than reduced value, despite increased competition in the M&A market

Have deals enhanced value?



Calculated based on KPMG's objective assessment

Base: 90 percent of corporations interviewed
Source: KPMG International

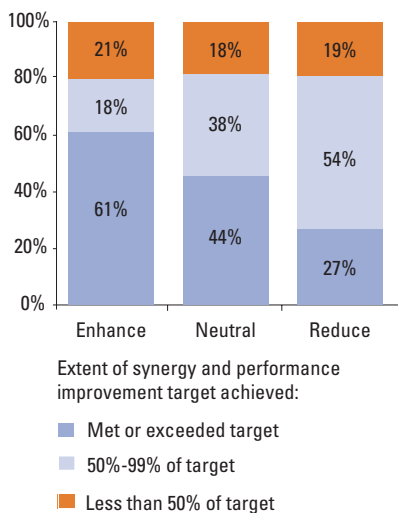
Over two thirds of deals failed to enhance value with 43 percent being value neutral. This suggests that companies are using acquisitions to hold their competitive position. This may also be indicative of a shift in power from the buyer to the seller through increased use of auctions and professionalization of the sell side process.

Nearly half of the corporate serial acquirers and 85 percent of the Private Equity houses interviewed agreed that the pressure to deliver the value identified pre deal is now greater than before.

The perception gap is wide - 93 percent of companies interviewed believed that their deal enhanced value, and over a third said that they would not do anything differently on their next deal. However KPMG's objective assessment of whether deals enhanced or reduced value, showed that only 31 percent of these deals enhanced value.

This suggests that companies may not yet be prepared to make an honest assessment of the success or otherwise of their deals in order to avoid making the same mistakes on future deals.

Value enhancement vs achievement of synergy and performance improvement targets



Base: 90 percent of corporations interviewed
Source: KPMG International

2 There was a strong correlation between companies that enhanced value and those that met or exceeded their synergy and performance improvement targets

Nearly two thirds of companies whose deal enhanced value met or exceeded their internal synergy and performance improvement target. Conversely, 73 percent of companies whose deal reduced value, failed to meet their synergy and performance improvement target.

Of those companies who met or exceeded their targets, 90 percent set out to exceed their target.

This helps to support KPMG's experience that synergies do not always materialize where expected. And that where companies just focus on delivering the cost synergies they fail to capture the full value of the deal, which would include revenue synergies.

3 Nearly two thirds of acquirers failed to realize their synergy target, however on average 43 percent of the synergy target was included in the purchase price

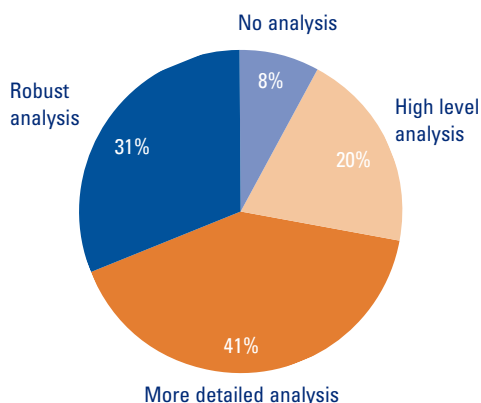
A common assertion in the past was that ‘you don’t pay for synergies’. This survey shows that, on average, 43 percent of the synergy target was included in the purchase price.

The bigger the target (relative to the buyer), the higher the percentage of the synergy target included in the purchase price: the average percentage increased significantly when the deal involved the entire acquiring organization versus those affecting just a business unit.

In spite of this, less than one third of companies said they had performed robust synergy analysis prior to completion. This contrasts with the approach of Private Equity houses in relation to the standalone acquisition, where not only did nearly two thirds of houses undertake robust performance improvement analysis but they also, on average, included a smaller percentage of the expected target in the purchase price.

The survey shows that buyers are having to pay for expected benefits in order to be competitive in the M&A market. Given the trend for competitive auctions, companies may need to take more seriously the ‘in-deal’ synergy analysis in order to reduce the risk of paying for an unrealistic target in the price.

Level of synergy analysis undertaken pre completion



Base: 49 percent of corporations interviewed
Source: KPMG International

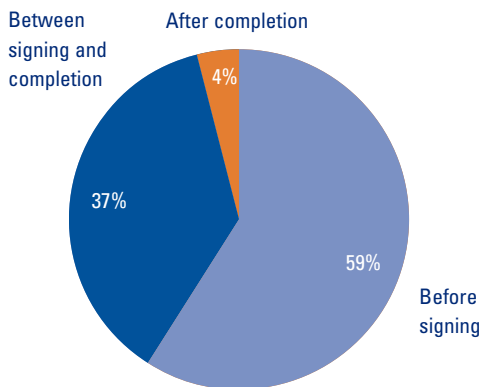
Planning and gaining control

4 Companies found they did not start post-deal planning early enough

In the survey, 95 percent of Private Equity houses and 59 percent of companies had started planning for the post deal period prior to signing the deal: of these approximately 90 percent said that they had developed a clear post deal strategy prior to completion.

However, of the top three actions companies would adopt on their next deal, earlier planning was the most commonly quoted.

When did planning for the post deal period start?



Base: 100 percent of corporations interviewed
Source: KPMG International

The advantages of early planning cited by respondents included:

- 1 Limiting the risk of losing customers
- 2 Bringing forward synergy delivery
- 3 Avoiding a communication vacuum, where rumors and misinformation prevail

A further benefit of early planning is the identification of potential deal breakers – 63 percent of companies and 90 percent of Private Equity houses interviewed said they had walked away from deals in the past due to anticipated post deal difficulties.

One third of respondents stated that they were restricted in the amount of pre-deal due diligence they could carry out; this can affect a company's ability to fully understand the extent of the issues / challenges to be faced post deal.

Nearly two thirds of companies had experienced a regulatory period of, on average, just over three months. KPMG's experience is that this can be a difficult period for both acquirer and acquiree, particularly given the inherent uncertainty on the decision and its timing. Some companies had used this pre-close time for planning and half of companies had been able to launch their post deal management work prior to completion, the main benefit of which was to accelerate the work post completion.

- 5 Although a difference in organizational culture was the second biggest post deal challenge, 80 percent of companies were not well prepared to handle this

The top three post deal challenges cited by respondents were:

- 1 Complex integration of two businesses
- 2 Dealing with different organizational cultures
- 3 Difficulty in integrating IT and reporting systems

What would companies do differently next time?

1 Plan earlier for post deal management

2 Conduct additional cultural due diligence

3 Appoint dedicated post deal management team

Top three actions quoted
Base: 100 percent of corporations interviewed
Source: KPMG International

Approximately half of respondents felt that they had been well prepared for the complex integration of the existing and acquired businesses and the integration of the IT and reporting systems but only one in five had been well prepared to handle the cultural differences.

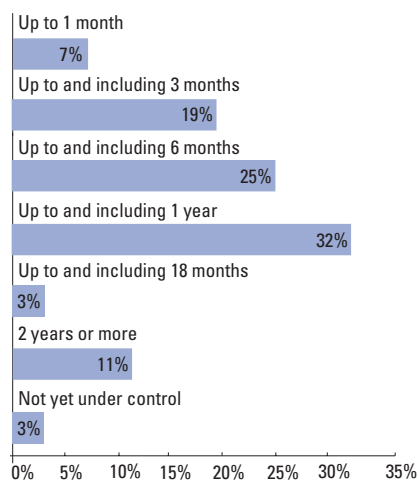
Two thirds of companies had not placed a great deal of emphasis on addressing people and cultural issues in planning for the post deal period and only 20 percent said that the people and cultural issues faced were less significant than originally anticipated.

The top three actions that people would do on their next deal were to plan earlier, perform additional cultural due diligence, and set up a dedicated team to handle the post deal work.

These results show that themes highlighted in previous KPMG's Transaction Services M&A surveys remain very relevant. Once again, companies recognize the importance of early planning for the post deal period and being ready to handle 'softer' aspects.

6 It took on average nine months for companies to feel they had control of the significant issues facing the business post deal

Time taken to get control of the key issues post deal



Base: 100 percent of corporations interviewed
Source: KPMG International

One third of companies said that it had taken longer to get control than originally anticipated, irrespective of whether the buyer was an experienced serial acquirer or not. More than 10 percent of the companies took over two years before they felt they had got control!

Three quarters of the companies who succeeded in taking control of the business within their anticipated timeframe prioritized two types of activity as important in the first month:

- 1 Gaining sufficient understanding of and confidence in the finances and reporting systems to be able to actively manage the business and meet reporting deadlines both internally and externally
- 2 Understanding and overcoming the cultural differences between the two companies

Changing accounting standards and regulatory requirements have increased the pressure on finance teams to fully understand the target company's financials and controls. For example, under IFRS, there is a requirement to align accounting policies, disclose material transactions by the year end and fair value intangible assets for subsidiaries. In addition, there is need for greater disclosure regarding internal risk management controls.

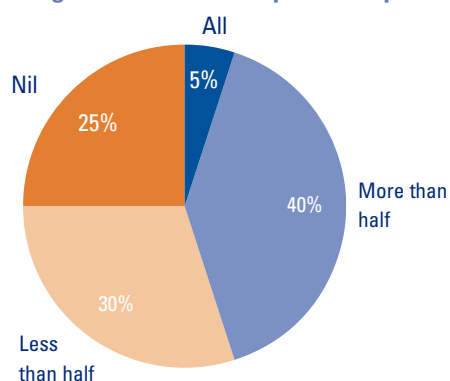
Private Equity approach

What difference in approach does this research show between Private Equity houses and corporations?

The findings from Private Equity houses are broadly in line with results from corporations. There were two notable differences in relation to pre deal work:

- 1 All Private Equity houses surveyed had started post deal planning prior to completion and in fact 95 percent of them had started prior to signing, compared with 59 percent of corporations. This is a clear signal of the importance Private Equity houses place on post deal issues. Not only does this effort mean they can “hit the ground running”, it also enables them to spot potential deal breakers earlier. As the survey has shown, 90 percent of Private Equity houses said they had walked away from a deal in the past because of post deal issues, compared with 63 percent of corporations.
- 2 Private Equity houses were much more likely to have conducted robust analysis pre-completion related to their performance improvement plans than corporations in relation to synergies. They tended to include a smaller percentage of their expected performance improvement targets into the purchase price, indeed one in four Private Equity houses said they had not included any of the target in the price.

Level of performance improvement target included in the purchase price



Base: 100 percent of Private Equity houses
Source: KPMG International

In KPMG’s experience, Private Equity backed management teams have a hunger for the deal and may be more aggressive about the performance improvement potential. They are more likely to be involved during the deal and tend to conduct robust evaluation of the post deal plans and performance improvement potential so they have confidence when they bid. In contrast, managers of corporations, who are conscious that any synergy number will be bedded into their budget, have a tendency to be more conservative.

Private Equity houses said their main post deal challenge related to the retention and selection of the management team. They also focused to a greater extent than corporations on day-to-day management rather than value delivery.

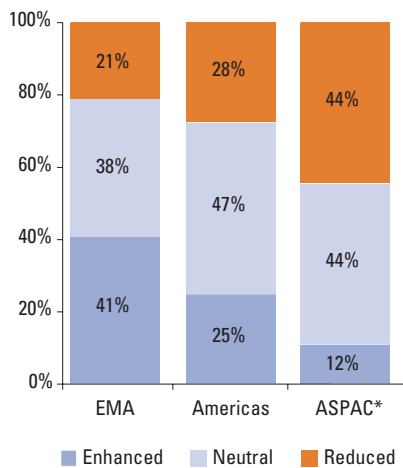
These results are not surprising when you consider that Private Equity houses have a greater focus on cash generation to alleviate debt pressure. On the other hand, corporations must focus on satisfying shareholders who will want to see progress in synergy delivery.

Geographical differences

What difference in approach does our research show between acquirers in different geographies?

A higher proportion of European, Middle East and Africa region (EMA) deals were value enhancing than deals in the Americas. There is a strong correlation in both geographies between value creation and those companies which met or exceed their synergy and performance improvement targets.

Value enhanced by geography



* The ASPAC corporation sample is too small for comparable analysis.

Base: 90 percent of corporations interviewed
Source: KPMG International

However, while nearly half the Americas companies achieved between 75 percent and 99 percent of their synergy and performance improvement targets, this does not appear to have translated into value enhancement.

A greater proportion of the Americas companies performed robust synergy analysis and on average included a smaller percentage of the synergies target in the purchase price than EMA companies, which one might expect to lead to enhanced value.

The main difference between Americas and EMA companies is in their focus on day-to-day management versus value delivery. While nearly a third of the Americas companies focused on delivering incremental value, only one in five EMA companies focused on this, rather they gave equal priority to value creation and day-to-day management. It could be concluded from this that real value is delivered when focus on incremental benefits is not at the expense of inherent value of the business acquired.

Two other key differences noted were that EMA companies commenced their planning earlier and were more likely to employ external assistance in the design and management of their post deal work.

Ten tips for acquirers

How can acquirers mitigate that 'Morning After' feeling?

The survey shows there are potential remedies in the pre-deal and in the post-deal space.

We have summarized these recommendations below:

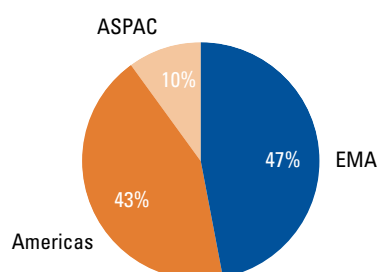
- 1** Perform robust analysis of synergy and performance targets. Be confident about what is achievable before including them in the purchase price
- 2** Identify and investigate post deal issues prior to completion – these issues could be deal breakers
- 3** Use the regulatory period - start post deal management work prior to completion
- 4** Set up a dedicated team to manage the post deal work
- 5** Obtain control over the finance and reporting systems as early as possible after close
- 6** Identify the cultural differences early and plan how to overcome them
- 7** Anticipate and plan for management and leadership issues early, then monitor them closely after completion
- 8** Balance focus on delivering incremental value with the need to keep an eye on the day-to-day business performance
- 9** Plan to exceed the original synergy and performance improvement targets
- 10** Track the value being delivered from the deal and honestly assess the success or otherwise of the post-deal work

Survey methodology

KPMG's Transaction Services extends its thanks to all the companies who have taken the time to participate in this survey.

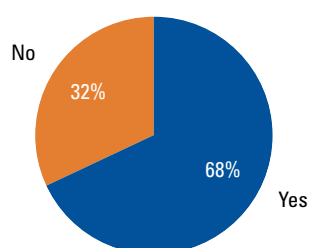
This is the fourth survey on major global M&A deals from KPMG's Transaction Services practice. Our objectives were to ascertain the proportion of deals that enhanced shareholder value and understand experiences and processes undertaken by corporations and Private Equity houses related to post-deal management.

Geography of corporate sample



Base: 100 percent of corporations interviewed
Source: KPMG International

Serial acquirers in the corporate sample



Base: 100 percent of corporations interviewed
Source: KPMG International

The fieldwork was conducted by MORI between August 2005 and October 2005 via telephone interviews. The 101 corporate participants were taken from a sample of global companies who had conducted deals worth over US\$100 million between 2002 and 2003. Twenty Private Equity houses agreed to participate and self-selected the deal they discussed from deals completed at least 12 months earlier. The quantitative fieldwork was supplemented by 10 qualitative interviews which have helped enrich our understanding of the quantitative findings.

Further research was conducted using share price information supplied by Datastream. Each deal was categorized as having enhanced, reduced or left unaffected shareholder value, according to an objective benchmark. For each deal, a relative measure of change in equity price was taken pre-deal and again one year later. This was then compared with the overall trend in the relevant industry segment.

To preserve the confidentiality and anonymity of survey respondents (and in accordance with standard market research guidelines) analysis of the survey findings was carried out by MORI and not by KPMG International or KPMG member firms.

Sector

| | |
|---------------------------------------------|------------|
| Industrial & Automotive | 34 percent |
| Infrastructure, Government & Healthcare | 25 percent |
| Financial Services | 19 percent |
| Information, Communications & Entertainment | 15 percent |
| Consumer Markets | 6 percent |
| Others | 1 percent |

KPMG's Transaction Services can provide M&A support through a transaction from pre-deal evaluation through to completion and post-deal integration or separation. We are part of a global network of over 2,200 transaction professionals focused on acquisitions, disposals, mergers, joint ventures, leveraged buyouts (LBOs) and Initial Public Offerings (IPOs), supported by the professional skills and experience of KPMG firms in nearly 150 countries. We are focused on value creation and helping our firms' clients, both corporations and Private Equity houses to deliver successful transactions.

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